

The Role of the Company at the Permission Stage in the Statutory Derivative Claim

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The role of the company in unfair prejudice petitions

Shareholders who are respondents to unfair prejudice petitions under s.994 of the Companies Act 2006 (“the CA 2006”), whether or not they are directors of the company, are not permitted to expend the company’s funds in defending the proceedings¹ and may be restrained from doing so by injunction.² This is because, as Hoffmann J. held in *Re Crossmore Electrical and Civil Engineering Ltd*³:

“The company is a nominal party to the [unfair prejudice petition], but in substance the dispute is between the two shareholders. It is a general principle of company law that the company’s money should not be expended on disputes between the shareholders: see *Pickering v Stevenson* (1872) LR 14 Eq 322.”

The improper use of the company’s resources on disputes between shareholders constitutes misfeasance on the part of the company’s directors, and may in and of itself constitute unfairly prejudicial conduct.⁴

Active participation by a company in an unfair prejudice petition is, however, not invariably improper, and in an appropriate case the company may apply to the court for authorisation to expend funds in the litigation. The principles were summarised by Lindsay J. in *Re a Company (No.001126 of 1992)* as follows⁵:

“Firstly, that there may be cases where a company’s active participation in or payment of its own costs in respect of active participation in [an unfair prejudice petition] as to its own affairs is ultra vires in the strict sense.

Secondly, leaving aside that possible class, there is no rule that necessarily and in all cases such active participation and such expenditure is improper.

¹ *Re Crossmore Electrical and Civil Engineering Ltd* [1989] B.C.L.C. 137 Ch D at 138; *Re a Company (No.005685 of 1988)* [1989] B.C.L.C. 424 Ch D; *Re Kenyon Swansea Ltd* [1987] B.C.L.C. 514 Ch D at 521; *Re a Company (No.004502 of 1988) Ex p. Johnson* [1992] B.C.L.C. 701 Ch D at 702–703; *Re Milgate Developments Ltd* [1993] B.C.L.C. 291 Ch D; *CAS (Nominees) Ltd v Nottingham Forest FC Plc* [2001] 1 All E.R. 954 Ch D at 956.

² *Re a Company (No.004502 of 1988) Ex p. Johnson* [1992] B.C.L.C. 701; *Re Milgate Developments Ltd* [1993] B.C.L.C. 291; *Arrow Trading & Investments Est 1920 v Edwardian Group Ltd* [2004] B.C.C. 955 Ch D.

³ [1989] B.C.L.C. 137 at 138e–138f.

⁴ *Re Hydrosan Ltd* [1991] B.C.L.C. 418 Ch D at 420.

⁵ [1994] 2 B.C.L.C. 146 at 155d–156c. In exceptional cases where the relief sought is purportedly for the benefit of the company, it may be appropriate for the company to take an active role in resisting a s.994 petition: *Re Chime Corp* [2004] 3 H.K.L.R.D. 922 at [53]–[55] (Lord Scott of Foscote). See too *Hawkes v Cuddy* [2007] EWHC 1789 (Ch); [2008] 1 B.C.L.C. 527 Ch D at [152], per H.H. Judge Havelock-Allan QC (sitting as a High Court Judge). Whilst the Court of Appeal ([2007] EWCA Civ 1789 (Ch); [2008] B.C.C. 125) reversed the judge’s decision in part, it did not cast any doubt on his treatment of this issue.

Thirdly, that the test of whether such participation and expenditure is proper is whether it is necessary or expedient in the interests of the company as a whole (to borrow from Harman J in *ex p Johnson*⁶).

Fourthly, that in considering that test the court's starting point is a sort of rebuttable distaste for such participation and expenditure, initial scepticism as to its necessity or expediency. The chorus of disapproval in the cases puts a heavy onus on a company which has actively participated or has so incurred costs to satisfy the court with evidence of the necessity or expedience in the particular case. What will be necessary to discharge that onus will obviously vary greatly from case to case.

Fifthly, if a company seeks approval by the court of such participation or expenditure *in advance* then, in the absence of the most compelling circumstances proven by cogent evidence, such advance approval is very unlikely.”

In view of the distaste shown by the courts for the expending of company monies on shareholders' disputes, there are only very limited respects in which it is ordinarily proper for the company to incur costs in relation to an unfair prejudice petition. These are, principally, in meeting its reasonable and proper costs of disclosure, or in attending at delivery of judgment (in a case where an order may be made that the company purchase the petitioner's shares or any other remedy may granted by the court which would affect the company).⁷ The principles applied by the court are the same whether the company seeks authorisation for the expenditure of costs in relation to an unfair prejudice petition or the petitioner seeks to restrain such expenditure, although in the latter case the petitioner is obliged to show in the first instance that the company is seeking to take part in the proceedings and that the purposes for which, or manner in which, it wishes to take part are not of such an exceptional nature as to justify a departure from the general rule.⁸

The statutory derivative claim

As in the case of unfair prejudice petitions, it will not normally be either necessary or appropriate for the company to take an active part in relation to a derivative claim brought under Ch.11 of the CA 2006.⁹ This is in accordance with the general principle outlined above that the company's money should not be expended on disputes between the shareholders. It also reflects the fact that the company is only a nominal defendant to the derivative claim. Whilst the company for the benefit of which a remedy is sought must be made a defendant to the derivative claim,¹⁰

⁶ *Re a Company (No.004502 of 1988) Ex p. Johnson* [1992] B.C.L.C. 701.

⁷ *Ex p. Johnson* [1992] B.C.L.C. 701. Where the s.994 petition is coupled with a petition for a just and equitable winding-up order, it would also be proper for the company to make an application for a validation order under s.127 of the Insolvency Act 1986.

⁸ *Arrow Trading & Investments Est 1920 v Edwardian Group Ltd* [2004] B.C.C. 955 at [10] (Sir Francis Ferris).

⁹ *Roberts v Gill & Co* [2008] EWCA Civ 803; [2009] 1 W.L.R. 531 at [29] (Arden L.J.).

¹⁰ CPR r.19.9(3). That rule “illustrates the general principle that in derivative actions the entity on whose behalf the claim is brought is a necessary party to the derivative claim”: *Roberts v Gill & Co* [2010] UKSC 22; [2010] 2 W.L.R. 1227 at [39], per Lord Collins. In obiter comments which did not reflect the views of the majority of the Supreme Court, Lord Clarke expressed the view, at [126]–[128], that CPR r.19.9(3) is subject to the overriding objective and that the court must have a discretion to postpone the joinder of the company in a particular case. He stated that there may be circumstances in a particular case which make it just to dispense with the necessity of joinder, suggesting that there may be no real point in joining the company if appropriate undertakings are given by the claimant

the rationale behind this requirement is that because the shareholder is suing to enforce the company's rights rather than his or her own it is necessary for the company to be a party in order to ensure both that it is bound by the judgment (thereby preventing it from bringing a subsequent action for the same relief) and that it receives any money recovered or the benefit of any other relief granted in the action.¹¹ Although the company is made a defendant, no specific relief is claimed against it.¹² The general rule has been summarised as follows¹³:

“The basic principle cannot be in doubt. It is that companies' money can only properly be expended for companies' purposes. It cannot be expended for the personal purposes of directors or of shareholders ... Although that rule is expressed in the context of [s.994] petitions, it may also be found expressed in relation to derivative actions ...”

Nevertheless, as explained below, there are circumstances, and stages in the litigation process, in which it is suggested that it may be appropriate for the company to be actively involved in a derivative claim and to incur costs in so doing.

The application for permission to continue the derivative claim

After the claim form is issued, the derivative claimant must file an application under CPR Pt 23 for permission to continue the claim,¹⁴ together with the written evidence on which he or she relies in support of the permission application.¹⁵ The claimant must not make the company a respondent to the permission application.¹⁶

The CA 2006 provides for a two-stage procedure for consideration by the court of the claimant's permission to continue a derivative claim. The first stage was not recommended by the Law Commission,¹⁷ but was added to the CA 2006 at a late stage in the House of Lords,¹⁸ with a view to enabling the court to make a speedy decision to dismiss the claim. Whilst the prescribed two-stage procedure has been followed in some cases,¹⁹ on several occasions it has not. Several derivative claimants have simply issued and served an application for permission, to which the defendants to the claim have been made respondents, thereby by-passing the first stage entirely. In such cases, in order to avoid unnecessary delay and cost,

to hold any moneys recovered for its benefit, especially if it consents, and noting the general principle that no action should fail for non-joinder of a party. It is far from clear, with respect, that the views which Lord Clarke expressed are correct. Certainly, it would be a brave derivative claimant who, relying on Lord Clarke's remarks, chose not to join the company as a defendant to the claim. It is difficult to envisage circumstances where a derivative claimant would have a sufficiently compelling reason to take the risk of adopting that course.

¹¹ *Spokes v Grosvenor Hotel Co Ltd* [1897] 2 Q.B. 124 CA at 128; *Roberts v Gill & Co* [2010] 2 W.L.R. 1227 at [57]–[61], per Lord Collins.

¹² Albeit that CPR r.19.9E provides that the court may order the company for the benefit of which a derivative claim is brought to indemnify the claimant against any liability in respect of costs incurred in the permission application or in the derivative claim, or both. If the claimant seeks an order that the company indemnify him or her against any liability for costs incurred in the permission application or the claim, this should be stated in the permission application or claim form, or both: Practice Direction 19C—Derivative Claims supplementing Pt 19 (“PD 19C”), para.2(2).

¹³ *Singh v Anand* (LTL 19/10/2006) at [10]–[11] (H.H. Judge Norris QC sitting as a High Court Judge).

¹⁴ CPR r.19.9A(2)(a).

¹⁵ CPR r.19.9A(2)(b).

¹⁶ CPR r.19.9A(3).

¹⁷ See Law Commission, *Shareholder Remedies* (HMSO, 1997) LC 246, paras 6.4 and 6.71.

¹⁸ *Hansard*, HL, col.885 (May 9, 2006).

¹⁹ The two-stage procedure was followed in *Iesini v Westrip Holdings Ltd* [2009] EWHC 2526 (Ch); [2010] B.C.C. 420 Ch D, where Lewison J. noted, at [78], that Norris J. had considered the application on paper and formed the view that there was a prima facie case.

defendants have frequently agreed to treat the hearing as the second stage of the permission application.²⁰ On one occasion, the court overrode the defendants' objection to telescoping the two-stage procedure into one.²¹

The first stage

Where notifying the company of the permission application would be likely to frustrate some part of the remedy sought, the court may, on application by the claimant, order that the company need not be notified for such period after the issue of the claim form as the court directs.²² Otherwise, the claimant must²³ notify the company of the claim and the permission application by sending²⁴ to the company as soon as reasonably practicable after the claim form is issued:

- a. a notice in the form set out in PD 19C, to which is to be attached a copy of the provisions of s.263(1)–(4) of the CA 2006;
- b. copies of the claim form and the particulars of claim;
- c. the application notice; and
- d. a copy of the evidence filed by the claimant in support of the permission application.

The claimant must file a witness statement confirming that he or she has notified the company in accordance with CPR r.19.9A(4).²⁵

At the first stage, if satisfied that the application and the evidence filed by the claimant in support of it do not disclose a prima facie case for giving permission, the court must dismiss the application for permission and make any consequential order it considers appropriate.²⁶ Where the court dismisses the claimant's permission application without a hearing, the court will notify the claimant and (unless the court orders otherwise) the company of that decision.²⁷

²⁰ *Franbar Holdings Ltd v Patel* [2008] EWHC 1534 (Ch); [2009] 1 B.C.L.C. 1 Ch D at [24]; *Mission Capital Plc v Sinclair* [2008] EWHC 1339 (Ch); [2010] 1 B.C.L.C. 304 Ch D at [36], where Floyd J. commented "in this case the parties have sensibly agreed to combine the two parts of the process". In *Wishart v Castlecroft Securities Ltd* [2009] CSIH 65; [2010] B.C.C. 161 at [9], Lord Reed (giving the judgment of the Inner House) noted: "In practice, the parties may agree to telescope this procedure by dealing with the application in its entirety at a single hearing."

²¹ In *Stimpson v Southern Landlords Association* [2009] EWHC 2072 (Ch); [2010] B.C.C. 387 Ch D at [3], H.H. Judge Pelling QC (sitting as a Deputy High Court Judge) stated: "Although the defendants suggest that I should stick to the two-stage process and start by asking myself whether a prima facie case has been made out, I consider that to be unduly elaborate in the circumstances of this case. I prefer to approach the application by reference to s 263 of [the CA 2006] as if the case had been considered initially because that reflects the procedural as well as the practical reality and will yield the fair and proper result."

²² CPR r.19.9A(7). CPR r.19.9A(8) provides that an application under CPR r.19.9A(7) may be made without notice. It is likely that most, if not all, such applications will be made without notice. Where the claimant applies for an order under CPR r.19.9A(7) delaying notice to the defendant company, he or she must (i) state in the application notice the reasons for the application, and (ii) file with it any written evidence in support of the application. Circumstances in which an order might be sought that for a certain period of time the company need not be notified of the permission application could include those identified by Walton J. in *Smith v Croft (No.1)* [1986] 1 W.L.R. 580 Ch D at 589. In that case, in the slightly different context of a derivative claimant withholding from disclosing material to the company when seeking a costs indemnity order, Walton J. gave as examples where withholding disclosure from the company could be fully justified on the grounds that disclosure "would stultify the success of the action", (i) keeping secret the identity of "that most repellent feature of modern society, the mole", lest the leak of unauthorised documents would then cease, and (ii) "any evidence tending to show that the company, or those in control, were taking steps to destroy documents, cover their tracks or matters of a like nature".

²³ CPR r.19.9A(4).

²⁴ The claimant may send the notice and documents required by CPR r.19.9A(4) to the company by any method permitted by CPR Pt 6 as if the notice and documents were being served on the company: CPR r.19.9A(5).

²⁵ CPR r.19.9A(6).

²⁶ CA 2006 s.261(2).

²⁷ CPR r.19.9A(9).

The claimant may ask for an oral hearing to reconsider the decision to dismiss the permission application, but must:

- a. make the request to the court in writing within seven days of being notified of the decision; and
- b. notify the company in writing, as soon as reasonably practicable, of that request unless the court orders otherwise.²⁸

Where the court subsequently dismisses the permission application at an oral hearing, it will notify the claimant and the company of its decision.²⁹

The decision whether the claimant's evidence discloses a prima facie case will normally be made without submissions from or (in the case of an oral hearing to reconsider such a decision pursuant to CPR r.19.9A(9)) attendance by the company. If, without invitation from the court, the company volunteers a submission or attendance, the company will not normally be allowed any costs of that submission or attendance.³⁰

Nevertheless, in an appropriate case the company may properly choose to file evidence at this stage focused specifically on issues of direct relevance to the question whether there is a prima facie case disclosed for granting the application for permission: e.g. providing a copy of its register of members if the claimant is not in fact a member of the company, or providing evidence that the act or omission complained of was authorised by the company before it occurred or has since been ratified by the company. At this stage, however, the company should not address the underlying merits of the claim.³¹

If the court does not dismiss the application at the first stage, it will³²:

- a. order that the company and any other appropriate party must be made respondents to the permission application; and
- b. give directions for the service on the company and any other appropriate party of the application notice and the claim form.

At this stage, the court has a choice³³ whether:

- a. to give directions as to the evidence to be provided by the company; or
- b. to adjourn the proceedings to enable the evidence to be obtained.

The phrase "to enable the evidence to be obtained" can include giving the company the opportunity to create facts on the ground, e.g. to ratify the alleged breaches, or to consult with an "independent organ".³⁴

²⁸ CPR r.19.9A(10).

²⁹ CPR r.19.9A(11).

³⁰ PD 19C, para.5.

³¹ See Chivers and Shaw, *The Law of Majority Shareholder Power* (Oxford: OUP, 2008), para.9.34.

³² CPR r.19.9A(12).

³³ CA 2006 s.261(3).

³⁴ *Smith v Croft (No.2)* [1988] Ch. 114 Ch D at 185b-185c (Knox J.) where an adjournment was granted to enable shareholders to be consulted. See too *Harley Street Capital Ltd v Tchigirinsky (No.2)* [2005] EWHC 1897 (Ch); [2006] B.C.C. 209 Ch D at [65], where the permission application was adjourned to enable the sole independent director of the company to commission and then consider an independent report into the alleged wrong on which the derivative claim was based.

The second stage

At the substantive hearing of the permission application, the court has three options. It can³⁵:

- a. give permission to continue the claim on such terms as it thinks fit;
- b. refuse permission, and dismiss the claim; or
- c. adjourn the proceedings on the application and give such directions as it thinks fit.

At the second stage of the permission application the court has a choice³⁶ whether to give directions as to the evidence to be provided by the company or to adjourn the proceedings to enable the evidence to be obtained. Section 261(3) of the CA 2006 does not expressly permit the court to give directions as to the provision of evidence by the substantive defendants to the derivative claim. Nor does s.262 give any indication that the substantive defendants are intended to participate in the proceedings on the application.

The wording of s.266(4)(c) (the Scottish equivalent of s.261(3)) led Lord Glennie, in *Wishart v Castlecroft Securities Ltd*,³⁷ to hold that it was not necessary for the substantive defendants to be served with the permission application, adding that it seemed to him:

“to be undesirable that the potential [defendants] should have the opportunity in their own name to have any say in proceedings commenced for the purpose of determining whether or not they should be sued by or on behalf of the company. Their involvement at the leave stage might result in that application being used as a dress rehearsal for the full action.”

Lord Glennie’s approach was endorsed on appeal. Lord Reed stated³⁸ that ss.265–269³⁹ of the CA 2006:

“are concerned with decisions concerning the commencement and continuation of legal proceedings by or on behalf of a company ... The fundamental issue which the court has to determine is whether it should interfere in the management of the company by overriding the decision of those responsible under the company’s articles for the management of its affairs, so as to permit proceedings to be brought on its behalf, by the member, in order to enforce the company’s rights. The provisions do not have in view the interests of third parties. The directors have no interest in the proceedings as individuals (other than in the most general sense), by reason of being intended [defendants] in the derivative proceedings. The court is not being asked to determine any issue affecting their rights or obligations as individuals. Nor does any third party who might be convened as a [defendant] in the derivative proceedings ordinarily have an interest in the leave proceedings: no legal liability will attach to them in consequence of the grant of leave.”

³⁵ CA 2006 s.261(4).

³⁶ CA 2006 s.261(3).

³⁷ [2010] B.C.C. 161 at [18].

³⁸ *Ibid*, at [19].

³⁹ The Scottish equivalents of ss.260–264.

This approach has not been, and is unlikely to be, adopted in England. The reasons for this are twofold. First, the approach which the Scottish courts adopted in *Wishart v Castlecroft Securities Ltd*⁴⁰ appears to have been strongly influenced by an important difference between Scottish and English procedure. Unlike in England, where the claimant does not require the permission of the court to issue a derivative claim but is required by s.261 of the CA 2006 to seek permission from the court to continue it, in Scotland the leave of the court must be sought and obtained before derivative proceedings can be brought. Accordingly, whereas in England the application for permission to continue the derivative claim is made in the derivative action itself, so that the application for permission is part of the procedure in the substantive action, in Scotland, where there cannot be any derivative action on foot when the application for leave is made, the application for leave must be made by a separate originating process. As a result, in Scotland there is a serious question as to whether the proposed defendants against whom substantive relief is intended to be sought in the derivative action should be entitled to participate in the entirely separate prior proceedings whose purpose is to determine whether the derivative claim should be permitted to be brought.

Secondly, English courts would be unlikely to endorse the adoption of an approach which would be likely to encourage the company in many cases to incur what may be substantial costs actively participating in the application for permission to continue the derivative claim. In *Carlisle and Cumbria United Independent Supporters' Society Ltd v CUFC Holdings Ltd*,⁴¹ Arden L.J., in response to the submission that the subject companies were entitled to incur costs in a derivative action, for instance by participating in an application for permission to continue a derivative action, was not prepared to go beyond stating that she accepted that “there are or may be limited occasions on which a company can incur costs even in a derivative action brought on its behalf”.

In that case, the Court of Appeal ordered the defendant director to reimburse both the costs that the subject companies had incurred responding to the application for permission to continue the derivative claim and the sums which those companies had paid towards his own costs. Arden L.J. stated⁴² that in principle the same rule should apply in a derivative claim as in a minority shareholder’s petition under s.994 of the CA 2006, and accordingly that the defendant director should not have recourse to the funds of the company on whose behalf the derivative action is brought, but added:

“unlike a minority shareholder’s petition in most cases, a derivative action is brought to enforce a claim that belongs to the company and not a personal claim, and consequences may flow from that difference.”

It is suggested that this is an important difference, and that it may well be appropriate for the company to participate, and to incur costs, at the permission stage. Personal and derivative corporate litigation are very different in nature, and the role which the company itself can and should play, at any rate at different stages of the litigation, may as a result be different. Accordingly, principles which

⁴⁰ [2010] B.C.C. 161 at [18].

⁴¹ [2010] EWCA Civ 463 at [22].

⁴² *Ibid.*, at [24].

case law—notably the decision of Lindsay J. in *Re a Company (No.001126 of 1992)*,⁴³ which expressly related to “a company’s active participation in or payment of its own costs in respect of active participation in a [s.994] petition as to its affairs”—has laid down for the conduct of companies the subject of unfair prejudice, and just and equitable winding-up, petitions should not mechanically and automatically be applied to derivative claims, at any rate until after the determination of (i) the claimant’s application for permission to continue the claim, and (ii) any other applications which may affect the company, such as an application by the claimant for a costs indemnity order or interim injunctive relief against the company.

Further, it is apparent from the procedure laid down by the CA 2006 (summarised above) that it is anticipated that the company the subject of the derivative claim will take active steps to put in evidence in relation to and to be represented at an application for permission to continue a derivative claim and/or an application for a costs indemnity order and/or interim injunctive relief and will incur legal costs in that regard.

It is suggested that the rationale behind the three-stage filter process at the permission stage is twofold:

- a. to enable applications which do not disclose a prima facie case to be dismissed without the need for the company to participate in the proceedings: hence para.5 of PD 19C, which makes clear that companies are ordinarily expected to take no steps until invited to do so by the court after the claimant has demonstrated a prima facie case, i.e. not until the full hearing of the application to continue⁴⁴; but
- b. to enable the company to put in evidence for and make submissions at the full hearing of the application to continue. Granting permission to bring a derivative claim impinges upon the company’s usual entitlement to decide for itself whether it wishes to bring legal proceedings. It may be appropriate that the company express its views to the court before that entitlement is removed from it.

The derivative claimant has no authority from the company to bring the claim. Rather, his or her authority to do so is only derived—retrospectively—from his or her obtaining an order from the court granting him or her permission to continue the claim. This derivative right will only be exercisable once the claim is properly constituted as one brought on behalf of the company, that is, once permission has been given to the shareholder to continue it. Until then, the derivative claimant is not authorised to bring the claim, and, by CPR r.19.9(4), cannot, without the court’s permission, take any further step in the proceedings until after he or she has obtained permission to continue the claim.

⁴³ [1994] 2 B.C.L.C. 146 at 155.

⁴⁴ Albeit that, as noted above, in an appropriate case the company may properly choose to file evidence at this stage focused specifically on issues of direct relevance to the question whether there is a prima facie case disclosed for granting the application for permission: e.g. providing a copy of its register of members if the claimant is not in fact a member of the company, or providing evidence that the act or omission complained of was authorised by the company before it occurred or has since been ratified by the company: see Chivers and Shaw, *The Law of Majority Shareholder Power*, para.9.34.

Once permission is granted to bring the claim, the role of the company should ordinarily be more limited, as the claim can then be viewed as one validly brought on the company's behalf. Furthermore, given the broad range of matters which the court must take into account in determining whether to give permission for the claim to proceed, and given that the claimant's prima facie case will have been tested before permission is granted, the legitimacy of the derivative claimant's role in representing the company after permission is granted should be more clear.⁴⁵

Before that stage is reached, however, it is submitted that the company can, and in an appropriate case should, take an active role. It has an interest in being represented where orders are sought against (or which directly affect) it, including applications for interim injunctive relief against the company, since the grant of such relief would inhibit the company in its actions; applications for permission to continue the claim; and applications for costs indemnity orders.

As regards applications for permission to continue the claim: until the derivative claimant obtains permission, it will not be clear that he or she should be permitted to act on behalf of the company. Given the potentially damaging effect of such litigation, the company accordingly may have an interest in resisting it where it has strong grounds for considering that the shareholder should not be given permission to proceed. The grant of permission derogates from the directors' right to determine whether or not the company should commence litigation. Hence the three-filter procedure laid down by s.262 of the CA 2006, which, as do CPR r.19.9 and 19C PD, expressly envisages the company taking active steps to put in evidence in relation to and to be represented at the application for permission to continue the claim. In particular, one of the factors that the court must expressly consider under s.262 is whether the company has decided not to pursue the claim. It is not sufficient for the court merely to note that the company has decided not to pursue the claim. The court must consider the reasons given by the company as to why it came to that decision:

“In circumstances where the company has decided not to pursue the claim, the court will want to look at why it decided that. There are a number of possibilities. One would be that it had made a bona fide decision that the claim ought not to be pursued. Such a decision would be very influential with the court, which may decide not to allow the claim to go ahead. Alternatively, the company may have decided not to pursue the claim for reasons that the court finds unsatisfactory, which might have the opposite effect. It would be for the court to determine.”⁴⁶

Accordingly, the company may need to put in evidence to explain why it has decided not to pursue the claim sought to be brought by the derivative claimant.

⁴⁵ See J. Loughrey, “Privileged Litigants: shareholder rights, information disclosure and corporate privilege” [2007] J.B.L. 778 at 798.

⁴⁶ *Hansard*, HL, col.GC8 (February 27, 2006), Lord Goldsmith.

Applications for costs indemnity orders

Further, it may well be appropriate for the company to be represented at the hearing of, and to make representations in relation to, any application by the claimant for a costs indemnity order,⁴⁷ since the company is the party which the claimant is seeking to make liable to grant him or her what may well be a very wide-ranging (and potentially uncapped) indemnity in respect of his or her costs and any adverse costs made against him or her. As Walton J. stated in *Smith v Croft*:

“the justice of an order which may throw upon the company which, in the event, is proved to have no cause of action whatsoever against the other defendants, who may prove to be completely blameless, the entire costs of an action which it did not wish to be prosecuted, is extremely difficult to comprehend”⁴⁸;

and

“In the case of a [costs indemnity] application there is no ... possibility of subsequent rectification of injustice: by how much more then, must it be quite clear that, in the normal case ... it must be right that ... the company should be joined and able to lay what facts it wishes to lay before the court.”⁴⁹

In *Smith v Croft (No.1)* itself the company successfully applied to set aside a costs indemnity order which the claimants had obtained ex parte. It is now clear that applications for costs indemnity orders must be made on notice to the company, since if the claimant seeks an order that the defendant company indemnify him or her against liability for costs incurred in the permission application or the claim, this should be stated in the permission application or claim form or both, as the case requires.⁵⁰ This is a further indication that in an appropriate case the company can, and indeed is expected to, take an active role in responding to an application by a derivative claimant for a costs indemnity order against it.

⁴⁷ See *Wallersteiner v Moir (No.2)* [1975] Q.B. 373 CA.

⁴⁸ *Smith v Croft (No.1)* [1986] 1 W.L.R. 580 at 583D–583E.

⁴⁹ *Ibid*, at 588E.

⁵⁰ PD 19C, para.2(2).