ISSUE **25**

serlespeak

RAISING THE BAR IN CHANCERY AND COMMERCIAL

Company Law

"A strong Chancery set with 'real strength in depth in company and partnership and fraud related matters'"

Chambers UK

Welcome to this new edition of Serlespeak on topics in company law. In the first article, I analyse recent cases on the reasons which can be relied on by a respondent to justify the removal of a section 994 petitioner from office as a director. Emma Hargreaves also writes on unfair prejudice petitions, specifically on the court's approach to share purchase orders where the petitioner is concerned that they may give rise to a tax liability. Timothy Collingwood then considers the scope for asserting that a duty of good faith has arisen under a shareholders' agreement. Matthew Morrison examines recent authority on the interrelationship between *de facto* and shadow directorships and the question whether shadow directors as such ordinarily owe fiduciary duties. Finally, Jamie Randall discusses the meaning of certain provisions limiting the exercise of shareholders' rights under the Companies Act 2006.

Daniel Lightman QC

Chambers News & Events

People

Serle Court welcomed Zoe O' Sullivan QC to Chambers from One Essex Court and Tim Benham-Mirando and Max Marenbon who started pupillage with us in October.

Andrew Bruce is congratulated on his selection to join the Pool of Arbitrators at the Court of Arbitration for Art (CAfA) based in The Hague.

Conferences and seminars

We have had an exceptionally busy year running a series of conferences, seminars and client meetings a few of which are highlighted below:

C5 Hong Kong. We sponsored the C5 Fraud and Asset Tracing conference in Hong Kong in June. Dakis Hagen QC and Andrew Moran QC took part as speakers. In addition, Philip Jones QC, Zoe O'Sullivan QC, Daniel Lightman QC, Richard Wilson QC and Tim Collingwood delivered seminars to several firms in Hong Kong over 4 visits in 2019.

Property Conference. We hosted a half-day property conference *"Trouble at Mall"* at Lincoln's Inn Old Hall. The conference was attended by 75 clients from London and beyond. Members of Serle Court took part in panel discussions during the conference. The conference was chaired by Christopher Stoner QC.

Jersey. We held a Commercial and Offshore Trusts Conference in Jersey in September, which included panel sessions on company law, trusts and civil fraud. Serle Court members took part in the panel discussions during the conference. The conference was chaired by Lance Ashworth QC.

Cyprus. We hosted our first Cross Border Litigation Conference in Cyprus in September at which Serle Court members took part together with Cypriot and international lawyers. The conference was chaired by Philip Jones QC.

Commercial Series of seminars. We delivered a series of three commercial seminars, *Fraud and Arbitration,* which took place in chambers. Zoe O'Sullivan QC chaired the session, and the speakers were Jennifer Haywood, James Mather and Sophia Hurst. They touched on topics about English and BVI cases on arbitration awards procured by fraud and court powers exercisable in support of arbitration.

1975 Act Seminar. We held a breakfast seminar at Serle Court on the 1975 Act. The session was chaired by Richard Wilson QC. Constance McDonnell QC, Jennifer Haywood, James Weale and Gregor Hogan were the speakers. Topics covered were What's been happening since *Ilott v Mitson?* The reasonableness of provision by way of an interest under a trust; Interim applications under s.5 of the 1975 Act; and Cases on claims out of time?

Client Party. We hosted our annual client party this year at the London Transport Museum in October, with over 300 clients attending and enjoying what was a memorable evening.

New York. We hosted our 4th International Trusts & Commercial Litigation Conference in New York on Monday, 11th November at the Top of the Rock at the Rainbow Room in the Rockefeller Centre. We welcomed over 100 clients from London, the Channel Islands, Bermuda, Bahamas, the Cayman Islands, the British Virgin Islands, Turks & Caicos Islands, and the USA with over 20 Serle Court members speaking on panel sessions.

Upcoming chambers events

Coming up later in the year: dates to be confirmed
Half-Day Property Conference
Half-Day Civil Fraud Conference

New date to follow
Serle Court Company Conference 2020: Company Law in the Real World

These events are supported by our Business Development team and Clerks who organise and attend events in London and around the world.

Awards and Directories

We want to congratulate Richard Wilson QC who won 'Advocate of the Year' at the 14th Annual STEP Private Client Awards 2019. The judges said *"Richard is an exceptionally talented practitioner, who plays ground-breaking strategies in high-profile cases that are forming our body of law. He is a star now and will be a bigger star in the future."*

We are delighted to be shortlisted as Chambers of the Year at the British Legal Awards 2019. The winners will be announced at an awards ceremony on Thursday, 21st November 2019 at the Ballroom Southbank.

Serle Court is thrilled to announce we have had another successful year in the directories. We have been recommended in 10 practice areas in Chambers & Partners 2020 UK Bar Guide including being ranked band 1 in 5 practice areas (Chancery Commercial, Chancery Traditional, Fraud: Civil, Partnership and Offshore). We were also recommended in the Legal 500 2020 edition where we are ranked as a top tier set in 4 practice areas (Fraud: Civil, Offshore, Private Client: Trust and Probate, and Partnership) and as a leading set in 11 practice areas.

LinkedIn

We have six discussion groups on LinkedIn to enable Serle Court members and clients to discuss topical issues in Partnership and LLP Law, Fraud and Asset Tracing, Contentious Trusts and Probate; Competition Law; Middle East & Arab Law Group and Intellectual Property, please join us.

Please also follow us on Twitter @Serle_Court.

***Serlespeak* is edited by Jonathan Fowles**

Can a petitioner's exclusion be justified by matters of which the respondent was unaware at the time?

A common complaint in an unfair prejudice petition is that there was an understanding that the petitioner would hold office as a director and that their removal as a director in breach of that understanding is unfairly prejudicial to their interests as a shareholder within the meaning of section 994 of the Companies Act 2006 (the 2006 Act).

If the petitioner can show that the exercise by the majority shareholder of the power to remove them as a director was subject to equitable constraints, then the majority shareholder needs to show that the petitioner's removal from office was justified by their misconduct — that their conduct merited their exclusion.

When seeking to justify their exercise of the power of removal, can the majority shareholder rely on matters of which they were unaware at the time of the removal, and which accordingly did not feature in their decision-making process at that time, but of which they subsequently become aware?

Two recent judgments have clarified the law on this issue, on which there had been a conflict of authorities.

In *Amin v Amin* [2009] EWHC 3356 (Ch), at [418], Warren J expressed the (obiter) view that the broad nature of the inquiry which the Court should carry out before deciding whether any (and if so what) relief should be granted under section 996 of the 2006 Act suggests that conduct prior to the presentation of the petition is a relevant consideration, regardless of whether it was known about at the time.

Mr Mark Cawson QC (sitting as a deputy High Court Judge) took a different view in *Judge v Bahd & Ors* [2014] EWHC 2206 (Ch), where he stated, at [119], that when considering whether the exclusion of the petitioner from management was justified he would not take account of two issues relevant to the petitioner's conduct which "*only arose as issues*" once he had been excluded, and which therefore *"did not operate on* [the respondent's] *mind at the relevant time".* Adopting that approach, where a respondent seeks to justify the petitioner's exclusion by reference to the petitioner's own misconduct, the respondent cannot do so by reference to alleged misconduct of which he was unaware at the time of the exclusion.

It should be noted that Mr Cawson QC did not refer in his judgment in *Judge v Bahd* to Warren J's judgment in *Amin v Amin.*

In *Waldron v Waldron* [2019] EWHC 115 (Ch); [2019] Bus LR 1351, however, HH Judge Eyre QC (sitting as a High Court Judge) concluded, at [49], that it would be wrong as a matter of principle to impose a requirement of causal connexion before account can be taken of an excluded party's conduct when addressing the fairness or unfairness of their exclusion. Judge Eyre QC went on to point out that in any event, separate from the question whether unfairness is made out, the Court must also consider what relief it thinks fit to grant. Accordingly, even if the petitioner's conduct were held not to be relevant to the fairness of an exclusion which it had not caused it would still be highly relevant to the question of the appropriate relief. This is because when considering what (if any) relief under section 996 it thinks fit to grant, the Court is bound to look to the circumstances as a whole and a petitioner's conduct would be of great significance at that stage.

This issue was considered again in the very recent case of *Re Dinglis Properties Ltd* [2019] EWHC 1664 (Ch). In that case, at the heart of the wrongdoing on which the respondents relied was an alleged misappropriation by the petitioner of which the respondents acknowledged that they were not aware, and so did not feature in their decision-making, when they terminated the petitioner's involvement in the business.

The respondents argued that the proper approach was not confined to matters of which they were aware at the time of the exclusion. Ultimately, they maintained, the issue was whether the petitioner had been unfairly prejudiced. That requires an objective analysis. Thus, in determining whether the conduct complained of was unfair, the conduct of both the petitioner and the respondents, *whether or not known about at the time*, would be relevant considerations, in accordance with the views which Warren J had expressed in *Amin v Amin.*

Accepting the respondents' argument, Adam Johnson QC (sitting as a deputy High Court Judge) agreed that the proper approach is a broad, objective one, and that in assessing the fairness or otherwise of the petitioner's exclusion, there is no bar to taking account of matters which were in existence at the time, but not actually known to the respondents. He thus preferred the approach of Warren J in *Amin v Amin* and of HH Judge Eyre QC in *Waldron v Waldron* to that of Mr Cawson QC in *Judge v Bahd.*

As Mr Johnson QC pointed out, this conclusion results from the language of section 994(1)(a):
"… the company's affairs are being or have been conducted in a manner that is unfairly prejudicial…"

This wording suggests that the determination of unfairness is, in principle, objective: it makes no reference to the state of knowledge of either the petitioner or the respondents. Where the petitioner has been excluded, the question is: was the exclusion fair? The respondents ought to be entitled to argue that it was, by reference to all of the relevant circumstances obtaining at the time of the exclusion, whether they were subjectively aware of them or not.

Take the example of a respondent who makes the decision to exclude the petitioner on an entirely mistaken basis, not knowing that at the same time — perhaps because the truth had been concealed from him — the petitioner was in fact guilty of serious misconduct which would certainly have justified exclusion, if known about. In such a case, Mr Johnson QC considered, it ought to be open to the respondent to argue that the petitioner's exclusion was objectively fair, in the sense that his (unknown) conduct was damaging to the business and he deserved to play no ongoing part in managing it.

Daniel Lightman QC *represented the respondents in* Re Dinglis Properties Ltd *[2019] EWHC 1664 (Ch).*

A contributor to Joffe on Minority Shareholders *(6th Ed, 2018), he is described by Legal 500, 2020, as "a leading company silk whose knowledge in the area and strategic nous is legendary".*

Structuring share purchase orders to mitigate tax

In *Re Edwardian Group Ltd* [2019] EWHC 2039 (Ch); [2019] S.T.C. 1814, Fancourt J has given important guidance on the proper approach where a petitioner seeks an order under section 996 of the 2006 Act obliging the company to purchase its shares pursuant to a structure designed to minimise the petitioner's UK tax liabilities.

Re Edwardian Group Ltd concerned an unfair prejudice petition relating to a well-known hotel group. Following split trials on liability ([2019] 1 BCLC 171) and quantum ([2019] EWHC 873 (Ch)), Fancourt J ordered the First Respondent ("JS") and the Company to purchase the Petitioners' shares on a joint and several basis, fixing the price payable.

After the handing down of the quantum judgment but prior to the sealing of the order, the Petitioners belatedly realised that a purchase by the Company (rather than any other person) would be treated as an income distribution by a UK resident company under sections 368 and 383 of the Income Tax (Trading and Other Income) Act 2005, giving rise to a 38.1% immediate tax liability. The Petitioners accordingly sought an order obliging the Company to engage in a purchase structure intended to avoid that tax liability (it being accepted that only the Company could fund the purchase).

JS and the Company had declined voluntarily to engage in the structure arguing that, first, there was a real risk it would be regarded by HMRC as aggressive tax avoidance which might have adverse implications for their affairs, and second, the structure required further delay until mid 2020.

The Judge held that there was jurisdiction under section 996 to make the order sought, but considered that the exercise of discretion raised the following questions:

1

"Is the proposed scheme capable of being viewed by a reasonable person (including HMRC) as aggressive tax avoidance, and therefore, although not unlawful, deserving of moral opprobrium? If so…it is hard to envisage circumstances in which the Court would order such a scheme to be carried out before it had been established that it was not improper in that sense."

On the facts, the Judge concluded yes.

2

"Does the proposed scheme give rise to a real risk that HMRC will wish to scrutinise the financial affairs of the Company or JS, thereby potentially causing difficulties for them?"

On the facts, the Judge concluded yes.

3

"If not improper tax avoidance (in the sense identified in (1) above), should the Court nevertheless make an order the sole purpose of which is to enable one party to avoid a tax liability that it will otherwise incur?"

The Judge concluded: "in a purely commercial context such as this, there is no compelling reason why the Court should force reluctant parties to enter into a transaction solely for the purpose of saving tax for another party".

4

"If the Court could do so, is it fair and just to exercise that discretion in favour of the Petitioners?"

On the facts, the Judge concluded no, because "[c]onsiderations of fairness, simplicity and finality far outweigh the interests of the Petitioners in avoiding all risk of paying tax…"

The decision is thus a reminder of the importance of a petitioner considering carefully, before issuing a petition, the tax implications of seeking a share purchase order against the company itself.

Emma Hargreaves *has a broad commercial chancery practice, with particular emphasis on domestic and offshore trust/probate litigation, civil fraud and company disputes. She appeared (led by Daniel Lightman QC) for the First Respondent in* Re Edwardian Group Limited.

"Good faith" in football?

Whether it be through the more prevalent use of shareholders' agreements or a judiciary that has fallen out of love with the term or become concerned by its misuse, the "quasi-partnership" has become a seemingly more endangered species. Troubled by a perceived oppressive course of conduct, how does the unfortunate minority appeal to concepts of fairness or fair play or reasonable conduct without relying on equitable constraints?

One potential line of argument for the minority in such shareholder or joint venture disputes is an allegation of a breach of a duty of good faith.

The inclusion in shareholder agreements of an express obligation of good faith, whether generally or in specific circumstances, is perhaps more common than previously (although the application of such clauses gives rise to problems of its own as to what is required). However, is all lost for a minority in the absence of an express provision? What scope is there to imply a term of good faith in a shareholders' agreement? How should courts treat the landmark decision of *Yam Seng Pte Ltd v International Trade Corp Ltd* ([2013] EWHC 111 (QB)) which first doubted the orthodox rejection of such an implied term outside of certain contexts (in particular insurance).

The recent trend of ball sports producing litigated shareholder and boardroom disputes has thrown up the latest judgment to address the state of the law. In *UTB LLC v Sheffield Utd Ltd* ([2019] EWHC 2322 (Ch)) Fancourt J reviewed the authorities and acknowledged the lack of settled clarity. He held that he should follow Yan Seng and the more recent decision of *Al-Nehayan v Kent* ([2018] EWHC 333 (Comm)). In Fancourt J's judgment the court should approach the issue as a matter of the implication of a term in the usual way on the facts of the case (as opposed to characterising contracts as within a particular classification of "relational contracts"). The question is whether a reasonable person reading the shareholders' agreement at the time it was made would consider that it was obvious that a party had to act in good faith in all dealings with the other (and vice versa) or whether such an obligation is necessary to give coherent business effect to the agreement.

On the facts of the Sheffield Utd case Fancourt J found that it was impossible to say that a mutual obligation of good faith was intended or required for business efficacy. Significant factors militating against such an implied term included: the detailed and professionally drafted nature of the contractual documents; the existence of clauses in the shareholders' agreement requiring good faith in certain specified circumstances; the existence of other clauses in the shareholders' agreement where a duty of good faith would run contrary to the nature of the provision; and the fact that the contractual rights operated well enough without the implication of a term of good faith.

The judgment is clear that a term of good faith will not be implied in all cases of long-term contracts, but there is encouragement for the minority to consider adding such an allegation to their bow in an appropriate case.

Timothy Collingwood, *recently described as "a guru" in Chambers & Partners, has extensive experience of shareholder disputes on both sides of the fence and is a contributor to* Joffe on Minority Shareholders *(6th Ed, 2018).*

The fiduciary nightmare of Casterbridge

The recent decision in *Popely v Popely* [2019] EWHC 1507 (Ch) involved the Chancery Division adopting guidance from the Royal Court of Guernsey in *Carlyle Capital Corporation & Anr v Conway & Ors* (38/2017) as to the interrelationship between *de facto* and shadow directorship. It also arguably presented a missed opportunity for further consideration of the circumstances in which shadow directors will owe fiduciary duties.

The background to the English proceedings which led to the decision of HH Judge Hacon (sitting as a High Court Judge) on 13 June 2019 was aptly described at a case management conference by Master Moncaster as an unhappy dispute in an unhappy family.

Two brothers (J and R) had established an offshore company, Casterbridge Limited, through which to conduct a timeshare business. The sole director of Casterbridge was a company incorporated in St Vincent. Their shareholdings were later transferred to St Vincent trusts for the benefit of their respective families. The beneficiaries of J's trust brought a double-derivative claim against R alleging fraudulent breach of fiduciary duty by R in his capacity as an alleged *de facto* director of Casterbridge.

Significantly, no allegation of shadow directorship appears to have been made against R, still yet any pleading that R would have owed fiduciary duties in such capacity.

It is possible for an individual simultaneously to be a shadow director in respect of some acts and a *de facto* director in respect of others (*Smithton Ltd v Naggar* [2014] EWCA Civ 939 at [32]). HHJ Hacon accepted this, but nevertheless endorsed a qualification found to exist by Lieutenant Bailiff Marshall QC, as part of her analysis of Guernsey law in *Carlyle* (at [743]-[746]), that a person could not simultaneously be a shadow director and a *de facto* director in respect of the same act.

HHJ Hacon further agreed with Lieutenant Bailiff Marshall QC that the concept of *de facto* directorship could not be extended to encompass the circumstances in which an individual would be found to have acted as a shadow director.

Having recognised that these proposition represented English law, HHJ Hacon held that R's actions in causing the corporate director to divert Casterbridge's assets meant that R had been acting as a shadow director and therefore could not have owed fiduciary duties as a *de facto* director. On the basis of the claimants' pleaded case, that was the end of their claim. However, it is unclear from the reports of HHJ Hacon's decision, and from earlier interlocutory decisions, why no case was advanced based upon breaches of fiduciary duty owed by R as a shadow director.

An appellate court is still to resolve the differences of approach between Lewison J in *Ultraframe (UK) Limited v Fielding* [2005] EWHC 1638 (Ch) — shadow directors do not typically owe fiduciary duties - and Newey J in *Vivendi SA v Richards* [2013] BCC 771 at [143] — shadow directors typically owe fiduciary duties in respect of instructions they give. A further attempt to square this particular circle was, however, made by Morgan J at first instance in *Instant Access Properties Ltd (in liquidation) v Rosser & Ors* [2018] EWHC 756 (Ch).

Morgan J went back to first principles and recognised that the question whether an individual owes fiduciary duties is a fact sensitive matter (at [262]). As a result, rather than focussing upon whether or not an individual had a particular role such as that of shadow director, the key question is instead *"whether the individual has expressly or impliedly (from the circumstances) undertaken or assumed a position of trust and confidence or whether there is a legitimate expectation that he will not use his position in a way adverse to the interests of the other"* (at [263]).

Given the background to the incorporation of Casterbridge as a vehicle for the brothers' venture, and its ownership by trusts established for the benefit of their respective families, it would clearly have been open to the claimants to argue for such an assumption of responsibility.

In the alternative they could have sought to persuade the court to follow Newey J in *Vivendi* and find that R owed fiduciary duties in respect of the instructions he gave. The claimant's apparent failure to do so means a lost opportunity for further consideration of the circumstances in which shadow directors will owe fiduciary duties, and the potential for an appeal which might have resolved this question once and for all.

Matthew Morrison *has a broad commercial chancery practice, with a particular emphasis on civil fraud, company and partnership, insolvency, and trust litigation. He was junior counsel in* Carlyle *and* IAP v Rosser.

Vexatious and improper: proper limits on shareholder rights

Being vexed by the neighbours is a near universal experience, so it is appropriate that disputing neighbours should form the background for consideration of the meaning of "vexatious" and "improper" in the provisions of the 2006 Act.

In *Kaye & Ors v Oxford House & Ors* [2019] EWHC 2181, a dispute over a patio ballooned into a litany of conflicts between flat owners, who were also shareholders of the company established to manage the block of flats. The three directors of the company were flat owners and one was in fact the defendant in the patio litigation commenced by the company.

A general meeting was requisitioned by shareholders under s.303(1) and resolutions were proposed to replace the directors. After 21 days, the directors called a general meeting, as required by s.304(1), and included in the notice the proposed resolutions, as required by s.304(2). But at the meeting, the directors said that they had been advised that the resolutions were ineffective under s.303(5)(a) and vexatious under s.303(5)(c) and announced that the meeting was closed and that the resolutions would not be moved.

Lance Ashworth QC (a member of Serle Court), sitting as a Deputy High Court Judge, held that the directors were wrong to do so. In his judgment, the purpose of the scheme in ss.303 and 304 is to give the directors a period, prior to giving notice of the meeting, to consider whether the resolutions can properly be moved and that, once notice has been given, *"there is no residual power remaining in the directors further to consider section 303(5)"*.

While noting that any comments were obiter, Mr Ashworth QC also indicated that he did not consider the resolutions to be vexatious and that he was doubtful that a resolution to remove a director could ever be vexatious for the purposes of s.303(5)(c). He noted that a resolution is vexatious if it is *"troublesome, burdensome or is proposed for no proper purpose"* and that this is to be determined from the perspective of the company, not the directors.

Pandongate House Management Company Limited v Barton [2019] L&TR 23 also concerned a leaseholder, Mr Barton, seeking to exercise his rights as a shareholder in a management company but on this occasion the shareholder's purpose was held to be improper.

Mr Barton had a history of not paying service charges and making futile complaints to various tribunals. HHJ Kramer, sitting as a High Court judge, held that Mr Barton's application under s.116 to inspect the register of members was made so that he could contact the leaseholders to continue his campaign against the company. This was not only detrimental to the directors performing their roles but also contrary to the interests of the other members. He held that this was not a proper purpose and directed that the company need not comply with the request, pursuant to s.117(3).

In many ways, the interpretation of "vexatious" and "improper" (in the words of s.117(3), "not sought for a proper purpose") in these decisions is entirely uncontroversial, but they are a salutary warning to directors and shareholders of when shareholder rights can properly be limited. The provisions exist as a protection to directors from unjustified troublemaking by shareholders, not as a broad power for directors to stifle the proper utilisation of shareholders' rights, even when it is neighbours who are causing the trouble.

Jamie Randall *is developing a practice across Chambers' core areas of expertise. He has been involved in cases across the principal areas of company law, including unfair prejudice petitions, claims against directors, and applications under provisions of the 2006 act.*

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