15 pages.

ROYAL COURT
(Samedi Division) 158.

10th August, 1995

P.R. Le Cras, Esq., Lieutenant Bailiff,
and Jurats Orchard and Gruchy.

Between:	Pacific Investments Limited	Plaintiff
And:	Robert Christensen	First Defendant
And:	Alison Mary Holland	Second Defendant
And:	Michael Allardice	Third Defendant
And:	Graeme Elliott	Fourth Defendant
And:	Firmandale Investments Limited	Fifth Defendant
And:	James Hardie Industries Limited	Sixth Defendant
And:	James Hardie Finance Limited	Seventh Defendant
And:	Govett American Endeavour Fund Limited	Eighth Defendant

Application by the First, Second, Third, Fourth, and Eighth Defendants for an adjournment of the proceedings pending an Extraordinary General Meeting of the Eighth Defendant on 4th September, 1995.

Advocate J.G. White for the Plaintiff.
Advocate W.J. Bailhache for the First, Second, Third, Fourth and Eighth Defendants.
Advocate A.D. Hoy for the Fifth Defendant.
Advocate R.J. Michel for the Sixth and Seventh Defendants.

JUDGMENT

THE LIEUTENANT BAILIFF: The present proceedings which are brought by a minority shareholder in the Eighth Defendant, American Endeavour Fund Limited, form part of wide ranging litigation.

The litigation in Jersey has produced a whole series of applications and representations which we do not presently need to set out in full as before we are called upon to deal with them, we have heard an application by Mr. Bailhache for the First, Second, Third, Fourth and Eighth Defendants, backed by Mr. Hoy for the Fifth Defendant, that all further proceedings should be stayed here until an Extraordinary General Meeting of the Eighth Defendant (the Fund) has been held on the fourth September, 1995.

The situation arises in this way. The Fifth Defendant, Firmandale Investments Limited, with nearly 75% of the shareholding of the Fund, has appointed the First to Fourth Defendants as Directors.

The Plaintiff, Pacific Investments Limited, owns nearly 5% of the shares in the fund, and is suspected by the Defendants of being connected to or of being a surrogate connected to or of being a surrogate of the Govett Group. The remaining 20% or so of the shares are owned by between (we are told) 150 and 180 independent shareholders.

The objectives of Pacific are clearly set out in the Order of Justice which accuses the Fund and Firmandale of wrongdoing.

Mr. Bailhache today raises the point that before embarking on a series of hearings relating to these proceedings the Court should consider whether the Plaintiff should be permitted, as a minority shareholder, to bring these proceedings. In considering this, it was, he submitted, vital for the Court of have before it the views of the independent shareholders as expressed at the Extraordinary General Meeting.

In order to ascertain this the Chairman, Mr. G. Elliot, wrote earlier this week to the shareholders requesting their support and in particular asking the independent shareholders to vote on the resolution attached:

> *"YOUR DIRECTORS BELIEVE THAT IT IS VITAL THAT ALL SHAREHOLDERS WHO ARE INDEPENDENT OF FIRMANDALE INVESTMENTS LIMITED ("FIRMANDALE") (which controls about 75% of the Company's issued share capital) VOTE ON THE RESOLUTION SET OUT ON THE ATTACHED NOTICE OF EXTRAORDINARY GENERAL MEETING: THIS IS BECAUSE, IF A MAJORITY OF THE INDEPENDENT SHAREHOLDERS VOTE IN FAVOUR OF THE RESOLUTION, THE COURT WILL BE ASKED TO DISMISS THE PACIFIC COMPLAINT ON THE GROUND THAT THE INDEPENDENT SHAREHOLDERS DO NOT WISH THE PACIFIC COMPLAINT TO CONTINUE. THIS WILL ALLOW YOUR COMPANY TO CONCENTRATE ITS EFFORTS ON THE MAIN LEGAL PROCEEDINGS IN CALIFORNIA."*

The letter went on to give descriptions of the various actions which Counsel thought were entirely fair.

In support of the proposition that the issues to be raised and the proceedings at the Extraordinary General Meeting were important to the Court, Counsel produced two cases. The first, a decision of the Court of Appeal of England, was Prudential Assurance Corp. -v- Newman Industries (No.2) (1982) 1 All ER 354. Without, in an interlocutory application, citing all the passages put to us by Counsel, we note that their Lordships made an observation at page 366 which reads as follows:

> *"So much for the summons of 10 May. The second observation which we wish to make is merely a comment on the judge's decision that there is an exception to the rule in Foss v Harbottle whenever the justice of the case so requires. We are not convinced that this is a practical test, particularly if it involves a full-dress trial before the test is applied. On the other hand we do not think that the right to bring a derivative action should be decided as a preliminary issue on the hypothesis that all the allegations in the statement of claim of 'fraud' and 'control' are facts, as they would be on the trial of a preliminary point of law. In our view, whatever may be the properly defined boundaries of the exception to the rule, the plaintiff ought at least to be required before proceeding with his action to establish a prima facie case (i) that the company is entitled to the relief claimed and (ii) that the action falls within the proper boundaries of the exception to the rule, in Foss v Harbottle. On the latter issue it may well be right for the judge trying the preliminary issue to grant a sufficient adjournment to enable a meeting of shareholders to be convened by the board, so that he can reach a conclusion in the light of the conduct of, and proceedings at, that meeting."*

Following on from this Counsel cited Smith v Croft (1987) 3 All ER 909. He cited first the headnote and the finding at 909 - 910 which we set out in full:

> *"The main shareholders of a company were the defendants, who held shares carrying 62.5% of the voting rights, and the plaintiffs, who, together with other shareholders who supported them, held shares carrying 14.44% of the voting rights. The defendants were (i) the executive directors of the company, (ii) companies associated with the executive directors (the associated companies) and (iii) the chairman, who was nominated to the board by WT Ltd, which was controlled by a large financial institution holding shares carrying 19.66% of the voting rights in the company. The plaintiffs commenced a minority*

shareholders' action against the defendants alleging (i) that the executive directors had paid themselves excessive remuneration, (ii) that the associated companies had received payments intended to benefit the executive directors rather than the company and that those payments were a dishonest breach of the directors' fiduciary duties and constituted a fraud on the minority shareholders, (iii) that the company's moneys were used to enable the associated companies illegally to purchase the company's shares, and (iv) that payments made to the executive directors supposedly to reimburse expenses were in substance gifts and therefore ultra vires and made in fraudulent breach of the executive directors' fiduciary duties. WT Ltd opposed the plaintiffs' action. The company and one of the executive directors applied to have the action struck out on the ground that the plaintiffs were not entitled to bring it. The issues arose (i) whether the plaintiffs had established a prima facie case that the company was entitled to the relief claimed and (ii) whether the plaintiffs were barred from bringing a minority shareholders' action by the rule that the proper plaintiff in an action in respect of a wrong done to the company was the company itself and not a shareholder or (iii) whether the plaintiffs fell within the exception to that rule which allowed a minority shareholder to bring an action where the wrong done to the company amounted to fraud and the wrongdoers were in control of the company and thus able to prevent the company suing.

Held - (1) The plaintiffs had failed to establish that the company had a prima facie case with respect to the remuneration paid to the executive directors, the payments made to the associated companies or the payments made to the directors as reimbursement of expenses, since it had not been shown that any of those transactions was either ultra vires or excessive and therefore in breach of duty. However, a prima facie case had been established that there had been a breach with respect to payments made to the associated companies for the purpose of acquiring the company's shares, since the defendants had not shown that those payments were properly made in connection with a liability likely to be incurred by the company, namely the remuneration of the executive directors connected with the respective associated companies. Since such a transaction was both ultra vires and illegal, and therefore unratifiable, the plaintiffs had established that the company was prima facie entitled to the relief claimed (see p 937 eh to p 938 a, p 940 c to g and p 941 j to p 942 b, post; Re halt Garage (1964) Ltd [1982] 3 All ER 1016 and dictum of Slade LJ in Rolled Steel Products (Holdings) Ltd v British Steel Corp [1985] 3 All ER at 85 applied.

(2) However, the plaintiffs were not the proper plaintiffs and were therefore barred from bringing their action, for the following reasons -

(a) even though a shareholder was enforcing a personal right when he sought to prevent a company from entering into an ultra vires transaction, any loss caused by the transaction was a wrong done to the company and a minority shareholder was not entitled as of right to bring an action on behalf of the company to recover payments made in the course of the transaction. Instead, it was the company which had the right of redress and accordingly, if there was any reason why the company could not sue, that would preclude the shareholder from suing (see p 945 d to j, post);

(b) since the shareholder could not sue as of right to recover the payments, he had to show, if he himself wished to bring the action, not only that he had locus standi and was not disentitled for personal reasons from suing but also that the company was not barred from suing; furthermore, although the circumstances in which a company could be barred from suing in respect of a wrong done to it under an ultra vires transaction were limited because, for example, such a transaction could not be ratified by the shareholders so as to prevent the company from suing, there was no reason in principle why the shareholders who were independent of the wrongdoers could not abandon or compromise a right of action arising out of an ultra vires transaction, and if they did so a minority shareholder would be precluded from suing on behalf of the company (see p 947 b to f, post);

(c) furthermore, the court would have regard to the views of the majority of the independent shareholders as to whether the action should proceed, since in determining whether a minority shareholder should be prevented from suing on behalf of the company the ultimate question was whether the plaintiff was being improperly prevented from bringing the proceedings, which would not be the case if the plaintiff was prevented from bringing his action by an appropriate independent organ of the company (see p 955e, p 956 b to d j to p 957 d, post);

(d) in deciding whether a shareholder, such as WT Ltd, was independent for the purpose of having regard to his views whether the plaintiffs' minority shareholders' action should be allowed to proceed, the general test was whether his vote would be exercised bona fide for the benefit of the company as a whole. However, in the case of WT Ltd the appropriate test was whether the court was satisfied that WT Ltd would cast its votes with a view to supporting the defendants rather than securing benefit to the company or that there was a substantial risk of WT Ltd doing so. Applying that test, it had not been shown that WT Ltd had, or that there was a substantial risk that it had, opposed the plaintiffs' action in order to support the defendants

would accordingly be treated as an independent shareholder and, taking into account its views, which constituted the views of the majority of the independent shareholders, the plaintiffs' action would be dismissed (see p 957 j to p 958 c and p 960 b to d, post) Allen v Gold Reefs of West Africa [1900-3] All ER Rep 746 and dictum of Walton J in Smith v Croft [1986] 2 All ER at 560 applied."

Following this he referred to a long passage at 955 d - 956 f. As it appears that this point has not previously been before the Courts of this island, we propose to cite it in *extenso*:-

"That passage was cited with approval by Harman LJ in Bamford v Bamford [1960] 1 All ER 969 at 974, [1970] Ch 212 at 240-241. In my judgment, it would not be right in a case where the court declines to act on the views of the board as not sufficiently disinterested to assume that the board was not merely disqualified but also opposed to a decision by the shareholders in general meeting. I see no difference in principle between directors referring a doubtful matter to shareholders in general meeting and the court taking into account the views of shareholders in general meeting where the directors are effectively disqualified from speaking for the company. On this aspect of the matter I accept the submission of counsel for the plaintiffs that the Court of Appeal in Prudential Assurance Co Ltd v Newman Industries Ltd (No 2) did not deal at all with the question of what sort of resolution would have been needed regarding the non-prosecution of the action.

The third point of counsel for the plaintiffs was that in any event Wren Trust's views should not be taken into account. I propose to deal with that later.

I turn now to the question whether it is right for the court to have regard to the views of the majority inside a minority which is, I assume for this purpose, in a position to bring an action to recover on behalf of the company in respect of breaches of duty by persons with overall control.

The fourth defendant and the company claim that it is; the plaintiffs claim that it is not. On the plaintiffs' view of the matter all that the court is concerned with, in cases where the exception to the rule in Foss v Harbottle based on frauds on the minority applies, is the single question whether the defendants have control. The issue is highlighted by the conflicting interpretations placed by the parties on what the Court of Appeal said in Prudential Assurance Co Ltd v Newman Industries Ltd (No 2). Immediately after the formulation of the two matters

which in the Court of Appeal's view a plaintiff ought at least to be required to show before proceeding with a minority shareholder's action there comes the following sentence ([1982] 1 All ER 354 at 366, [1982] Ch 204 at 222):

> *'On the latter issue it may well be right for the judge trying the preliminary issue to grant a sufficient adjournment to enable a meeting of shareholders to be convened by the board, so that he can reach a conclusion in the light of the conduct of, and proceedings at that meeting.'*

Counsel for the plaintiffs submitted that the purpose of that adjournment was to enable the courts to discern whether the defendants had control. I reject that submission. In my judgment the concern of the Court of Appeal in making that statement was to secure for the benefit of a judge deciding whether to allow a minority shareholder's action on behalf of a company to go forward what was described as the commercial assessment whether the prosecution of the action was likely to do more harm than good or, as it was put originally by counsel for Newman Industries, to kill the company by kindness (see [1982] 1 All ER 354 at 366, [1982] Ch 204 at 221). The whole tenor of the Court of Appeal's judgment was directed at securing that a realistic assessment of the practical desirability of the action going forward should be made and should be made by the organ that had the power and ability to take decisions on behalf of the company. Also the question of control pure and simple hardly admitted of any doubt in that particular case.

Counsel for the plaintiffs submitted in the alternative that what the Court of Appeal said was obiter. This I accept, but it was clearly a carefully considered statement contrasting with the express acknowledgment that they had had little argument on the proper boundaries of the exception to the rule in Foss v Harbottle and were therefore not making any definitive statement on that subject, and I propose to follow what I understand to be the true construction of this statement, albeit obiter, unless there is other authority binding on me the other way.

As to that counsel for the plaintiffs 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, i.e. those other than the plaintiffs and the wrongdoers, think should be done. I accept that in many reported cases the court has not gone on to the second stage. Mason v Harris (1879) 11 Ch D 97 is one

such case, and there are modern examples too, such as Pavlides v Jensen [1956] 2 All ER 518, [1956] Ch 565 and Daniels v Daniels [1978] 2 All ER 89, [1978] Ch 406. But the fact that such an investigation was not conducted is not conclusive that it could not be conducted, more especially in the absence of any argument on this precise point. An investigation for interlocutory purposes of the propriety of the exercise of voting power in connection with the proposed prosecution of a minority shareholder's action was conducted by Megarry V-C in Estmanco (Kilner House) Ltd v Greater London Council [1982] 1 All ER 437, [1982] 1 WLR 2. In that case he permitted the action, but counsel for the company submitted that the careful scrutiny to which the propriety of the shareholders' voting activities was subjected is of itself an indication of the significance that the court in a proper case will attach to it. This I accept. Another indication in the same direction is Walton J's reaction in the earlier proceedings. He said ([1986] 2 All ER 551 at 560, [1986] 1 WLR 580 at 591):

> *'this is, of course, not an application to strike out the action on the grounds that it cannot be justified as a minority shareholders' action, but quite clearly the same kind of considerations apply. If the majority of the independent shareholders do not wish the action to be continued, clearly the court will not sanction its continuance and certainly not at the expense of the company."*

Finally Counsel referred the Court to the short passage at 957 a to c.

"Finally on this aspect of the matter I remain unconvinced that a just result is achieved by a single minority shareholder having the right to involve a company in an action for recovery of compensation for the company if all the other minority shareholders are for disinterested reasons satisfied that the proceedings will be productive of more harm than good. If the argument of counsel for the plaintiffs is well founded, once control by the defendants is established the views of the rest of the minority as to the advisability of the prosecution of the suit are necessarily irrelevant. I find that hard to square with the concept of a form of pleading originally introduced on the ground of necessity alone in order to prevent a wrong going without redress.

I therefore conclude that it is proper to have regard to the views of independent shareholders. In this case it is common ground that there would be no useful purpose served by adjourning to enable a general meeting to be

called. For all practical purposes it is quite clear how the votes would be cast, and that I described at the outset of this judgment. The questions therefore remain: what is the test of independence? and does Wren Trust pass it?"

Counsel submitted that it was not known how the independent votes would be cast, and went on to submit that if a majority of the independent shareholders ratify the Directors the Plaintiff's claim must be struck out.

We should say at once that we make no decision on this point, nor indeed are we asked to do so, as we are dealing solely with an application for an adjournment until after the Extraordinary General Meeting.

Counsel, who claim that no prejudice was in any event being suffered by this delay, therefore, put it in this way: that until the result of the Extraordinary General Meeting was known, the Court could not, or at any rate ought not, to decide whether the Plaintiff could proceed even if it were to have a good case.

Until that issue was decided, it was pointless to try to deal with the various applications made by the parties, as if the Defendants won on this point there would be no need for the Court to decide:

a) whether leave to serve proceedings on the Sixth and Seventh Defendants (a point involving an argument as to *forum conveniens*) should have been given by the Judicial Greffier.
b) whether Messrs. Bailhache Labesse should not represent the Directors;
c) whether the Court should consider the position of Messrs. Ogier and Le Masurier (though Counsel reserved his position on that); and
d) on an abbreviated timetable which could not seriously be argued.

All these summonses, he submitted, should be adjourned.

In passing we may add that an application for security for costs is not before this Court but is due to be heard by the Greffier.

Mr. Hoy, for the Fifth Defendant, supported Counsel's submissions.

In answer, Mr. White for the Plaintiff, although he conceded that the Court had a discretion to grant an adjournment, first submitted that it should be refused on account of its lateness. (v. RSC 0.35/3/2).

The Directors could and should have thought about convening an Extraordinary General Meeting months ago.

This application, he submitted, was for tactical advantage.

As to Smith v Croft (1987) 3 All ER 909 the situation there was quite different (see for example at page 926 f and what follows and at 934 and what follows). There, there was an independent report; here the Directors - and this was another reason for seeking independent directors and an independent overview - had simply created their own case and put it, as it were, under the banner of the Company.

Further the facts should be, but were not being, put independently.

He conceded, however, as we think he was right to do, that the view of the majority of the independent shareholders was material and it was proper to have regard to them. The Court could, however, review the circumstances, and the way that the information was provided was important.

He went on to put a number of detailed criticisms of the circular put out by Mr. Elliot. These may be extremely relevant in due course but do not in our view fall to be decided by us on an application for an adjournment pending the Extraordinary General Meeting.

They may very well be most relevant when the application comes on, as will be, we are sure, any representation to the other shareholders by Pacific Investments prior to the Extraordinary General Meeting and careful consideration of the events at the Extraordinary General Meeting and any other facts which ought properly to be before the Court at that time.

In our view, the criticisms certainly do not sufficiently support the proposition that the Court should proceed before the Extraordinary General Meeting has been held.

Counsel for Pacific Investments then submitted that these proceedings were not only derivative but also proceeded under Article 141 of the Companies (Jersey) Law 1991. In his submission, the Order of Justice represented an application to the Court under Article 141 which reads:-

"UNFAIR PREJUDICE
ARTICLE 141.
Power for Member to Apply to Court

(1) A member of a company may apply to the court for an order under Article 143 on the ground that the company's affairs are being or have been conducted in a manner which is unfairly prejudicial to the interest of its members generally or of some part of its members (including at least himself) or that an actual or proposed act or

omission of the company (including an act or omission on its behalf) is or would be so prejudicial."

In support of this he cited in re a Company (1986) BCLC 362 where the Plaintiffs had petitioned the Court under Article 459 of the English Companies Act 1985.

In his submission, an application under Article 141 was a personal application, and the views of the shareholders were of much less importance than where there is derivative action.

In reply, Mr. Bailhache submitted that if the action were not a derivative action it would have been started differently: but even if the Court proceeded on that basis, under Article 143 it would have to take into account the votes of the minority shareholders.

We think that view, that is that in an action brought under section 141, the views of the independent shareholders should in any event be heard, is correct at any rate in the light of the facts claimed in the various pleadings in this litigation.

We wish to add that we are not of course making any finding as to whether the action has been properly pleaded to bring it within the ambit of section 143 as we are dealing solely with an application to adjourn so that the remarks which follow are strictly obiter. Mr. White submitted that the two types of action spring from different bases. One is a personal application and one by a shareholder on behalf of the Company. Article 141 to our mind clearly envisages an application to the Court and not a proceeding commenced by an Order of Justice and we were surprised to hear on the pleadings as they stand that this relief was being sought. This is, we are sure, something which Mr. White will consider in case he should come to the conclusion that he ought to amend his pleadings. However, as we say, even on the basis that Mr. White was correct we still consider that the Court should have before it the result and report of the proceedings at the Extraordinary General Meeting.

In our view the arguments for an adjournment until after the Extraordinary General Meeting, despite the lateness of the application, are all one way.

Whether it is a derivative action or an Article 141 application, the Court will need to know the views of the independent shareholders and the circumstances in which they were obtained including, and not least as we apprehend, how and by whom they were canvassed.

We therefore order an adjournment of the proceedings until after the Extraordinary General Meeting.

The next steps in this litigation, we apprehend, will turn on the circumstances of the Extraordinary General Meeting. Counsel this morning were not entirely agreed as to the next step, and we therefore order that, in the absence of agreement between Counsel as to the course events should take after the Extraordinary General Meeting that, as soon as may be possible and convenient after that event, the parties return to the Court on a summons for directions.

Authorities

Prudential Assurance Corp. Ltd. -v- Newman Industries Ltd. (No.2) (1982) All ER 354.

Smith -v- Croft (No.2) (1987) 3 All ER 909.

Barrett -v- Duckett & Ors. (1993) B C C 778.

Re a Company 008699 of 1985 (1986) 2 B C C 99024.

Re a Company (1986) B C L C 362.

Re a Company (No 003843 of 1986) (1987) B C L C 562.

Re Sam Weller & Sons Ltd. (1990) B C L C 80.

Re Elgindata Limited (1991) B C L C 959.

4 Halsbury 37: pp. 384-5.

R.S.C. (1995 Ed'n) O. 35 r.3.

Royal Court Rules 1992. Rule 8/5.