The Interrelationship between the Derivative Action and the Unfair Prejudice Remedy

8.1 Introduction

The argument so far has concerned itself with reformulating the application and structure of the derivative action as well as resolving the funding and lack of incentives barriers. And the FFM which was put together in previous chapters is meant to provide a procedure for analysing and addressing these concerns. However, given the constraints of space, the ambitions of the remainder of this book are more limited. The investigation will be restricted to certain important practical aspects of the law governing derivative actions.

The availability of 'other adequate remedies' may prevent a minority shareholder from bringing a derivative action.¹ An attractive alternative is the unfair prejudice remedy under s 994 of CA 2006.² Shareholders, even in situations whereby they are adversely affected by the breach of the directors’ duties, are more inclined to pursue the unfair prejudice remedy. In many ways, this is a more flexible and useful remedy for the minority shareholder than derivative actions. The presence of this remedy and the unclear interaction between the two remedies projects an uneasy shadow, which in turn affects the viability of derivative actions.

First, with the exception of situations where only the company would have an action, a shareholder would be better off to rely upon 'unfair prejudice' since there is no need to go through the expense and uncertainty of a preliminary costs order application. In addition, there is no requirement to make an application for leave to bring the unfair prejudice remedy. Secondly, two decisions indicate that...

¹ Barrett v Ducket [1995] 1 BCLC 243, 250; Report, Draft Rules 50.9 and 50.10 in Appendix B.
² Formerly CA 1985, s 459. Sections 459–461 of CA 1985 have been restated in CA 2006, Pt 30 (ss 994–998). Section 999 is a new section which ensures that, if the court makes an order under Pt 30 amending the company’s articles, updated articles are registered and a copy of the court order is supplied with any copies of the articles that are issued by the company, unless they already incorporate the amendments. This chapter will refer to the new sections under CA 2006 for the sake of ease of reference, although it should be noted that much of the case law and arguments below are concerned with ss 459–461 of CA 1985.
the unfair prejudice remedy could substantially replace the derivative action.³ Even in situations where the relief sought is claimed under s 996 of CA 2006⁴ but is sought for the benefit of the company, it is still open for a shareholder to seek a recovery order against the company for payment to him of any cost incurred by him.⁵ This is likely, in turn, as explained below, to make (perhaps unintentionally) derivative actions even less attractive than they already are. Thirdly, proving unfair prejudice may be easier than proving a breach of a corporate right and clearing all the monumental hurdles if one applies to the court for permission to continue a derivative claim under CA 2006, Pt 11.⁶ Finally, in most cases, the applicant personally receives the benefit of the relief provided under the unfair prejudice remedy whereas the benefit of any recovery under the derivative action accrues to the company directly and only indirectly to the applicant. The fact that recovery is the right of the company in derivative action means that a successful litigant will not be better off than fellow shareholders who made no effort to support the proceedings.⁷

Against this backdrop, the popularity of the unfair prejudice remedy is not surprising. The experience in Canada indeed illustrates that the derivative action will be perceived as more procedurally complex and the less favourable form of action without some limit being placed upon the scope of the unfairly prejudicial conduct action.⁸ Several questions arise with respect to the interrelationship between the two remedies: (1) Should the derivative action be dispensed with in favour of a single form of action, making identification of the type of wrong less significant? (2) Alternatively, if it is necessary to maintain a clear division between personal and corporate actions and if accordingly both forms of action should be retained,⁹ should the derivative action be applicable to corporate wrongs and the unfairly prejudicial conduct action solely reserved for personal wrongs? Or should it be possible to obtain a corporate remedy by means of the unfair prejudice remedy? And if so, at what price? The purpose of this concluding chapter is to look into these important questions. By way of disclaimer, it should be clarified that given the constraints of space, the chapter does not consider the theory underlying

⁴ Formerly s CA 1985, s 461.
⁵ Clark v Cutland [2003] EWCA Civ 810, [35], considered below under 8.4.2.
⁶ See Ch 4 above under 4.3.
⁷ See Ch 6 above under 6.2.1.
⁹ Report para 6.11.
the unfair prejudice remedy in any detail,¹⁰ and is not concerned either with the proposals to reform of the unfair prejudice remedy discussed in recent years.¹¹ Instead, the focus here is on the interaction between the two remedies and, in particular on those aspects which may affect the viability of the derivative action.

The chapter proceeds as follows.¹² Section 8.2 briefly examines the history of s 994 of CA 2006. Subsequently, the arguments of assimilating the derivative and the unfair prejudice remedy into a single provision are assessed. Section 8.3 evaluates the merits of the demarcation of the two remedies. As will be seen, the assimilation of these two remedies should be resisted. Accordingly, section 8.4 explores the measures that can be introduced to clarify and simplify the interaction between the two remedies. Section 8.5 concludes.

8.2 The Interaction between the Unfair Prejudice Remedy and the Derivative Action

8.2.1 Introduction

Section 994 of CA 2006 provides that a member of a company may petition for an order on the ground that the affairs of the company are being or have been conducted in a manner which is unfairly prejudicial to the interests of its members generally, or of some part of the members (including at least himself), or that any actual or proposed act or omission of the company is or would be so prejudicial. Under CA 2006, s 996(1), if the court is satisfied that a petition under s 994 is well founded, it may make such order as it thinks fit for giving relief in respect of the matters complained of.¹³


¹¹ For a detailed discussion of the Law Commission’s proposals see, for example, AJ Boyle, above n 10, Ch 5; P Roberts and J Poole ‘Shareholder Remedies—Efficient Litigation and the Unfair Prejudice Remedy’ [1999] JBL 38. The CLR’s proposals are broadly based on the principles put forward by the Law Commission but differ in several key respects: CLR Final Report para 7.41. At the end of the day, not much will change, however, with respect to unfair prejudice petitions (formerly CA 1985, ss 459–461) under CA 2006. These petitions have been restated in CA 2006, ss 994–998.

¹² For an article derived from this chapter, see A Reisberg ‘Shareholders’ Remedies: In Search of Consistency of Principle in English Law’ (2005) 5 EBLR 1063.

¹³ Including regulating the conduct of the company’s affairs; requiring the company to do, or refrain from doing certain acts; authorizing civil proceedings to be brought in the name and on behalf of the company; and ordering the purchase of shares.
To appreciate the breadth of the modern unfair prejudice remedy it is useful to consider briefly its antecedence and to outline the role which its architects had in mind when framing the remedy. Initially, the remedy was introduced to give the courts more flexibility and as an alternative to winding up a company on just and equitable grounds.¹⁴ The forerunner of s 994 was s 210 of the Companies Act 1948, which gave the court power to grant discretionary relief to minority shareholders where they had been victims of ‘oppression’. However, s 210 turned out to be a disappointment in practice, partly because its wording was restrictive and partly as a result of a series of cases in which it was very narrowly construed,¹⁵ so that relief was granted in only a very few cases. A fresh start was made with the Companies Act 1980, when s 210 of the 1948 Act was repealed and replaced by s 75 of the 1980 Act, which was consolidated as s 459 of CA 1985. ‘Oppression’ was replaced by ‘unfairly prejudicial’ conduct, and in a number of other ways the scope of the section was broadened. The result is that a remedy under the new provision has proved to be much more readily available. A further statutory modification was made by the Companies Act 1989, which added the words ‘of its members generally’ to s 459 of CA 1985, so that it is no longer necessary to show that the conduct complained of has had a discriminatory effect as between one part of the shareholders and another. Finally, as part of the reforms introduced by CA 2006, the Government restated CA 1985, ss 459–461 in CA 2006, Pt 30 (ss 994–998). In terms of continuity it is not expected that much will change.¹⁶

In its amended form the statutory remedy under CA 1985, s 459 has proved very popular, particularly in its application to small companies.¹⁷ The range of conduct covered and the flexibility of the relief offered means that it has rapidly become the most attractive solution for a dissatisfied shareholder. Likewise, it avoids the problems of standing and other complexities associated with the rule in *Foss v Harbottle* on the one hand, and the drastic consequences of a winding-up order on the other.¹⁸ But this popularity has brought its own difficulties. In particular, since the jurisdiction to grant a remedy depends upon the ‘unfairness’ of the respondent’s conduct, and since the determination of a suitable remedy may call for an examination of the behaviour of all the parties concerned, many cases have occupied a considerable amount of court time and run up costs on an alarming scale.¹⁹ In response to the widespread concern over these trends, the

¹⁴ Consultation Paper para 7.5.
¹⁵ ibid para 9.1.
¹⁶ This is a positive move particularly as s 260(2)(b) mentions that statutory derivative claims may be launched under the remedies jurisdiction flowing from a successful unfair prejudice petition (and this ties in with the former s 461(2)(c), now CA 2006, s 996(2)(c).
¹⁷ On the difficulties of the application of the unfair prejudice remedy with regard to public companies, see, for example, *Re Astec (BSR) plc* [1999] BCC 59, 86–7; J Payne ‘Section 459 and Public Companies’ (1999) 115 LQR 368; DD Prentice, above n 10.
¹⁸ Consultation Paper 148.
¹⁹ For example, in *Re Elgindata Ltd* [1991] BCLC 959, the hearing lasted 43 days and costs totalled £320,000, when the shares in dispute were worth less than £25,000. That did not even include the costs of the appeal.
Law Commission has made recommendations for procedural changes designed to cut the length and cost of trials, and sought to find alternative ways of resolving internal disputes within small companies. It also put forward the view that if the circumstances in which a derivative action can be brought are made more transparent, members may be encouraged to bring this claim rather than the wide-ranging proceedings under CA 2006, s 994 and accordingly this will shift some of the burden from the unfair prejudice remedy.²⁰ This in itself suggests that the derivative action and the unfair prejudice remedy have some functional equivalence.²¹ It may seem strange at first sight that a right of petition under CA 2006, s 994 vested in the individual member may be used to secure the redress of wrongs done to the company, especially those committed by its directors. However, the language of s 994 is wider in scope and is drafted so as to protect the interests of the members and not just their rights, and it has been so interpreted by the courts.²² Similarly, it cannot be denied that a wrong done to the company may affect the interests of its members. In fact, the Jenkins Committee, whose report recommended the introduction of the unfair prejudice remedy, envisaged that it would have a role in relation to wrongs done to the company.²³ Similarly, in December 1995 a specialist Chancery Working Group considered some of the implications of Lord Woolf’s work²⁴ on Chancery proceedings.²⁵ It expressed the view that proceedings under the unfair prejudice remedy were now instituted where formerly a derivative action would have been brought, and that this had a number of undesirable consequences, including a longer, less certain, and more costly trial.²⁶ Overall then, there is no denying that ‘enabling the court in appropriate cases to outflank the rule in Foss v Harbottle was one of the purposes of the section’.²⁷

8.2.2 Towards amalgamation of the two remedies?

Two decisions in 2003 reaffirmed the view that the unfair prejudice remedy could substantially replace the derivative action.²⁸ Arden LJ gives no reasons for her expansion of the role of the unfair prejudice remedy in Cutland. However, some strong arguments do exist to support this decision. First, the pre-Cutland

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²⁰ Consultation Paper 148.
²² For example, Slade J in Re Bovey Hotel Ventures Ltd (unreported, 13 July 1981), adopted by Nourse J in Re R A Noble & Sons (Clothing) Ltd [1983] BCLC 273, 290.
²⁴ Published in Access to Justice: an Interim Report to the Lord Chancellor on the Civil Justice System in England and Wales (June 1995).
²⁶ Consultation Paper 172 n 2.
²⁷ Re Saul D Harrison & Sons plc [1995] 1 BCLC 14, 18 per Hoffmann LJ (as he then was).
The Derivative Action and the Unfair Prejudice Remedy

line drawn by the judges allowed the unfair prejudice remedy to be brought where a wrong is done to the company but only in order to support a claim for personal relief for the petitioner.²⁹ However, this approach is not necessitated by the terms of s 994 and there is nothing within the legislation to prevent Arden LJ’s approach.³⁰ Indeed s 996(2)(c) provides that a corporate remedy may be awarded by the courts, albeit via the commencement of a new piece of litigation in the company’s name. In circumstances where a wrong is done to the company and corporate relief is sought by a petitioner, it is difficult to see why the cost and inconvenience of two sets of proceedings should be preferable to the court awarding corporate relief directly under s 996.³¹ The chances of a petitioning shareholder wishing to undertake a second piece of litigation are also extremely unlikely given the fact that in most circumstances they are seeking to exit the company by obtaining a buyout order. Unsurprisingly, s 996(2)(c) has been little used in practice and few reported cases exist in which such an order has been made.³²

Secondly, as between these two forms of shareholder remedy, the unfair prejudice remedy has been in the ascendant for some time. As we saw, the law regarding the ability of a minority shareholder to bring a derivative action has long been criticized as being ‘complex and obscure’³³ which, coupled with the significant procedural and financial barriers to bringing a claim, means that very few derivative actions are actually brought. All in all, the unfair prejudice remedy is, and is likely to remain, a far more attractive and convenient remedy for shareholders. Arguably then, a derivative action is now unnecessary because the common law action has been somewhat overshadowed by unfair prejudice petitions.

The initial conclusion might follow that perhaps the most efficient way to proceed is to clarify and slightly broaden the unfair prejudice remedy and amalgamate the derivative action with the other types of actions available under this section.³⁴ In other words, a practical solution would be to combine the derivative action and the unfair prejudice remedy into a single provision embracing all forms of action.

²⁹ See, for example, Re Charnley Davies Ltd (No 2) [1990] BCLC 760, 784 per Millett J. These cases undoubtedly blur the classic distinction between personal wrongs and corporate wrongs, and raise some potentially difficult questions about the ability of shareholders to recover reflective loss, but they do not infringe the principle of collective enforcement of directors’ wrongs because of the personal nature of the remedy involved. See H Hirt ‘In What Circumstances Should Breaches of Directors’ Duties Give Rise to a Remedy under ss 459–461 of the Companies Act 1985?’ (2003) 24 Company Lawyer 100, 109.


³¹ See, for example, Re a Company (No 005287 of 1985) [1986] 1 WLR 281; Consultation Paper para 10.9

³² Formerly CA 1985, s 461(2)(c). One example is Re Cyplon Developments Ltd, unreported, 3 March 1982 (CA). L Kosmin ‘Minority Shareholders’ Remedies: A Practitioner Perspective’ [1997] 2 CFILR 201, 213 (‘If ever an example were sought of an impractical remedy which exists only in the minds of the parliamentary draftsman, this is it’).

³³ Consultation Paper para 6.6.

³⁴ Regrettably, the Law Commission’s reform has not seriously addressed the fundamental question of the distinction between personal and corporate wrongs. See further J Poole and P Roberts ‘Shareholder Remedies—Corporate Wrongs and the Derivative Action’ [1999] JBL 99, 112.
A unified provision could funnel all derivative actions through a leave procedure, while eliminating insupportable differences in matters of standing, procedure, remedies, and substance as between derivative and the unfair prejudice remedy.³⁵ Arguably, this would be desirable for several reasons. First, this would remove the unclear and confusing interaction between the remedies.³⁶ A single, wide-ranging provision would negate argument regarding dual or concurrent claims, while circumventing the chaotic mêlée left in the wake of Foss v Harbottle. Secondly, converting the unfair prejudice remedy to the overt status of a remedy of all-round applicability would have the advantage of breadth and also of certainty in which cause of action to cite.³⁷ Finally, it is arguable that it is difficult to see a justification for the provisions to be separated if in truth they are both designed to achieve the same end of overseeing the actions of directors and management by providing shareholders with an avenue to seek redress for a wrong done.³⁸

8.3 The Case for Retaining Two Separate Remedies

The foregoing discussion raises two immediate questions: (1) Why has it taken the courts so long to make use of the unfair prejudice remedy to provide a substantive remedy to the company in relation to corporate wrongs; and (2) Why was the assimilation of these two remedies actively resisted by the Law Commission when it investigated the issue of shareholders’ remedies? As will be seen below, there are, indeed, very compelling reasons for this resistance.

8.3.1 Leaving a gap in the enforcement mechanisms of corporate governance³⁹

First and foremost, recall that the rule in Foss v Harbottle, which stresses that in relation to a wrong done to the company the company is the only proper plaintiff, emphasizes the collective nature of the process of enforcing directors’ duties.⁴⁰ The collective nature of the process is further emphasized in Wallersteiner v Moir (No 2) that the company and not the individual shareholder should bear the costs of the action in appropriate circumstances.⁴¹ Under a derivative action the claim

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³⁵ JG MacIntosh, above n 8, 68.
³⁶ Similar calls have been voiced in Canada. MacIntosh argues that these two remedies are ‘two pieces of a puzzle that steadfastly refuse to fit together in a tractable fashion’. He explains that this is hindering the orderly development of corporate law doctrine in Canada. JG MacIntosh, above n 8, 29–30 and 66–7.
³⁸ C Hale, above n 21, 222.
³⁹ This section draws heavily on J Payne, above n 30.
⁴⁰ Smith v Croft (No 2) [1988] Ch 144; J Payne, above n 30, 503.
⁴¹ [1975] QB 373, discussed in Ch 6 above under 6.3.2.
against the wrongdoers belongs to the company and should be treated as being equivalent to a claim by the company itself. The issue for the court is doing justice to the company, ie the shareholders as a whole in a solvent company, and not to the petitioning shareholder. This means that a shareholder should not have an indefeasible right to bring an action on the company’s behalf.

However, the effect of the judgment in Cutland is that the unfair prejudice remedy can be used by a minority shareholder to obtain a corporate remedy in response to a corporate wrong without going through the leave and notice requirements which are in place in a derivative action, and which are in place to deal with the concerns raised in Prudential. Cutland potentially means that the decision whether to litigate on behalf of the company can be delegated to individual minority shareholders, whether the company likes it or not and whether in the court’s view it would be better for the company as a whole for the action be brought or not. Nothing in Arden LJ’s judgment in Cutland suggests any limits to this principle. This is a very different role for the unfair prejudice remedy from that envisaged pre-Cutland, in which the remedy was developed by the courts as a personal remedy for shareholders, whether in response to personal wrongs or in relation to corporate wrongs.

So, if the change of role is to take place then it should only come at a price, the price being a recognition that substantive relief for the company under the unfair prejudice remedy must be denied in some circumstances in order to protect the company against malicious or misguided minority shareholders. However, problems run deep here. Unsurprisingly, it has been suggested that the tools which are available to the judges at present to screen out inappropriate actions under CA 2006, s 994 are inadequate for this task. These concepts, nonetheless, have been developed in a way which focuses very strongly on the petitioner’s position and whether his or her rights attaching to shares have been infringed.

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42 J Payne ‘Clean Hands in Derivative Actions’ (2002) 61 Cambridge Law Journal 76. It is inappropriate to allow a shareholder such as that in Barrett v Duckett to circumvent the procedural hurdles designed to protect the company by bringing an unfair prejudice petition to right the same wrong.

43 One control which would remain in place in the unfair prejudice petition is the need to show that the wrongdoers are in de facto control of the company: Re Legal Costs Negotiators Ltd [1999] 2 BCLC 171.


45 As Payne notes (above n 30, 504) when the House of Lords reviewed the unfair prejudice remedy in O’Neill v Phillips [1999] 1 WLR 1092 Lord Hoffmann emphasized this aspect, setting out two broad categories of cases in which the unfair prejudice remedy will be relevant: where the company’s controllers act in breach of the constitution or where the controllers’ behaviour is lawful in the sense that it does not breach the constitution but it nevertheless breaches some informal agreement between the shareholders. This was not intended to be an exhaustive list, but nevertheless it is telling that both of these categories involve resolutely personal wrongs to the shareholder.

46 See, for example, Re Saul D Harrison & Sons plc [1995] 1 BCLC 14.

47 J Payne, above n 30, 504.

48 These tools are, first, to require there to have been unfair prejudice to the petitioner and, secondly, to use their discretion under s 996 if they believe that the collective position has been too heavily compromised: J Payne, above n 30, 504–5.
Lord Hoffmann in *O’Neill v Phillips*, with its emphasis on contractualism, stresses the fundamentally promissory nature of the basis on which relief may be granted. This makes some sense given the courts’ view, pre- *Cutland*, of the unfair prejudice remedy as a personal claim to provide personal relief to the petitioner. However, clearly, this focus on inter-shareholder disputes provides no basis for determining whether or not a claim on the company’s behalf under CA 2006, s 996 would be in the collective best interests of the shareholders. The judges’ discretion under s 996 could be used to refuse a substantive corporate remedy if the shareholder’s claim was felt to compromise the collective position, but of course by that point the time and expense of litigation has already been expended. Instead, new tools will need to be developed to accomplish this task. But these tools are either not practical or far from ideal, in part because they involve introducing collective concepts such as ratification into what is at heart a personal claim, and in part because those collective concepts are themselves in a state of some disarray.

It can be seen then that importing a screening process into s 994 may be impractical. Fundamentally, the unfair prejudice remedy is a remedy for shareholders who have suffered personal harm in a form amounting to ‘unfair prejudice’. Essentially, the unfair prejudice remedy is the minority shareholder’s remedy. The derivative action is, simply, a different creature: its function is to enable minority shareholders, in limited circumstances, to pursue an action for harm done to the company and to recover on the company’s behalf. If the law is to retain coherence, it is important that this distinction is observed. In any event, a claimant cannot rely with any certainty on the unfair prejudice remedy as a means of exercising enforcement rights belonging purely to a company. There could still be circumstances where a shareholder might be unable to obtain relief under the unfair prejudice remedy where harm has been done to the company, for example where the petitioner has contributed to the situation with the result that the prejudice is not regarded as ‘unfair’, or where that relief is limited because of the petitioner’s conduct. There is no reason therefore why claims based on breaches of fiduciary duties by directors, where the claimant prefers to remain a shareholder, should be forced into the unfair prejudice remedy based on a different statutory test.

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49 One effect of the requirement of unfair prejudice may be to prevent some forms of corporate wrongdoing being litigated in some circumstances, for example where there is a breach by a director of his duty of care and skill and no gross mismanagement is involved. However, this operates in a manner unrelated to the issue of potential misuse of the jurisdiction by the petitioning shareholder. ibid.

50 J Payne, above n 30, 504–6 and Ch 5 above under 5.4.4.1 (A).

51 C Hale, above n 21, 221.


53 C Hale, above n 21, 222.

54 Although it is not necessary that a petitioner ‘come with clean hands’, his conduct may be relevant in deciding whether the relief should be granted and what the nature of such relief should be: *Re London School of Electronics* [1986] 1 Ch 211; *Jesner vJarrad Properties Ltd* [1993] BCLC 1032.

55 *Re London School of Electronics* [1986] 1 Ch 211.

56 L Kosmin, above n 32, 213.
Also, as will be seen below, derivative actions are often more focused than an s 994 petition and in that sense an easier subject of case management by the court. In short, the change of role envisaged in Cutland should be resisted, for the reasons set out above. The unfair prejudice remedy is clearly an attractive and convenient remedy for shareholders and its impact, particularly in private companies, should not be underestimated. However, reliance on the unfair prejudice remedy alone and the abolition of any form of derivative action could leave a gap in the enforcement mechanisms of corporate governance. It is the purpose of the following sections to show that, doctrinally, there are valid reasons for these two remedies to co-exist, not least from a practical viewpoint.

8.3.2 The unfair prejudice remedy and breaches of fiduciary duties

The main proposition advanced in this section is that founding a petition under s 994 upon breaches of fiduciary duty owed to the company is somewhat controversial. Following O’Neill v Phillips, it is firmly established that conduct will be unfair where it breaches the terms on which it was agreed that the company would be run. Unfairness can also arise where a power is exercised in a manner regarded by equity as contrary to good faith. The courts have found that breaches of directors’ duties can form the basis of a successful petition under ss 994–998, as can a director’s exclusion from management where an expectation of participation exists.

However, founding a petition under s 994 upon breaches of fiduciary duty owed to the company is somewhat controversial, not least because of two related issues. First, the petitioning shareholder normally seeks a personal remedy (such as an order that his shares be bought by the company or majority shareholders), where the wrong has been suffered by the company. Secondly, personal relief granted to a member as a result of a petition under s 994 based on a wrong done to the company seems to sit uneasily with the principle that a shareholder cannot ‘recover’ for damage, which is merely a reflection of the company’s damage. This principle was clearly established in Prudential Assurance Co Ltd v Newman.

57 S Deakin E Ferran and R Nolan, above n 52, 164. On the reasons which exist to justify the difference in approach between shareholders’ remedies in public and private companies, see BR Cheffins Company Law: Theory, Structure and Operation (OUP 1997) 463–71.
58 [1999] I WLR 1092 (HL).
59 Above n 29. The application of the unfair prejudice remedy in respect of breaches of directors’ duties is restricted, however, by the requirement that the conduct of the company’s affairs must be unfairly prejudicial. Thus conduct by a director in his personal capacity (ie stealing money from the company’s safe) cannot be remedied by a petition under s 994. R Hollington Minority Shareholders’ Rights (3rd edn Sweet & Maxwell 1999) 75 (renamed Shareholders’ Rights in the 4th edn (Sweet & Maxwell 2004).
60 See, for example, Re Phoenix Office Supplies Ltd [2002] EWCA Civ 1740.
61 See further HC Hirt, above n 29. For judicial consideration of this point, see Atlasview Ltd v Brightview Ltd [2004] All ER (D) 95 (Apr), [58]–[64].
Industries Ltd (No 2)⁶² and reconsidered and endorsed by the House of Lords in Johnson v Gore Wood.⁶³ It makes the company the primary agent to recover in such circumstances. This seems to be the right approach to protect, on the one hand, the defendant(s) from double recovery and, on the other hand, the interests of the creditors.⁶⁴ On the other hand, it was held in 2004 that the principle of reflective loss will not provide a bar to an action under s 994.⁶⁵

In addition, it has been suggested that the function of the unfair prejudice remedy with regard to directors’ duties should be very limited, as this undermines the policy on which the rule in Foss v Harbottle is based.⁶⁶ To reconcile such use of the unfair prejudice remedy with the principles of the rule in Foss v Harbottle, a petitioner should be required to demonstrate that his interests as a member are unfairly prejudiced as a result of the presence of two elements, namely, a director’s breach of duty and the majority’s ‘wrongful’ failure to initiate or prevention of litigation against the wrongdoer in circumstances where a derivative action is not available.⁶⁷ It was further suggested that it would generally only be possible to establish the second element if the wrongdoing director is also the majority or controlling shareholder. For this reason, it was concluded that the application of the unfair prejudice remedy with regard to breaches of directors’ duties would normally be confined to companies that are small in terms of the number of shareholders involved, particularly quasi-partnerships.⁶⁸ However, as Auld LJ pointed out in Phoenix Office Supplies Ltd v Larvin,⁶⁹ ‘it is important to keep in mind that s 459 [now CA 2006, s 994] is designed for the protection of members of companies’. This is a significant point to take into account when analysing and interpreting the unfair prejudice remedy. At any rate, it seems unlikely that it was the legislator’s intention to allow a shareholder without more to avoid the restrictions of the rule in Foss v Harbottle by presenting an unfair prejudice petition.⁷⁰

8.3.3 The Law Commission’s arguments

The Law Commission briefly considered unifying the remedies, exclusively in the context of channelling all proceedings into the unfair prejudice remedy. It

⁶³ [2001] 1 All ER 481 (HL). On the application of the principle including later developments, see Ch 7 above under 7.2.2.3.
⁶⁵ Atlasview Ltd v Brightview Ltd [2004] All ER (D) 95, (Apr) [58]–[64].
⁶⁶ HC Hirt, above n 29, 110.
⁶⁷ ibid.
⁶⁸ ibid.
⁶⁹ [2002] EWCA Civ 1740, [27].
rejected this option on three counts. It is worth looking carefully at the expressed rationales behind this position.

First, under the unfair prejudice remedy the applicant must show unfairly prejudicial conduct. In a derivative action, apart from the preliminary issue as to standing, the issue is whether the company has a cause of action against (say) a director. If the main complaint in the unfair prejudice remedy is that a party to the proceedings has committed a wrong against the company, the applicant, in order to succeed in his proceedings, must show not only that the company has a good cause of action in respect of this wrong, but also that the company’s failure to pursue this cause of action is unfairly prejudicial conduct. In order to bolster his case the applicant will probably include a number of other allegations of unfairly prejudicial conduct. In this way the issues in the unfair prejudice remedy, from a case management point of view, are less focused and, moreover, tend to proliferate. It follows that from ‘the point of view of limiting costs and making economical use of court time, it may be better if the issues are confined to the wrong to the company if this is the substantial complaint, and the issues would be so confined at trial if the proceedings were a derivative action’.⁷¹ In addition, the Law Commission points out that, if claims for wrongs to the company are combined with personal claims in an unfair prejudice petition, the proceedings will lack a clear focus from a case management point of view. This has adverse implications for limiting costs and the economical use of court time. There is also the problem that, if a shareholder decides to apply for a personal remedy (for example a buyout) under s 996, then, even though the complaints which he has proved could have led to relief in favour of the company, the court cannot on that ground alone refuse him personal relief. This means that the cause of action vested in the company is not affected by the judgment. Moreover, so long as the directors remain unwilling to enforce it, it will not be enforced unless a liquidator is appointed. The advantage of a derivative action, on the other hand, is that ‘it offers the possibility that, in appropriate circumstances, the company’s cause of action may be enforced without a liquidation’.⁷² Thirdly, ‘creditors are likely to be better off and treated equally if wrongs to the company are remedied by relief for the company, rather than its shareholders personally under section 459’.⁷³ The Commission also points to the duty of care and skill which, while it involves a wrong to the company, does not amount to unfairly prejudicial conduct unless there is serious mismanagement.⁷⁴ It is perhaps helpful at this point to turn to Table 8–1, which illustrates why the Law Commission’s position is correct.⁷⁵ As the table clearly shows, there are some striking differences between the two remedies as they are

⁷¹ Consultation Paper para 16.4.  
⁷² ibid.  
⁷³ ibid.  
⁷⁴ ibid.  
⁷⁵ It is worth emphasizing that Table 8–1 intends to be representative rather than exhaustive as it serves to illustrate the different perspective as between the two remedies.
Table 8–1. The derivative action vis-à-vis the unfair prejudice remedy

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<tr>
<th>Major differences</th>
<th>Derivative action</th>
<th>The ‘unfair prejudice’ remedy</th>
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<tbody>
<tr>
<td>Who may apply?</td>
<td>A shareholder</td>
<td>(1) A member or members</td>
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<td>(2) A person to whom shares have</td>
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<td></td>
<td></td>
<td>(3) The Secretary of State</td>
</tr>
<tr>
<td>On behalf of whom?</td>
<td>The company</td>
<td>Normally, a shareholder seeking to protect his rights as a member and not as agent for the companya</td>
</tr>
<tr>
<td>Who are the respondents?</td>
<td>Company is made a nominal defendant</td>
<td>Normally, controlling shareholders and/or directors</td>
</tr>
<tr>
<td></td>
<td></td>
<td>If the company is made a party, this is usually made on a nominal basis</td>
</tr>
<tr>
<td>Relief/ Main beneficiaries</td>
<td>The company b</td>
<td>Primarily concerned to protect members of quasi-partnership companies, who have taken their interest on the basis of legitimate confidences and expectationsc</td>
</tr>
<tr>
<td>Equity requirements</td>
<td>A shareholder may be prevented if there is evidence of ‘behaviour by the minority shareholder, which, in the eyes of equity, would render it unjust to allow a claim brought by the company at his insistence to succeed’ d</td>
<td>It is not necessary that a petitioner come with clean hands, but his conduct may be relevant in deciding whether the relief should be granted and what the nature of such relief should be e</td>
</tr>
<tr>
<td>Interim relief</td>
<td>The court can order interim relief</td>
<td>Usually, the court will not grant interim relief prior to a trial on the merits f</td>
</tr>
<tr>
<td>Can a former member sue?</td>
<td>A former member has no standing to sue, but he can nonetheless bring derivative actions in relation to wrongs which were done to the company before he became a member g</td>
<td>A former member has no standing to sue, even if the conduct which he wishes to complain about occurred while he was a member h</td>
</tr>
<tr>
<td>Discretion of the court</td>
<td>Must apply for permission to continue the claim and may not take any other step in the proceedings except where the court gives permission i</td>
<td>The court has discretion as to what type of relief should be granted, and even as to whether relief should be granted at all j</td>
</tr>
<tr>
<td>Ratification of a ratifiable wrong</td>
<td>Possible under certain circumstances k</td>
<td>Will have no bearing m</td>
</tr>
<tr>
<td>Group of companies</td>
<td>The idea of ‘double’ or ‘multiple’ derivative actions was rejected by the Law Commission n</td>
<td>The way in which the affairs of a subsidiary are conducted can constitute unfair prejudice with respect to the parent company’s affairs o</td>
</tr>
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</table>
Major differences

<table>
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<th>Derivative action</th>
<th>The 'unfair prejudice' remedy</th>
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<td><strong>Relevance of</strong></td>
<td>&quot;The shareholder will be allowed to sue on behalf of the company if no other remedy is available.&quot;</td>
<td>In few cases the court refused relief to a petitioner who was complaining about a situation, which he could remedy by using his own votes.</td>
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<td><strong>alternative remedies</strong></td>
<td></td>
<td></td>
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<tr>
<td><strong>Position in liquidation</strong></td>
<td>There is no need for such a device as the liquidator will have taken control of the company's affairs from the alleged wrongdoers</td>
<td>Not available</td>
</tr>
</tbody>
</table>

* Jones v Jones [2002] EWCA Civ 961. But note s 996(2)(c) under which the court has specific powers ‘to authorize civil proceedings to be brought in the name and on behalf of the company’.
* Shareholders only gain indirectly and to the extent that the value of their shares increased.
* Re London School of Electronics [1986] 1 Ch 211.
* The courts’ power to grant relief derives from the truth of the facts alleged being established: Re a Company (No 004175 of 1986) [1987] BCLC 574. This rule was not followed in Re Blue Arrow plc [1987] BCLC 585. However, the court may exercise its general jurisdiction and make an interim order for payment to the petitioners, for example, where the parties agreed that the affairs of the company had been conducted in a manner which was unfairly prejudicial and the court had no doubt that the petitioners would be entitled to an order for the purchase of their shares: Re Clearsprings (Management) Ltd [2003] EWHC 2516 (Ch), [43].
* Re a Company (No 005278 of 1985) [1986] 1 WLR 281. Prentice submits that the classes of persons entitled to invoke the unfair prejudice remedy should be extended to cover, at least, former members of the company, as unfairly prejudicial conduct which occurred when they were members of the company may only come to light after they have ceased to be so: DD Prentice, above n 10, 64. The Law Commission left this question open: Consultation Paper paras 20.34–20.38.
* CPR r 19.9 (3); now CA 2006, s 261(1).
* CA 2006, s 996 (formerly CA 1985, s 461). Note also that in practice a large number of the reported cases under the unfair prejudice remedy are the result of applications by respondents to strike out petitions under the inherent jurisdiction of the court.
* See discussion in Ch 3 above under 3.3.6.2.
* Report para 6.109 discussed in Ch 5 above under 5.4.4.1 (b) and is therefore not found in CA 2006, Pt 11.
* Gros v Rackind [2004] EWCA Civ 815.
* Barrett v Duckett [1995] 1 BCLC 243, 250 per Gibson LJ. For the Law Commission’s proposals, see Report para 6.15, discussed in Ch 3 above. Note, however, that this factor does not appear as part of the criteria for the grant of leave under CA 2006, s 263 (see discussion above under 4.3.5.5) under 3.4.2.
* For example, Re Legal Cost Negotiators Ltd [1999] 2 BCLC 17.
currently drafted and used, which, in turn, suggest that the derivative action has sufficient relevance to merit independent existence.

8.3.4 The question of relief

An important factor in considering the assimilation of the remedies is the question of relief. If the court is satisfied that a petition under s 994 is well founded, ‘it may make such order as it thinks fit for giving relief in respect of the matters complained of’ under s 996(1). Although there is a wide range of possible remedies under s 996(2), the most common relief in practice is a court order for the purchase of the shares of the aggrieved shareholder by other shareholders (generally but not necessarily by the majority) or the company itself.⁷⁶ Indeed, the unfair prejudice remedy has in essence become an exit remedy⁷⁷ which ensures that an aggrieved shareholder can leave the company with proper compensation.⁷⁸

There are at least two fundamental problems with this. First, shareholders in listed companies do not generally require a buyout order, because the market normally enables an exit with reasonable compensation (although the market rate may reflect breaches of directors’ duties). Therefore the most common remedy under s 996 is of very limited use for shareholders in such companies.⁷⁹ More generally, the exit option might be undesired by or unacceptable to shareholders who want to stay in the company. Recall that at heart the derivative action is a remedy for shareholders who want to remain in the company and challenge the wrongdoing by directors.⁸⁰ Thus an exit right is (at best) an appropriate and satisfactory remedy for a limited number of shareholders.⁸¹ Finally, selling the shares may not always be the best option, for example if an alleged wrongdoing has resulted in the depression of share values.

8.3.5 The ‘alternative remedy’ argument revisited

The Law Commission Report proposed that the court should take into account any alternative remedy to that available in a derivative claim before granting leave to pursue.⁸² While the Law Commission clearly has in mind the alternative of winding up, this might also include the unfair prejudice remedy since, in principle, a corporate remedy is obtainable if specifically sought. Although the

⁷⁶ CA 2006, s 996(2)(e), formerly CA 1985, s 461(2)(d).
⁷⁷ Report para 6.11 and Appendix J.
⁷⁸ In accordance with s 996(2) and the guidance highlighted in O’Neill v Phillips [1999] 1 WLR 1092. See also Report para 6.11 and Appendix J.
⁷⁹ Consultation Paper para 7.5.
⁸⁰ See Ch 5 above under 5.3.1.
⁸¹ H Hirt, above n 29, 110.
⁸² See Ch 3 above under 3.4.2.
availability of an alternative remedy is not conclusive on the issue of leave, if the unfair prejudice remedy were to be considered an alternative it would mean that, despite complying with notice, leave for the derivative action might be refused and the applicant would have to start again by issuing an s 994 petition. But this should not necessarily be the case. Interestingly, a principal argument raised in *Wilson v Inverness Retail*⁸³ (a Scottish case) relied heavily on the Court of Appeal decision in *Barrett v Duckett*.⁸⁶ The argument made was that shareholders are precluded from bringing an action on the company’s behalf where a remedy is available under the unfair prejudice petition. However, it is unlikely that *Barrett* will be interpreted as giving rise to such a strict rule, not least because the equitable character of the derivative action gives the court discretion to decide whether a derivative action should be allowed to proceed.⁸⁷ Moreover, the Court of Appeal in *Barrett* did not decide that a derivative action should be halted on the basis that a remedy was potentially available under the unfair prejudice remedy. Instead, the court decided (in what it regarded as the ‘unusual’ circumstances before it), that the better course of action was for the company to be placed in liquidation in order that the liquidator could decide whether legal action should be taken. It also found that the claimant was bringing the action for personal reasons and not bona fide for the benefit of the company. In addition, it is perhaps surprising that no reference was made in *Wilson* to another decision. In *Cooke v Cooke*,⁸⁸ a derivative action and an unfair prejudice petition were brought in respect of the substantially the same allegations. The derivative action proceedings were stayed because the court believed that the issues would be better dealt with under the unfair prejudice petition. It is clear, nevertheless, that what is unifying *Cook* and *Barrett* is the fact that the derivative action was halted because, when compared to another way forward (the unfair prejudice petition in *Cooke* and liquidator instigated litigation in *Barrett*), it is seen as a *less suitable* forum for considering the issues raised. This situation is far removed from the claim that the derivative action is barred where the conduct of which complaint is made would give rise to relief under the unfair prejudice remedy.⁸⁹

There is a further problem with the argument raised in *Wilson*. It assumes an equivalence between the remedies provided to the company where the derivative action is successful, and that available to the petitioning shareholder under the unfair prejudice remedy. While it is certainly the case that s 996 permits an action to be brought on the company’s behalf, as we saw, the remedy granted in

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⁸³ See generally, Consultation Paper para 5.19; Report para 6.15.
⁸⁴ And indeed this factor does not appear as part of the criteria for the grant of leave under CA 2006, s 263. See discussion above under 4.3.5.5.
⁸⁵ 2003 SLT 301 (OH).
⁸⁹ R Goddard, above n 87.
the vast majority of cases is the purchase of the petitioning shareholder’s shares by the company or the majority shareholders. Where the petitioner’s shares are bought, the remedy directly benefits the shareholder. Where an action is brought on the company’s behalf, the company directly benefits. This difficulty is only overcome if the above argument is taken to imply that the shareholder cannot bring an action on the company’s behalf because an equivalent provision exists under s 996.⁹⁰ So there is no surprise that, in Wilson, Lord Eassie rejected the above argument, while stressing that the purpose of the unfair prejudice remedy was to improve the minority shareholder’s position and that ‘[t]here is nothing in the terms of those sections… or their predecessors, which removes the derivative action from the aggrieved minority shareholder’s forensic arsenal’.⁹¹ This is clearly correct, as is the Lord Ordinary’s view that ‘Section 459 [now CA 2006, s 994] proceedings and the derivative action are not directly equivalent or co-extensive. The former is wider in scope’. This seems to confirm the view held in previous English decisions that, indeed, a factual overlap is not a functional equivalence.⁹² Although there may be more than one legal dimension of the same set of facts, as breaches of duty capable of generating a derivative action may form part of a pattern of unfairly prejudicial conduct, this should not disguise the fact that there is still, nonetheless, a difference of perspective, as the nature of a complaint based on unfairly prejudicial conduct and of one which might support a derivative action is different in the two cases, as is the relief sought.⁹³

8.3.6 Both remedies can operate together to ensure added value for the aggrieved shareholder and the company

To highlight the difference of the derivative action vis-à-vis the unfair prejudice remedy and the utility of the former consider the following scenario.⁹⁴ A minority shareholder of a company is seeking an order for the majority shareholder to buy his shares under s 996 where a significant loss has been sustained by the company as a result of the actions of the majority. Assume further that the company has been deprived of the benefit of, say, £10 million to which it would have been legally entitled but for the actions of the wrongdoer. This will obviously have an appreciable effect upon the value of the company and its shares. Therefore it is safe to say that if a legal adviser counsels the minority shareholder simply to present a petition under s 994 for its shares to be bought out by the majority, they would be doing their clients a great disservice, depriving it of the uplift in

⁹⁰ ibid.
⁹¹ 2003 SLT 301, 306 (OH).
⁹² C Hale, above n 21, 222.
⁹³ Re Charnley Davies Ltd (No 2) [1990] BCC 605, 625 per Millett J; Re BSB Holdings Ltd (No 2) [1996] 1 BCLC 155 per Arden J.
the capital value of the shares that would be secured as a result of a successful derivative action. Therefore the counsel of perfection would be to raise a derivative action and present a petition under s 994 for a wrongdoer ‘call’ order under s 996. The latter proceedings could be stayed pending resolution of the derivative action, which, if successful, would result in ordering the directors or controlling (offending) shareholders to reimburse the company in respect of that loss. The staying on the s 994 proceedings could then be lifted, safe in the knowledge that the capital uplift in the value of the minority shareholder’s shares secured as a result of the successful derivative action would be captured in any valuation of the shares ordered by the court as a result of any successful s 994 petition. In the example above, a successful derivative action clearly injects value into the hands of the company and a successful s 994 petition (in the main) injects value into the hands of the shareholder on the transfer of his shares. This fluidity highlights the difference between the two remedies, which though similar, can operate together to ensure added value for the minority/agrieved shareholder and the company.

Given the myriad of cases brought under the unfair prejudice remedy, it is perhaps unfortunate then that the usefulness of the derivative action as a remedy per se has been overlooked in recent times.

8.3.7 Comparative perspective

The unfair prejudice remedy, or variants of it, is part of the legislation in virtually all Commonwealth countries. That the derivative action is a different creature from the unfair prejudice remedy can also be seen in Canada and New Zealand. In spite of calls to unite the remedies, the two separate forms of action have been retained in these jurisdictions and it would be surprising, and out of tune with international developments, if the UK had chosen to depart from this position. More importantly, although there has not been an abundance of derivative action cases in Canada, there have been some important cases in which such proceedings prove justified as a technique of redressing serious corporate abuse. Canada has differed from England by its enactment of a virtual ‘bill of remedies’. The presence in Canada of the statutory derivative action and the oppression remedy

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95 ibid.
96 ibid 75.
97 As Lord Eassie stated in Wilson v Inverness Retail 2003 SLT 301, 308 (OH): ‘[the] consequent restoration to the company of its entitlement to its share of the profits…does not necessarily resolve the issues of unfairness to the minority extensively canvassed in the other [CA 1985, s 459 (now CA 2006, s 994)] proceedings. Reduction is not a remedy available in those proceedings.’
98 See above under 8.2.2.
99 Which includes the statutory derivative action, the oppression remedy (the equivalent to the unfair prejudice remedy), various restraining orders, an appraisal remedy, and, as in England, just and equitable winding up. For a survey of the scope and historical evolution of the oppression remedy under Canadian law, see S Copp and K McGuinness ‘Protecting Shareholder Expectations: A Comparison of UK and Canadian Approaches to Conduct Unfairly Prejudicial to Shareholders: Part 1’ (2000) 11 ICCLR 184.
(the parallel to the unfair prejudice remedy) has raised the question of the interrelationship between the remedies and in particular whether both personal and derivative actions are available under the oppression remedy. Arguably, the derivative action could exclusively be available under legislation pertaining to the statutory derivative action, and the oppression remedy should be linked solely to personal wrongs against minority shareholders.¹⁰⁰ The Dickerson Committee¹⁰¹ considered that the objective of the statutory derivative action was to remedy wrongs to the corporation, whereas the oppression remedy would generally be invoked by minority shareholders in a close corporation.¹⁰² The committee also recognized that in some situations actions may constitute a wrong to the company and a wrong to minority shareholders. In such a case ‘the aggrieved person may select the remedy that will best resolve his problem . . . [and] the courts should have very broad discretion, applying general standards of fairness, to decide these cases on their merits’.¹⁰³ The Dickerson Committee believed therefore that the two pieces of legislation could live side by side.

There is another crucial element to add to this. The unfair prejudice remedy is likely to remain a far more attractive and convenient remedy for shareholders in private companies. It offers advantages which should ensure that it remains the remedy of choice among shareholders. Yet, in spite of these factors, the evidence emerging in Canada¹⁰⁴ and more recently, Australia,¹⁰⁵ reveals a somewhat surprising practice: most of the decisions involving the statutory derivative action have involved closely held companies, a point which has left some scholars puzzled.¹⁰⁶ The Australian case is particularly interesting since the Australian government reports saw the statutory derivative action as an important means of maintaining investor confidence,¹⁰⁷ which might indicate that the primary role of the statutory derivative action was intended to be in large public companies, where shareholders were to act as watchdogs, guarding their investments by monitoring the actions of management. Instead, the statutory derivative action has been much more widely used in small proprietary companies, to overcome internal disputes. Whatever the case may be, it does mean, however, that the derivative action is not

¹⁰¹ RWV Dickerson JL Howard and L Getz Proposals for a New Business Corporation Law for Canada (Ottawa 1971).
¹⁰³ Dickerson Committee, above n 100, para 484.
¹⁰⁴ BR Cheffins, above n 8, 241–2.
¹⁰⁵ An empirical study of the Australian statutory derivative action between March 2000 (the introduction of new procedure) to August 2005 revealed that the vast majority of cases involved privately held companies (87.1% of cases). See I Ramsay and B Saunders ‘Litigation by Shareholders and Directors: An Empirical Study of the Statutory Derivative Action’ (2006) 6 JCLS 397, 420, Table 5.
¹⁰⁶ BR Cheffins, above n 8, 241–2.
¹⁰⁷ See CLERP Proposals for Reform, Directors’ Duties and Corporate Governance: Facilitating Innovation and Protecting Investors (Paper No 3 1997) 8.
solely a theoretical remedy in private companies. This is all the more important when we bear in mind that in the UK private companies constitute the vast bulk of companies\(^{108}\) and accordingly most minority shareholder legal actions tend to arise from the private end of the company spectrum. Also, from a practical viewpoint, a minority shareholder in a private company is better positioned to seek relief in the courts than is his counterpart in a listed company.\(^{109}\)

Turning to New Zealand, the ‘oppression remedy’ (the equivalent to the unfair prejudice remedy) is found in s 174 of the Companies Act 1993.\(^{110}\) It sits side by side with a statutory derivative action\(^{111}\) and is conceived as a supplement to, rather than a replacement of, other remedies which the shareholder might utilize.\(^{112}\) The liberal approach currently favoured in the interpretation of the oppression remedy has made it a very effective remedial tool for minority shareholders.\(^{113}\) Interestingly, the 1980 amendment to the Companies Act 1955 included the addition of paragraph (d) to the orders set out in s 209(2). Paragraph (d) provided that the court could make an order ‘authorising a member or members of the company to institute, defend, or discontinue court proceedings in the name and on behalf of the company’. However, it has been observed that this provision did not fit neatly within s 209. The oppression remedy is concerned with conduct of the company that adversely affects shareholders, rather than with wrongs done to the company itself.\(^{114}\) Thus, while the current liberalization of the courts’ attitude to the oppression remedy has enhanced the rights of shareholders to remedy

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\(^{108}\) At the end of 2005 public companies constitute only 0.5% of the register. See DTI Companies in 2005–2006, Table A2.

\(^{109}\) In a private company, a shareholder will usually find it considerably easier to establish ‘wrongdoer control’ (one of requirements under common law to bring a derivative action, see Ch 3 above under 3.3.2.1), because those who manage the business usually own a substantial percentage of the equity. This means that those in charge will often have the votes required to pass a resolution purporting to terminate any litigation. See further BR Cheffins, above n 57, 465–6, 305 and accompanying text; J Freedman and M Godwin ‘The Statutory Audit and Micro Company—An Empirical Investigation’ [1993] JBL 105, 108–9. But see also Breckland Group Holdings v London & Suffolk Properties [1989] BCLC 100.

\(^{110}\) In the past, the provision has been interpreted very narrowly, and only a handful of successful actions were brought between 1955 and 1981. However, amendments in the early 1980s have resulted in a significant liberalization of the courts’ approach to the oppression remedy. See M Berkahn ‘The Derivative Action in Australia and New Zealand: Will the Statutory Provisions Improve Shareholders Enforcement Rights?’ (1998) 10 Bond Law Review 74, 90; A Borrowdale ‘Shareholder’s Protection: The Section 209 Remedy—A Survey’ [1988] NZLJ 196.

\(^{111}\) Under s 165 of the Companies Act 1993.


\(^{113}\) M Berkahn, above n 110, 90.

\(^{114}\) This conclusion is supported by the fact that, during the period in which s 209(2)(d) was in force (1 April 1981–30 June 1994), there were no reported cases in which the court made such an order. See G Stapledon ‘Use of the Oppression Provision in Listed Companies in Australia and the United Kingdom’ (1993) 67 Australian Law Journal 575, 584–5; G Shapira ‘Minority Shareholders’ Protection—Recent Developments’ (1982) 10 New Zealand Universities Law Review 134, 159.
personal wrongs, its effect on shareholders’ ability to enforce corporate causes of action was far from significant.¹¹⁵

8.4 The Way Forward—Practical Steps

Thus far we have seen that there is clearly a case for having two separate statutory minority remedies. But that is not to say that the unclear interaction between the two remedies could not be improved. Two such ways are examined and assessed next.

8.4.1 Redressing the balance—the case for duality

There is no doubt that in some situations actions may constitute a wrong to the company and a wrong to minority shareholders.¹¹⁶ It is proposed therefore that to reflect the extent of inherent duality which seemingly exists within the majority of minority claims, an applicant should have the right to choose whether to bring a derivative action or proceedings under the unfair prejudice remedy, or cumulative claims under both.¹¹⁷ At the same time, in order to maintain consistency of principle, in such a case: (1) the aggrieved shareholder may select the remedy that will best resolve his problem; and (2) the courts should have very broad discretion, applying general standards of fairness, to decide these cases on their merits.¹¹⁸ For example, in cases where applicants seeking personal relief under s 996 (for example, a buyout order) in circumstances where the facts of the case would justify relief for the company (for example, the return of company property), the courts should have adequate powers to order issues to be tried separately and, in the case of duplication of remedies, to require election between them.¹¹⁹

It is further suggested that an entertaining of an s 994 petition, in a case where a derivative action could have been brought, should prima facie lie in fulfilling the screening tests as set out above as part of the FFM.¹²⁰ In appropriate cases,

¹¹⁵ M Berkahn, above n 110, 90.
¹¹⁶ So it may be difficult to determine whether an action should be personal or derivative in from. A classic example is Marx v Estates and General Investments Ltd [1976] 1 WLR 380.
¹¹⁷ This would be in line with the proposals of the Consultation Paper para 16.4. Griggs and Lowry have argued that a demarcation of actions would represent a valid alternative to a single form of action, suggesting that if there was any doubt as to the appropriate form of action ‘either party could seek directions of the court as to the appropriate course to take’. This solution would avoid any ‘radical reappraisal of the remedies’ while providing appropriate means of redress for minority shareholders. L Griggs and J Lowry, above n 100, 475–7.
¹¹⁸ cf Dickerson Committee Report, above n 101, para 484.
¹¹⁹ Consultation Paper para 16.6 and Slough Estates Ltd v Slough Borough Council [1968] Ch 299. Arguably, the court should also have the power to make an order in favour of the company, even where such an order is not sought by the applicant if that proves to be in the company’s best interests.
¹²⁰ See Ch 5 above under 5.4.4.3.
the courts would not have a problem in granting relief under s 996 against third parties,¹²¹ a relief which could equally be granted in a separate derivative action.¹²² Equally, where such a party, irrespective that he is a member, has personal rights against a company and these rights are invaded, courts would not have a problem finding that the rule in *Foss v Harbottle* is irrelevant, as observed (obiter dictum) by Lord Cooke in *Johnson v Gore Wood*.¹²³ In the later case situation, an s 994 petition would be entertained as a practical consequence that the threshold of the FFM would not fairly provide a remedy route.¹²⁴

### 8.4.2 A new test for obtaining costs orders

In parallel, a new test should be introduced for deciding the issue of funding the application, as explained elsewhere.¹²⁵ Pre-*Cutland*, the court had normally no jurisdiction in proceedings under the unfair prejudice remedy, unlike with derivative actions, to grant the petitioner in advance an order requiring the company to indemnify him as to costs.¹²⁶ Post-*Cutland*, it is clear that even in situations where the relief sought is claimed under s 994, the important factor for the purpose of determining where the costs should fall is *for whose benefit the relief is sought*. If, as in *Cutland*, it is the company then it is open for a shareholder to seek a recovery order against the company for payment to him of any cost incurred by him (essentially importing the *Wallersteiner* procedure into s 994 proceedings). But was the court correct? Or in a wider context, what should be the critical factor or factors that should determine whether a petitioner in an unfair prejudice petition should be entitled to an indemnity cost order?

A plausible alternative is that the critical factor should be *the nature of the wrong alleged* rather than the nature of the remedy sought, as in *Cutland*.¹²⁷ The reason is that under s 996 a petitioner who proves unfair prejudice that involves a wrong to the company can nevertheless obtain a remedy that is personal in form. And

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¹²¹ Equally, where the petitioner does not satisfy these tests, the court should strike out the petition, which in turn would force petitioners of unmeritorious claims to seek alternative settlement routes other than wasting the court’s time. This seems to have been the approach in *Stein v Blake* [1998] BCC 316, 317, where the claimant had brought a personal claim against the defendant, and on analysis of the facts, it was held that the proper claimant was the company itself, by then it was a matter exclusively for the liquidator to bring proceedings. See further J Mukwiri ‘Using Section 459 as an Instrument of Oppression?’ (2004) 25 Company Lawyer 282.

¹²² *Clark v Cutland* [2003] EWCA Civ 810.

¹²³ [2001] 1 All ER 481 (HL) discussed above under 7.2.2.3.

¹²⁴ See Ch 5 above under 5.4.4.3.


¹²⁶ *Re Sherborne Park Residents Co Ltd* [1987] BCLC 82; *Re a Company (No 005278 of 1985)* [1986] 1 WLR 281. The ban on using company funds with respect to the unfair prejudice remedy is not absolute, but the burden of justification for such expenditure will be a heavy one. Cogent and compelling evidence will be needed to justify such expenditure in advance. *Re a Company (No 1126 of 1992)* [1994] 2 BCLC 126.

¹²⁷ DD Prentice, above n 10, 67.
in such a case there is no reason for the company to indemnify him as to costs, because the relief is given directly to the member.¹²⁸ So that, in fact, the question for whose benefit the relief is sought for may not invariably help indicate the true nature of the action, as it can be personal, derivative, or even combined. This may ultimately blur (or in fact collapse) the distinction between personal and derivative actions, as there would be no substantial difference between them. As the law currently stands this is simply not the case.¹²⁹ But more importantly, where a petition under s 994 alleges wrongs that are both personal and derivative (as, indeed, seems to be the case in *Cutland*) should the indemnity costs order be also available? And if so, would the test of *for whose benefit the relief is sought* be of any assistance?

On the one hand, there is nothing in the nature of the *Wallersteiner* procedure that necessarily makes it unavailable where a shareholder joins a derivative action with a personal cause of action. At worst this would involve *de minimis* departure from principle.¹³⁰ On the face of it, there is no good reason why a petitioner who invests financial resources, time, and effort should not obtain an indemnity order as to costs, when the company and all other shareholders may enjoy the fruits of his initiative.¹³¹ The fact that the High Court judge in *Cutland* ordered a purchase by Mr Clark of Mr Cutland’s remaining shares (essentially a personal relief) did not seem to prevent the Court of Appeal from reaching its conclusion that the petitioner could nevertheless obtain an indemnity order as to costs as well as obtaining a remedy that is proprietary in nature. On the other hand, as a matter of policy this may entail an adverse effect on the use of derivative actions. It is likely that the possibility of obtaining such orders under unfair prejudice petitions would make (perhaps unintentionally) derivative actions even more unattractive than they already are. Shareholders would think twice before pursuing the separate and risky route of derivative actions, when it is possible for them now to obtain a similar recovery order for costs under s 996 when the relief sought is for the benefit of the company. The opportunity to gain an order for costs was up until now one of the very few advantages the derivative action had over the unfair prejudice remedy (from the viewpoint of funding).¹³²

Although in the unfair prejudice proceedings the company is not usually ordered to pay any of the costs, there are circumstances under which granting

¹²⁸ For example, where the unfairly prejudicial conduct takes the form of payment of excessive salaries, the court may order the oppressors to purchase the petitioner’s shares: *Re Abraham and Inter Wide Investments Ltd* (1985) 51 OR (2d) 460. Indeed, the High Court in *Cutland* ordered a purchase by Mr Clark of Mr Cutland’s remaining shares.

¹²⁹ DD Prentice, above n 10, 66.

¹³⁰ ibid 67.


¹³² Which, as shown in Chs 6 and 7, is a pivotal factor when a member has to decide whether to opt for litigation (whether by means of derivative actions or through the unfair prejudice remedy).
such an order would be justified. Since the relief sought in *Cutland* was sought for the benefit of the company, there was no good reason why a petitioner should not obtain an indemnity order with respect to costs.¹³³ But the test applied by the court tells us very little of the nature of the wrong alleged, when proceedings involve both personal and derivative causes of actions. Perhaps a better approach would be to require, in such circumstances, that both the nature of the wrong alleged and the nature of the remedy sought would be the critical factors that should determine whether a petitioner should be entitled to an indemnity order under unfair prejudice proceedings. This may help maintain the important distinction between personal and derivative actions.

Although it is now clear that it is possible to obtain a recovery on behalf of the company through an unfair prejudice petition,¹³⁴ it is, nonetheless, important as a matter of policy to maintain a doctrinal distinction between the two remedies. Otherwise, there is a danger that derivative actions will be made redundant. Accordingly, and in line with previous cases, it is important to require that both the nature of the wrong alleged and the nature of the remedy sought would be the critical factors that should determine whether a petitioner should be entitled to an indemnity order.¹³⁵ Only if the two are corporate in nature (ie if the action is, at least partly, derivative in form and for the benefit of the company) could the petitioner then obtain an indemnity order as to costs. This could work as a two-stage test. When deciding on whether to grant an indemnity costs order, the court should initially inquire as to whether the alleged wrongs are personal, derivative, or combined. If the answer is that they are either derivative or combined, then the court should proceed to the second question, namely what is the nature of the remedy sought (in other words, for whose benefit it is brought—that of the company or that of the member personally?). If it is mainly for the company, then, the argument runs, the company should be made to pay for it. Conversely, if the remedy is chiefly personal in form, then a member should normally be denied such costs orders as the rationale for such orders falls. This is a fairly straightforward test to apply. The court invariably deals with these questions in cases of this sort. More importantly, besides the positive practical effect this may have on the use of derivative actions, as explained above, this may also help maintain much clarity. When it is clear now that it is possible to obtain a recovery on behalf of the company through an unfair prejudice petition, it should be likewise clear under what circumstances an indemnity order should be available. If the test provided above is followed, it is submitted, the necessary consistency and clarity may be restored.

¹³³ And, of course, s 996(2)(c) (formerly CA 1985, s 461(2)(c)) expressly empowers the court to grant a successful petitioner an order authorizing a derivative action to be brought on behalf of the company.

¹³⁴ See also *Anderson v Hogg* 2002 SLT 354 (IH).

¹³⁵ *Re Charnley Davies Ltd (No 2)* [1990] BCC 605, 625 per Millett J; *Re BSB Holdings Ltd (No 2)* [1996] 1 BCLC 155 per Arden J.
8.5 Conclusion

It has been argued in this chapter that the derivative action has sufficient relevance to merit independent existence. The benefits of retaining the derivative action would outweigh the gains from dispensing the derivative action in favour of a single form of action under the unfair prejudice remedy. This could also leave a gap in the enforcement apparatus of corporate governance. Although the unfair prejudice remedy could be developed to meet this need, s 994 has had limited success in public companies. In addition, the unfair prejudice remedy itself is not beyond criticism, a point highlighted by the Law Commission. But irrespective of the ways in which the unfair prejudice remedy might be improved and despite the flexibility that the courts have demonstrated in relation to remedies once unfair prejudice has been established, fundamentally s 994 is a remedy for shareholders who have suffered personal harm amounting to unfair prejudice. The derivative action is simply a different apparatus: under a derivative action the issue for the court is doing justice to the company, ie the shareholders as a whole in a solvent company, and not to the petitioning shareholder.

There is no denying that as it presently stands the derivative action does not offer an effective or an attractive weapon to shareholders, as does the unfair prejudice remedy. Indeed, it seems the judiciary has been more willing to apply the unfair prejudice remedy to derivative-type actions, because they too wish to avoid the complexities surrounding derivative action litigation. But surely formulating a focused and effective derivative action remedy as put forward by the FFM above would also mean that (1) there would be less need to resort to the less adequate unfair prejudice remedy in cases where a corporate remedy in response to a corporate wrong is required; and (2) it could potentially enhance the capabilities of other mechanisms of accountability, not least s 994, as members may be encouraged to bring this claim rather than the wide-ranging proceedings under s 994, and accordingly this will shift some of the burden from the unfair prejudice remedy. Be that as it may, the presence of the unfair prejudice remedy and the unclear interaction between the two remedies could be improved. In order to remedy these defects two proposed ways were examined and assessed. If these measures are followed, perhaps the necessary consistency and clarity can be restored.