CHANCERY BAR ASSOCIATION
BERMUDA CONFERENCE
SHAREHOLDER DISPUTES PANEL

DERIVATIVE ACTIONS: A TOPICAL REVIEW

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10 May 2019

Introduction

1. This note addresses a number of topical issues relevant to derivative actions at common law, with particular reference to the 2018 introduction in Bermuda of a requirement to obtain the leave of the Court to continue a derivative action.

The requirement for leave: an overview

2. RSC O.15 r.12A came into force in Bermuda on 9 July 2018. The key provisions are contained in the first two subparagraphs, as follows:

> **15/12A Derivative actions**
> 12A (1) This rule applies to every action begun by writ by one or more shareholders of a company where the cause of action is vested in the company and relief is accordingly sought on its behalf (referred to in this rule as a "derivative action").
> (2) Where a defendant in a derivative action has entered an appearance, the plaintiff must apply to the Court for leave to continue the action.

3. This development provides a useful opportunity to consider the implications of the new leave provision, including those aspects which are not straightforwardly evidence from the drafting of the rule, together with other issues arising in relation to derivative actions in various jurisdictions.

The substance of the leave requirement (the "Leave Rule")

4. The Leave Rule is in identical terms to its Cayman Islands equivalent – also O.15 r.12A (of the Grand Court Rules). A requirement for permission to commence or continue a derivative action is widely found in common-law jurisdictions, and indeed in codified derivative action provisions. It is a "gatekeeper" provision, providing (by built-in judicial scrutiny) protection against frivolous or vexations shareholder claims. It also provides an early opportunity for the court to consider whether the claim is well-founded, including whether the plaintiff/claimant has a right *qua* shareholder to bring the claim at all.

5. In accordance with the general principle (also relevant to unfair prejudice/minority oppression claims) that a company's money should not be expended on disputes between its shareholders, it will not normally be necessary or appropriate for the company, as a nominal defendant, to participate actively where leave is sought.[1] However, there may be limited circumstances in which evidence from the company is pertinent; for

[1] *Roberts v Gill* [2009] 1 WLR 531 at [29].

example, providing a copy of its register of members where the locus standi of the petitioner as an alleged shareholder is in issue.

Multiple derivative actions ("MDAs")

6. An MDA is a creature of common law, permitting a minority shareholder of a parent company to pursue a cause of action vested in a subsidiary (or sub-subsidiary) of the parent.

7. The leading case is the decision of the Hong Kong Court of Final Appeal in *Waddington Ltd v Chan Chun Hoo Thomas* & ors.[2] Lord Millett's careful judgment in that case has been followed in a line of authorities, notably (in England) *Universal Project Management Services v Fort Gilkicker*[3] and *Abouraya v Sigmund*.[4] It has also been followed by the Royal Court of Guernsey in *Jackson v Dear*.[5]

Would Rule 12A apply to a Bermudian MDA?

8. Rule 12A applies to "*actions begun by writ by one or more shareholders of a company where the cause of action is vested in the company and relief is accordingly sought on its behalf*".

9. On the face of the drafting, therefore, it is not obvious that the Leave Rule would apply to an MDA as opposed to a "direct" derivative action.

10. Nevertheless, there is no good common-sense or policy reason why a "gatekeeper" provision should not apply to an MDA just as it applies to any other derivative action. Indeed, the authorities discourage an overly technical approach: a derivative action is merely a "*procedural device designed to prevent a wrong going without a remedy*" according to Briggs J in *Fort Gilkicker*.[6]

11. In an MDA case concerning a Cayman-incorporated company heard in the Grand Court of the Cayman Islands, *Renova Resources v Gilbertson*,[7] the court proceeded – sensibly, it is suggested - on the basis that the Cayman leave requirement applied in the same way it would apply to any other derivative action, and went on to determine the merits of the leave

[2] [2008] HKCU 1381; [2009] 2 BCLC 82.
[3] [2013] Ch 551.
[4] [2015] BCC 503.
[5] Guernsey Judgment 10/2013.
[6] [2013] Ch 551, at [24].
[7] [2009 CILR 268].

application. Acting Judge Foster (as he then was) referred extensively to *Waddington* and held, at ¶66, that:

"In my opinion, Lord Millett's analysis and conclusion also represents the law in this country and I can see no reason why, in appropriate circumstances, a multiple derivative action should not be permitted."

12. One would expect on the basis of *Renova* as persuasive authority to have a strong argument in favour of leave being both needed and, in appropriate cases, granted, for an MDA in the Bermudian jurisdiction.

13. So far as the BVI statutory position is concerned, there is clear authority from the Court of Appeal of the Eastern Caribbean in *Microsoft Corporation v Vadem Ltd* that S184(C) does not provide jurisdiction for the BVI court to grant leave for an MDA. What is not clear, however, is whether there remains any room for an MDA at common law in relation to a BVI company, notwithstanding the codification of the derivative action process – which presumably would not require leave, as the BVI's only leave provision is the statutory one.

14. This might not be as unlikely as it at first sounds; both *Waddington* (in Hong Kong) and *Fort Gilkicker* (in England) provide precedent in other jurisdictions for a common-law MDA surviving the codification of the single derivative action. In England the statutory and common-law routes are put on the same footing as to the permission procedure by the express terms of CPR 19(9)C; in Hong Kong the relevant statute has now been amended explicitly to provide for MDAs, as was already the case in the law of (at least) Australia, New Zealand, Canada and Singapore.

Granting MDA leave: the test

15. There is recent English authority on the test to be applied on an application for MDA leave, in the judgment of Morgan J in *Bhullar v Bhullar*.[8] He derived from the authorities a two-stranded test; the claimant must:
    a. Satisfy the court that there is a prima facie case that the relevant subsidiary company is entitled to the relevant claimed against the relevant defendant(s),[9] and
    b. That an independent board could (rather than would) reach the conclusion that it was appropriate to bring the proceedings.[10]

[8] [2016] 1 BCLC 106.
[9] At [20], applying the obiter remarks of the Court of Appeal in *Prudential Assurance Co v Newman Industries Ltd (No. 2)* [1982] Ch. 204, 221H-222B.
[10] At [38], applying *Airey v Cordell* [2007] BCC 785.

16. It is of interest to note that in applying limb (b), Morgan J took a different approach from that taken by the Cayman court in *Renova Resources v Gilbertson*, in which it was held (at 31) that, in the absence of an application for a costs indemnity from the company, the views of a hypothetical board were irrelevant.[11]

The international context for derivative actions

17. It seems clear that the Bermudian Leave Rule will apply procedurally even to derivative actions brought on behalf of overseas companies. "Company" includes an overseas company: Bermuda Companies Act 1981, ss2, 4(1).

18. A more difficult question arises in considering whether O.15 r.12A leave will be required where proceedings in the name of a Bermudian company are brought in an overseas court. The answer is that it depends whether the Leave Rule is to be construed as substantive or procedural.

19. Substantive matters, including those going to *locus standi*, are governed by place of incorporation of the relevant company: *Konamaneni v Rolls-Royce Industrial Power (India) Ltd*;[12] *Wong Ming Bun v Wang Ming Fan*.[13] It is to be noted that the *lex incorporationis* of the intermediate (holding) company is likely to be irrelevant in MDA, according to the reasoning in *Waddington* and *Fort Gilkicker*.

20. On the other hand, matters of pure procedure governed by *lex fori*: *Wong Ming Bun; Novatrust Ltd v Kea Investments Ltd*.[14]

21. Different leave provisions are to be analysed on their own terms. The statutory BVI leave provision[15] has been held to be substantive; in the context of the statute it is a condition precedent to the right to litigate: *Wong Ming Bun; Novatrust*.

22. On the other hand the Cayman leave rule (other than in the Hong Kong case *Zhi v SRK Consulting*,[16] which relied heavily on the authorities dealing with the materially different BVI provision) has been held to be purely

[11] In *Bhullar v Bhullar* there was a claim for a pre-emptive indemnity, but Morgan J refused it and his characterisation of the relevant test for the granting of permission to continue an MDA does not appear to be conditional on such a claim being made.
[12] [2002] 1 WLR 1269, [50].
[13] [2014] 1 HKLRD 1108.
[14] [2014] EWHC 4061 (Ch).
[15] S184C Business Companies Act 2004.
[16] HCA 2247/2014.

procedural and having no application to a foreign derivative action: *Top Jet Enterprises v Sino Jet Enterprises*.[17]

23. The Grand Court of the Cayman Islands in *Top Jet* found that the Cayman leave rule was properly to be construed as clearly contemplating and presupposing that the relevant derivative action was being conducted before the Grand Court, so that an application for leave to continue the action could be made within that action and the court could make orders regulating the future conduct of the action. Given that the (Bermudian) Leave Rule is identical to its Cayman equivalent, one would expect the *Top Jet* approach to be strongly persuasive in Bermuda.

24. These issues of jurisdiction will be of relevance both to cases brought in overseas courts in the name of a Bermudian company and cases brought in Bermuda in relation to an overseas company. In the latter category of case, it may be possible for a defendant to argue successfully for a strike-out, or a refusal of permission to continue the action in the forum, if a procedural failing in the place of incorporation gives rise to an absence of locus standi on the part of the plaintiff.

25. Any such argument must be raised positively by the defendant at an early stage; *Popely v Popely*[18] is English authority for the proposition that a plaintiff/claimant's derivative proceedings are not fatally flawed by a failure to prove its right to claim under the foreign law of incorporation, if the defendant has been prepared to proceed on the basis that the *lex incorporationis* is, for relevant purposes, the same as the *lex fori*.

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[17] [2018 (1) CILR 18].
[18] [2018] EWHC 276 (Ch).