

Disputes against Directors
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1. Breach of directors' duties can give rise to a wide range of potential disputes in many contexts. It is relevant to both litigators and corporate/commercial lawyers.
2. As a corporate/commercial lawyer advising companies, directors or shareholders either prior to setting up a venture or during its operation, you need to be aware of the difficulties that can arise from failing to appreciate who your client is and the separate interests of the company. This is of particular relevance in the context of joint ventures and closely held companies where the controlling shareholders/directors may commonly fail to appreciate that their interests are not necessarily the same as those of the company itself.
3. Companies are artificial bodies acting through human agents. Who are you advising? Is it the company itself, the majority shareholder, the directors in their capacity as such, or perhaps a minority shareholder? Getting that straight at the outset may help ensure that your client is advised appropriately. The client may not have a clear understanding of that issue themselves: it is up to you as their lawyer to ensure they have the correct focus and address the correct questions.
4. Similarly, as a litigator, it is important to understand the focus of any particular dispute in order to ensure that you identify the correct cause of action, that you have formulated your claim correctly and that you have the appropriate authority to act on behalf of your client.
5. In a short twenty-minute talk, it is not possible to cover the multitude of areas in which directors' duties may be relevant. I am going to touch on some recent case law in relation to one particular aspect of directors' duties: the exercise of directors' powers for a proper purpose. That was considered by the Supreme Court in Eclairs v JKX. I will briefly mention some of the areas in which claims against directors are relevant and who is the proper claimant (and defendant) for a claim. I will then touch on some common pitfalls in relation to claims against directors: in particular the role of the Company and the issue of privilege. Finally, I will look at claims by directors to obtain access to information.
6. You will see from this second slide that the issue of directors' duties can arise in a multitude of litigation contexts. That may include proceedings brought against the director by the company itself or an insolvency practitioner in an insolvency context. It might also involve third parties who have knowingly assisted a director who has acted in breach of duty or received money or assets misapplied by a director.
7. Such claims may also include claims by members of the company itself. These may be through the unfair prejudice remedy or, rather less commonly, for a just and equitable winding up or via a statutory derivative claim, which is now a part of the Gibraltar arsenal of remedies since the 2014 Companies Act. However, you should not forget that there may be a personal claim available for a member in certain contexts, if it can be shown that the

director's actions involves a breach of the contract of membership contained in the Articles of Association or, perhaps, a separate shareholders' or joint venture agreement.

8. The scope of directors' duties has now largely been codified under English law. They arise out of the directors' powers of control as fiduciaries. Whilst Gibraltar has not elected to codify directors' duties, English and other Common Law jurisdictions remain relevant as the English statutory duties are based on common law rules and equitable principles.
9. Turning to one aspect of directors' duties, let us look at the duty to act for a proper purpose. That is set out in section 171(b) of the English Companies Act 2006. This provides that a director must "*only exercise powers for the purposes for which they are conferred*". This is equivalent to the equitable rule that applies to trustees exercising discretionary powers. It has its origins in the equitable doctrine known as "*fraud on a power*".
10. In the context of companies, it has particular resonance where the exercise of a fiduciary power may affect the balance of control or economic benefit between shareholders. A prime example is the allotment of shares by the directors: Howard Smith v Ampol Petroleum [2964] 1 AC 821.
11. Another example of the use of this power can be seen in the recent Supreme Court decision of Eclairs Group Ltd v JKX Oil & Gas Plc [2015] UKSC 71.
12. In that case, two shareholders proposed a resolution for the removal of two directors and the appointment of three new directors who were associates of theirs. The Board issued disclosure notices seeking information about interests in shares and arrangements between the shareholders under s.793 CA 2006. The Articles of Association permitted the Board to issue a restriction notice if the board had reasonable cause to believe that the information provided was false or incorrect. The board used these notices to impose restrictions on the voting and transfer of the claimants' shares.
13. The Claimants sought declaratory relief that the restriction notices were invalid and of no effect on the basis that the power to impose such restrictions had been exercised for an improper purpose.
14. At first instance, Mann J granted the declarations, holding that the primary purpose in imposing restrictions had been to stop the claimants voting the shares at the AGM, rather than to ensure the provision of the information sought. That was beyond the purpose for which the power was conferred.
15. The Court of Appeal (Briggs LJ as he then was dissenting) allowed an appeal, on the basis that it was not material to the validity of the notices that the board's purpose had been to prevent the shareholder voting, suggesting that the proper purpose doctrine had no significant place in relation to the operation of Articles of Association.
16. The Supreme Court allowed the appeal, finding that the proper purpose doctrine did control the exercise of fiduciary powers. That was not necessary determined by the instrument creating those powers. If the instrument was silent, that would require an inference to be drawn from the mischief of the provision conferring it. That was based on the express

terms, their effect and the business context. In the present case, Article 42 was ancillary to the statutory power under s.793 CA 2006. Influencing the outcome of a shareholder vote was held not to be part of the proper purpose.

17. One question in particular potentially remains at large following JKX. Lord Sumption suggested that the Court might not intervene in the context of a situation where the directors had “mixed” purposes. He suggested, based on Australian authorities, that the exercise of a fiduciary power would be invalidated only if, “but for” the impermissible purpose, the power would not have been exercised.
18. This was not an approach which found favour with the rest of the Supreme Court. Lord Mance, for example, indicated that the exercise of the fiduciary power would be upheld only if the primary or principal purpose was a proper one. As Lord Mance indicated more recently in Willers v Joyce [2016] UKSC 43 at [140], this was likely to be easier to identify, as well as being more consistent with such guidance as authority afforded.
19. So, what are the consequences of this for lawyers advising in relation to the exercise of fiduciary powers by directors? They should consider carefully and identify the scope of the purpose for which the power is conferred before exercising that power. Where, in particular, the directors are exercising a power which could affect the balance of control or power in relation to a company, for example in the context of restricting voting rights or issuing shares, they may wish to take advice.
20. JKX is also an interesting case because of the claim was not brought as an unfair prejudice claim or a derivative action, but rather as a personal claim seeking declaratory relief and an injunction restraining the company from acting on the basis of the notice. It is important to remember that, save in exceptional cases, directors owe their fiduciary duties to the company and not to individual shareholders. However, where a right is vested in the shareholder personally, the rule in Foss v Harbottle will have no application. That might include enforcing a right provided for under the articles of association or a resolution to amend the articles of association. In JKX, that included the possibility to obtain an injunction to restrain what would otherwise be a breach of duty.
21. Other than a personal claim, a disgruntled shareholder might seek to pursue a claim under the unfair prejudice remedy or the statutory derivative claim or even, more unusually these days, through a just and equitable winding up petition. The different remedies available under those routes are likely to determine which is most attractive to a claimant. In cases of “corporate divorce”, the flexibility of the unfair prejudice remedy may be the most attractive option.
22. In advising the company, it is important to have regard to the different role that it may play under each of these forms of dispute. In shareholder disputes, the company is only a nominal party – the substantive dispute being between the members. As such, the company’s participation is limited to giving disclosure and, potentially, making submissions in relation to the form of any order to be made. It is likely to constitute a breach of duty for the directors to utilise company resources in defending the petition and an injunction may be granted in order to restrain the misapplication of funds in this way: Arrow Trading & Investments v Edwardian Group [2004] BCC 955

23. In relation to a derivative claim, on the other hand, there may be circumstances in which the company might play a more active role – particularly at the stage where permission is sought. Permission to pursue such a claim will be refused if no person acting in accordance with the duty to promote the success of the company would continue the claim, or where the proposed act or omission has been authorised or, where the cause of action arises from a past act or omission, where it was authorised before it occurred or has been ratified since it occurred. In those circumstances, the company may seek to explain why a claim has not been pursued. Furthermore, the Court will consider the views of other members – perhaps directing a meeting of independent members (if such exist).
24. Another issue which commonly catches out both corporate lawyers and litigators is the issue of privilege. Based on the authorities set out in this slide, you should be aware that advice taken and paid for by the company will not be privileged from disclosure against a minority shareholder bringing an unfair prejudice claim in relation to matters relating to the company’s administration. A failure to appreciate that the interests of the controlling shareholders and directors are not the same as those of the company itself may therefore lead to highly embarrassing advice being provided to a minority shareholder complaining about that very failing.
25. Finally, I should briefly touch on the common law rights of a director to obtain access to information and documentation legitimately required by the director in order to carry out their role as an officer of the company: Conway v Petronius [1978] 2 WLR 72. This is subject to certain limitations, in that the right cannot be exercised where the purpose of inspection is improper or to injure the company. It is, however, a potentially valuable weapon in the arsenal of a director who has been excluded from access to the business.
26. So, in conclusion, a couple of “takeaway” points for corporate advisors. Always consider carefully at the outset who your client is. Is it the company itself, the majority shareholder or perhaps the directors? Getting that clear at the outset, ideally in a clearly drafted engagement letter, will help limit your exposure and also help identify the interests that you have to protect with your advice. If advising the company, be aware that your advice may become disclosable in the event of a dispute.
27. For the litigators amongst you - again, consider carefully what form your proceedings might best take. Do you want the flexibility of the unfair prejudice jurisdiction with a view to corporate divorce, or would a narrower personal claim be more appropriate, allowing an attack on a particular resolution or transaction carried out by the directors. Again, consider your client’s (and the other side’s) ability to get hold of information either through the common law rights of a director or through the advice having been taken by the company. Do, in particular, have regard to the potential minefield of privilege.

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