PROTECTING THE MINORITY SHAREHOLDER

Introduction

It is one of the ironies of law that despite the fact that a company is a democratic organisation *par excellence*, tyranny in companies is so common. The problem that the law faces is trying to strike an acceptable balance between the right of the majority to have their way and the rights of a dissentient minority.

In a totally *laisser faire* system, the minority would just have to grin and bear it. This is the golden rule in action — he who has the gold makes the rules. Until 1948, the only "remedy" — if one could call it that — which a minority shareholder had in the case of major disagreement with the majority was to have the company wound up. In many cases, the cure was worse than the disease, involving as it did the termination of the business. In practice, a winding up might not be feasible where the directors (including the minority shareholder) had given personal guarantees for the company's debts.

The UK Companies Act 1948 introduced the "alternative remedy" in section 210[1]. This gave the court the power to grant relief other than winding up in a case where a winding up was justified under the "just and equitable" rule. The utility of this section was such that it was gradually widened, so that the current UK sections[2] no longer require the behaviour of the majority to be "oppressive" but only "unfairly prejudicial". The link with winding up has also been severed in that it is not necessary to show that it would be just and equitable to have the company wound up. A similar liberalisation can be seen in the equivalent Australian provisions[3].

Singapore's section 216 traces its history back to 1967, when the present Companies Act came into force[4]. There is no requirement in section 216 that it be just and equitable for the company to be wound up before relief

1 On the recommendation of the Cohen Committee. See *Report of the Committee on Company Law Amendment 1945* (Cmnd 6659).

2 Sections 459 to 461 of the Companies Act 1985. This section was introduced in its present form as section 75 of the Companies Act 1980, following recommendations of the Jenkins Committee; see *Report of the Company Law Committee 1962* (Cmnd 1749), paras 199–212.

3 Now section 260 of the Corporations Law 1989.

4 According to Pillai, the section was modelled on section 218 of the Ghana Companies Code 1961: see *Sourcebook of Singapore and Malaysian Company Law* (2nd ed, 1986), p 1036. The author reproduces Gower's comments on the section. Malaysia's section 181 is almost identical.

can be given. Instead of the formula "oppressive" used in the contemporary UK legislation, section 216 uses four different tests: "oppression", "disregard of interests", "unfair discrimination" and "prejudice". When the section was amended in 1984, it was originally proposed to replace "oppression" with the English "unfairly prejudicial" formula. This proposal was however dropped. The 1984 amendment[5] did introduce what is now section 216(2)(c), which actually deals with a totally different problem, ie, derivative actions.

Given the difference in wording between the UK, Australian and Singapore provisions it is wise to keep in mind Lord Wilberforce's admonition in *Re Kong Thai Sawmills (Miri) Sdn Bhd*[6] that the section should be construed according to its own terms. Australian, English and other Commonwealth cases may be useful as analogies, keeping in mind the sometimes more restrictive wording of the sections considered.

The difficulty with a section like this is to formulate some coherent approach to its application[7]. One possibility is to analyse the section into "limbs" and try to fit each case within a particular limb. It is suggested that a more useful approach would be to look at the big picture and interpret the section purposively in the light of the mischief that it is designed to cure.

The mischief

The problem with companies, as with other corporate organisations, is that the members do not always see eye to eye. In the normal case, the will of the majority prevails. A person who takes a minority stake in a company does so on the understanding that he may be outvoted when disagreements arise. It is for this reason that a minority stake in a company is often valued at a discount. However, there is a thin but substantial line that the majority cannot cross. Majority rule is one thing; oppression of the minority is quite another. As Lord Wilberforce said in *Re Kong Thai Sawmills (Miri) Sdn Bhd*[8]:

> "The mere fact that one or more of those managing the company possess a majority of the voting power and, in reliance upon that power, make policy decisions, with which the complainant does not agree, is not

5 See the Companies (Amendment) Act 1984 (No 15/84).
6 [1978] 2 MLJ 227 (Privy Council on appeal from Malaysia).
7 Neither of the two recent Singapore cases on section 216 gives much guidance as to the general approach to interpretation. See *Kuah Kok Kim* v. *Cheong Lee Leong Seng Co (Pte) Ltd* [1991] 2 MLJ 129 (Court of Appeal) and *Re Gee Hoe Chan Trading Co Pte Ltd* [1991] 3 MLJ 137 (High Court).
8 *Ibid*, at page 229.

> enough. Those who take interests in companies limited by shares have to accept majority rule. It is only when majority rule passes over into rule oppressive of the minority, or in disregard of their interests, that the section can be invoked."

Thus, section 216 is designed to allow the court to strike a fair balance between majority rule and minority rights.

Comparative approaches

The term "oppression", although a convenient label, is not completely accurate. The term has over the years acquired a rather restrictive meaning through judicial interpretation. Section 216 covers not only "oppression", but also "disregard of members' interests", "unfair discrimination" against members and "prejudice" to members. This was legislatively recognised when the marginal note was amended in 1987 (at this author's suggestion) to indicate the broader nature of the remedy. The marginal note was amended from "Remedy in cases of oppression" to "Remedy in cases of oppression and injustice". This was a recognition that the section covered more than just oppression[9]. An examination of the UK and Australian judicial approaches is useful in formulating our own approach to the application of section 216.

The approach of the English courts to their section 459 has been set out by Peter Gibson J in *Re A Company (No 005134 of 1986), ex p Harris*[10]:

> "(1) The test of unfair prejudice is objective. (2) It is not necessary for the petitioner to show bad faith. (3) It is not necessary for the petitioner to show a conscious intention to prejudice the petitioner. (4) The test is one of unfairness, not unlawfulness. Counsel for the respondents, however, has submitted that because the test is objective it was irrelevant that the respondent may have acted for an improper purpose or with an improper motive. I do not doubt that if the objective bystander observes unfairly prejudicial conduct by a respondent the fact that the respondent had a proper purpose and a proper motive will not prevent that conduct from falling within the section. But if the objective bystander observes that the conduct of the respondent was for an improper purpose or with an improper motive, that may well be a relevant consideration in determining whether the conduct is unfairly prejudicial."

9 See *Report of the Select Committee on the Companies (Amendment) Bill 1986*, page B90 column 180 paras 374 and 375.

10 [1989] BCLC 383, 389–390 (High Court, England).

The same judge also expounded the principles on which section 459 would be applied in *Re Ringtower Holdings plc*[11]:

> "Under section 459(1) the condition that must be satisfied if the court is to give relief under section 461 is that the company's affairs are being or have been conducted in a manner which is unfairly prejudicial to the interests of some part of the members, including the petitioners, or that any actual or proposed act or omission of the company (including an act or omission on its behalf) is or would be so prejudicial. Four points on the wording of the section are to be noted:
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> (1) the relevant conduct (of commission or omission) must relate to the affairs of the company of which the petitioners are members;
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> (2) the conduct must be both prejudicial (in the sense of causing prejudice or harm) to the relevant interests and also unfairly so: conduct may be unfair without being prejudicial or prejudicial without being unfair and in neither case would the section be satisfied;
>
> (3) the test is of unfair prejudice, not of unlawfulness, and conduct may be lawful but unfairly prejudicial;
>
> (4) the relevant interests are the interests of members (including the petitioners) as members, but such interests are not necessarily limited to strict legal rights under the company's constitution, and the court may take into account wider equitable considerations such as any legitimate expectation which a member has which go beyond his legal rights.

The Australian approach to their section has been set out in two cases. In *Phosphate Cooperative Co of Australia Ltd* v. *Shears*[12], Beach J quoted with approval the following dicta of Brennan J in *Wayde* v. *New South Wales Rugby League Ltd*[13]:

> "[The section] requires proof of oppression or proof of unfairness: proof of mere prejudice to or discrimination against a member is insufficient to attract the court's jurisdiction to intervene. In the case of some discretionary powers any prejudice to a member or any discrimination against him may be a badge of unfairness in the exercise of the power but not when the discretionary power contemplates the effecting of prejudice or discrimination. It is not necessary now to decide whether

11 (1989) 5 BCC 82, 90 (High Court, England).

12 (1987) 12 ACLR 649, 653 (High Court of Australia). The section considered is the predecessor of the present section 260 of the Corporations Law 1989. The two sections are similar.

13 (1985) 10 ACLR 87 (High Court of Australia).

> "oppressive" carries in the context of section 320 the meaning which it carried in the context of the statutory precursors of section 320. At a minimum, "oppressive" imports unfairness and that is the critical question in the present case."

In *Morgan* v. *45 Flers Avenue Pty Ltd*[14] Young J said:

> ". . . it has been accepted that one no longer looks at the word 'oppressive' in isolation but rather asks whether objectively in the eyes of a commercial bystander, there has been unfairness, namely, conduct that is so unfair that reasonable directors who consider the matter would not have though the decision fair ... in my view a court now looks at [s 320(2)(a)] as a composite whole and the individual elements mentioned in the section should be considered merely as different aspects of the essential criterion, namely commercial unfairness".

It will be noted that the trend seems to be to construe the provisions broadly and not quibble over particular words in the definition. This, it is suggested, is the correct way to apply the sections; look at the whole forest, not at the individual trees. Our section 216 is even wider than section 459 of the UK Companies Act 1985 and section 320 of the Australian Companies Act 1981. Parliament has recognised this by amending the marginal note. It is suggested that judges can take this cue to interpret section 216 more widely to give remedy to a shareholder who is treated unfairly.

Legitimate expectations

The problem is that "unfairness" cannot be gauged in a vacuum. There has to be some standard by which to judge whether particular behaviour is or is not unfair to a minority shareholder. We start with the dicta of Lord Wilberforce in *Ebrahimi* v. *Westbourne Galleries*[15]:

> "[A] limited company is more than a mere legal entity, with a personality in law of its own: . . . there is room in company law for recognition of the fact that behind it, or amongst it, there are individuals, with rights, expectations and obligations inter se which are not necessarily submerged in the company structure . . . [the just and equitable rule] does, as equity always does, entitle the court to subject

14 (1986) 10 ACLR 692, 704 (Supreme Court of New South Wales).

15 [1973] AC 360, 379 (House of Lords). Although he was considering the "just and equitable" rule for winding a company up, his words are equally apt in a section 216 context; see *Re Novabron Pty Ltd (No 2)* (1986) 11 ACLR 279, 292 (Supreme Court of Queensland) per Derrington J.

> the exercise of legal rights to equitable considerations; considerations, that is, of a personal character arising between one individual and another, which may make it unjust, or inequitable, to insist on legal rights or to exercise them in a particular way."

In *Re Posgate & Denby (Agencies) Ltd*[16] Hoffmann J said:

> "[T]he concept of unfair prejudice . . . enables the court to take into account not only the rights of the members under the company's constitution, but also their legitimate expectations arising from the agreements or understandings of the members inter se. There is an analogy in Lord Wilberforce's analysis of the concept of what is 'just and equitable' in *Ebrahimi* v. *Westbourne Galleries Ltd.*"

In a similar vein are the dicta of Derrington J in *Re Novabron Pty Ltd (No 2)*[17]:

> "Further for the determination of the rights, expectations and obligations inter se of the persons behind it, a company is more than a mere judicial entity, and those rights are not necessarily merged into its structure: *Ebrahimi* v. *Westbourne Galleries Ltd.* Although that case was decided on the "just and equitable" provision, in this respect precisely the same considerations apply to section 320, where the relationship of those persons *inter se* is the foundation of the remedy."

Thus, in deciding to grant relief, the court should take into account not only members' legal rights but also their legitimate expectations[18].

It is submitted that what the legitimate expectations of minority members are is a question of law to be determined objectively considering the nature of the company involved. Not every company is the same. The legitimate expectations of the members of a large public company may well be different from the legitimate expectations of a member of a small private family company. A person who invests money in a public company cannot legitimately expect to have a say in the running of the company unless he makes a take-over bid. On the other hand, where a partnership is incorporated (as in *Ebrahimi's case*) each partner can legitimately expect to play a part in management.

16 [1987] BCLC 8, 14 (High Court, England).
17 (1986) 11 ACLR 279, 292 (Supreme Court of Queensland).
18 See *Re Posgate & Denby (Agencies) Ltd* [1987] BCLC 8, 14 (High Court, England) per Hoffman J; *Re Ringtower Holdings plc* (1989) 5 BCC 82, 90 (High Court, England) per Peter Gibson J.

The circumstances in which the aggrieved person became a member are important in determining what his legitimate expectations are: see eg *Tay Bok Choon* v. *Tahansan Sdn Bhd*[19]; *Re Dalkeith Investments Pty Ltd*[20]. Take for example the question of board representation. Normally a minority member has no right to appoint any directors. But the circumstances surrounding his investment (as in *Tay Bok Choon* v. *Tahansan Sdn Bhd*[21]) or the way the company has been run (as in *Re Gee Hoe Chan Trading Co Pte Ltd*[22]) may give rise to such an expectation.

Although it is not possible to set out exhaustively what the legitimate expectations of minority members are, the following are offered as speculations:

(1) It is a legitimate expectation on the part of members of a company that the company should be run in the interest of all the members and not only of the majority: see *Re H R Harmer*[23]; *Re Coliseum Stand Car Service Ltd*[24]; *Re City Meat Co Pty Ltd*[25]. This principle is so obvious that it hardly needs authority.

(2) It is a legitimate expectation of members of a company that they should receive a fair share of the profits of the business[26]. It is clearly unfair to the minority if the majority receive large sums of money from the company while they get nothing: see *Re A Company (No 00370 of 1987), ex p Glossop*[27] where Harman J said:

> "It seems to me that it is important to remember that a company is simply a vehicle for carrying on business for the benefit of all members. One of the major benefits to shareholders, ie members, in a company is, or ought to be, the payment of dividends. Undoubtedly, directors have express power to put a ceiling on the amount of dividends paid in almost all (and certainly in this company's) articles. Undoubtedly, directors are responsible for the commercial affairs of the company and should not be forced to pay out moneys which may leave them at risk of trading while insolvent or incurring debts which the company cannot easily meet; that would put directors at peril of committing, at worst, criminal offences

19 [1987] 1 MLJ 433, 435 (Privy Council on appeal from Malaysia).
20 (1984) 9 ACLR 247, 252 (Supreme Court of Queensland).
21 *Ibid.*
22 [1991] 3 MLJ 137.
23 [1958] 3 All ER 689 (Court of Appeal, England).
24 [1972] 1 MLJ 109 (High Court, Malaysia).
25 (1983) 8 ACLR 673 (Supreme Court of South Australia).
26 *Re Gee Hoe Chan Trading Co Pte Ltd* [1991] 3 MLJ 137 (High Court, Singapore).
27 [1988] BCLC 570, 576 (High Court, England).

and, at lower levels, actions which would be wrong and could be the subject of censure. Undoubtedly, it must be extremely difficult in any case to prove that more dividend should be paid out than has been paid out. But as a matter of concept, it seems to me, it must be capable of being an improper conduct of the affairs of a company to retain in the company for the greater growth and glory of the company profits which could with entire propriety and commercial ease be paid out to members in dividends for the benefit of members."

The failure to declare dividends may amount to unfairness to minority members, especially when contrasted to the benefits the majority obtained from the company: *Re Sam Weller & Sons Ltd*[28]. It is no defence to say that the majority are equally prejudiced by the failure to declare dividends if they are themselves drawing remuneration from the company in some other way[29].

(3) It is a legitimate expectation of a member of a company that the directors will act honestly and diligently and will account to the members for their stewardship of the company. Directors are stewards and are accountable to the shareholders for their stewardship of the company's assets: *Caparo Industries plc* v. *Dickman*[30]. It is for this reason that by convention directors are required to answer members' questions at general meetings of the company. A member of a company is entitled to expect that the directors will act honestly and diligently in the discharge of the duties of their office. If there are grounds to a suspect a breach of fiduciary duty or negligence, it is unfair to the minority members if the directors consistently refuse to provide them with evidence that the company is indeed being properly run or if the directors use their majority voting power to prevent an action being brought against them. This may justify the court in granting an order under section 216(2)(*c*), to authorise proceedings to be brought by the minority in the company's name[31].

The relief

The great advantage of section 216 is that it gives the court an unfettered power to tailor the remedy to meet the mischief. Although very often winding up is asked for as a relief, a section 216 petition is not a winding up petition: *Kuah Kok Kim* v. *Chong Lee Leong Seng Co (Pte) Ltd*[32]. This

28 [1990] BCLC 80, 88 (High Court, England).
29 *Re Gee Hoe Chan Trading Co Pte Ltd* [1991] 3 MLJ 137 (High Court, Singapore).
30 [1990] 1 All ER 568, 583 (House of Lords).
31 This would amount to a statutory derivative action and would avoid the problems inherent in the rule in *Foss* v. *Harbottle* (1843) 2 Hare 461.
32 [1991] 2 MLJ 129 (Court of Appeal).

may have some practical advantage, as the advertisement of a winding up petition often has a detrimental effect (to put it mildly) on a company's business. Furthermore, the standard of unfairness required would vary according to the nature of the remedy sought. Obviously, a high degree of unfairness would have to be shown to justify winding up a company, whereas a lesser degree would suffice if all that was desired was, say, to prevent the directors from abusing their powers[33].

A few points should be noted. Firstly, section 216 should not be used as a panacea for all ills where other sections may provide a more specific remedy. For example, an injunction may be obtained under section 409A, irregularities may be cured under section 392, relief from liability may be obtained under section 391, etc. Secondly, although theoretically the court can make any order under section 216, the practicality of enforcement must be considered. To "regulate the conduct of the affairs of the company in future" under section 216(2)(*b*) sounds fine in theory, but is impracticable unless the judge wants to run the company himself.

Thirdly, the cost of litigation means that a minority shareholder is not likely to seek relief unless matters are very serious indeed. In such a case, very often the only practical solution is a divorce. Thus, for example, in *Re Gee Hoe Chan Trading Co Pte Ltd*[34] the petitioners asked for board representation, a buy-out (ie, that the respondents should purchase their shares) or a winding up. Under the circumstances, the judge concluded that board representation was out of the question given the animosity that existed between majority and minority. He was inclined to order a buy-out, but since the respondents were unwilling, the company was ordered to be wound up. Often, this is the only realistic order to make. Anything short of a divorce and clean break is apt to mean that the court will get repeat customers in future. Section 216 is more flexible than a winding up petition in achieving a clean break. The court could order a buy-out if the majority has the means to effect one. If the company is solvent, a share buy-back under section 216(2)(*d*) will let the minority out without killing the business. Winding up can be granted if that is the only practical remedy.

Conclusion

Minority shareholders have a lot of rights in theory; the problem in practice is enforcing them. The cost of doing so deters all but the very

33 As for example in *Re S Q Wong Holdings Pte Ltd* [1987] 2 MLJ 298 (High Court, Singapore).
34 [1991] 3 MLJ 137 (High Court, Singapore).

wealthy or the very bitter. The lot of the minority shareholder may be ameliorated if courts are willing to take a more liberal view of section 216. The mere existence of the remedy and the willingness of the courts to enforce it will be sufficient deterrent to the autocratic so that needless litigation can be avoided.

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