ROYAL COURT
(Samedi Division)

18th December, 1997

Before: Sir Philip Bailhache, Bailiff

Between:	**FLOOR KHAN née Osman**	**First Plaintiff**
	SHEIKH ZAHER BIN HAMAD AL-HARTHY	**Second Plaintiff**
And:	**LEISURE ENTERPRISES (JERSEY) LIMITED**	**First Defendant**
	ALAN OKE DART	**Second Defendant**
	MICHAEL HENRY RICHARDSON	**Third Defendant**

Application by Second and Third Defendants to strike out the Plaintiff's Order of Justice

Advocate M.J. Thompson for the First and Second Plaintiffs
Advocate M. St. J. O'Connell for the Second and Third Defendants

THE BAILIFF: This is a summons issued by the Second and Third defendants ("the applicants") seeking to strike out an Order of Justice on the grounds that it discloses no reasonable cause of action, is frivolous and vexatious, and is an abuse of the process of the Court. The Order of Justice was served on the applicants on 7th February, 1997. The plaintiffs claim between them to hold a minority of the shares in a Jersey registered company, Leisure Enterprises (Jersey) Ltd. ("the company"). The plaintiffs have joined the company as first defendant. The applicants, who are partners in the legal firm of Bedell and Cristin, are and were at all material times directors of the company.

The brief history of the matter is that on 20th September, 1993 all the shareholders of the company wrote to the applicants' firm giving directions for various share transfers and concluding with the following instructions:

> *"Finally we confirm our joint irrevocable instructions to you to hereafter act in your capacity as the controlling directors of the Company solely in accordance with the directions of the holders for the time being of the majority of the shares in the Company.*

Please address your reply to us c/o Julian Holy, 31 Brechin Place, London SW7 4QD, England."

The instructions were, as I have stated, signed by or on behalf of all the shareholders.

On the same day the first plaintiff granted an irrevocable proxy to Ashley Guarantee Ltd. over the shareholding in the company registered in her name *"with intent that Ashley Guarantee shall hereafter have and be entitled to exercise in its absolute discretion all of the rights to vote in any general meeting of the company in my name and on my behalf".*

Again on the same day, 20th September, 1993, an agreement was executed by all the company's shareholders and Kamal Mustafa Khan relating to the administration of Las Colinas de Marbella SA ("Las Colinas"), a company registered in Spain, and the appointment of new officers for Las Colinas, including a nominee of the first plaintiff.

On 4th February, 1994 Alfonso Lopez-Ibor, a Spanish lawyer, wrote by fax to the applicants' firm sending a draft power of attorney relating to the sale of shares in Las Colinas which were owned by the company.

On 7th February, 1994, Julian Holy, an English solicitor, wrote from the address previously given, 31, Brechin Place, London, to the applicants' firm in the following terms:

"Leisure Enterprises (Jersey) Limited

I have received a copy of Mr Lopez-Ibor's fax to you of the 4th of February under cover of which he encloses a form of the power of attorney which is required for the sale of the shares of Las Colinas de Marbella SA owned by the above company.

In accordance with the instructions of the owners of the majority of the shares in the above company, I confirm that it is entirely in order for you to comply with Mr Lopez-Ibor's request and to issue the power of attorney which I should be grateful if you would kindly arrange to do as soon as ever possible.

As ever, your assistance in this matter is much appreciated."

On 9th February, 1994 the applicants held a meeting of the board of the company, resolved to execute the power of attorney, and did so. It provided, *inter alia*, that Mr. Lopez-Ibor and another Spanish lawyer *"may exercise, in the name and stead of [the company] the following faculties ... (a) ... sell to [Beltrana SA] ... (11,880) ordinary shares [in Las Colinas] for the consideration and terms and conditions as the attorneys may consider appropriate ..."*

In April 1995 the first plaintiff wrote twice to the applicants' firm requesting certain information relating to the company's dealings. In February 1997, without any letter before action, proceedings were instituted.

The plaintiffs alleged that Las Colinas owned a site in Spain valued at about £14 million, and that, in reliance upon the power of attorney executed by the applicants, on or

about 14th June, 1995 the Spanish lawyers transferred the issued share capital of La Colinas to a Gibraltar company known as Beltrana Properties Ltd. for no consideration. The plaintiffs alleged that the applicants acted in breach of duty, and/or negligently, and/or in breach of trust, and claimed, inter alia, damages for the company. They also claimed alternatively on the basis of "unfair prejudice" pursuant to the Companies (Jersey) Law 1991 ("the 1991 Law").

Further pleadings were filed and on 5th June, 1997 this summons was issued. On 15th October, 1997 the applicants' outline submissions were sent to the plaintiffs. The outline submissions made it clear that the principal ground of attack was that the action was precluded by the rule in Foss v. Harbottle, that is that as a matter of general principle minority shareholders cannot sue for wrongs done to the company, unless an established exception to the rule applies. It was argued that the "fraud on a minority" exception did not apply.

On 5th November, 1997 the plaintiffs faxed to the applicants an amended Order of Justice and sought consent to its being filed. At the hearing Mr. O'Connell for the applicants did not object to the amendments, subject to the usual terms as to costs, and argument proceeded on the basis of the amended Order of Justice. Mr. O'Connell maintained his submission that the amended Order of Justice disclosed no cause of action. The amended Order of Justice contained two significant amendments. I interpose that it is common ground that the majority shareholders are Mr. Darwish, Ashley Guarantee plc. and Mr. Franklin. The first is that in the original Order of Justice the plaintiffs asserted that they brought the action as "representing" the majority shareholders. In the amended Order of Justice that assertion is deleted and the majority shareholders are joined as fourth, fifth and sixth defendants respectively. No explanation was given for this volte-face. The second is that the plaintiffs now allege against the applicants *"a lack of probity such as to amount to dishonesty"*. The relevant paragraphs are as follows:

> *"14. In the premises of paragraphs 1 to 13, the Plaintiffs aver that the Second and Third Defendants acted with a lack of probity such as to amount to dishonesty. The Plaintiffs further aver that the want of probity of the Defendant Directors and the breaches of their duties pleaded at paragraphs 1 to 13 hereof amount to a fraud on the minority.*
>
> *PARTICULARS*
>
> *(i) The Defendant Directors executed a Power of Attorney on 9 February 1994 without ascertaining the price for which Las Colinas was to be sold.*
>
> *(ii) The Defendant Directors executed the said Power of Attorney without ascertaining to whom the property was to be sold.*
>
> *(iii) The Defendant Directors executed the Power of Attorney without enquiry as to what was to happen to the proceeds of sale of Las Colinas.*
>
> *(iv) The Defendant Directors failed to enquire on what basis the First Plaintiff had authorised the sale since the Power of Attorney in favour of the Fifth Defendant was inadequate as pleaded at paragraph 10(iii) hereof.*

(v) *The Defendant Directors failed to obtain shareholder approval through a meeting of shareholders as pleaded at paragraph 11.*

(vi) *The Defendant Directors failed to call a meeting of all the directors notwithstanding that the First Plaintiff was a director as pleaded at paragraph 12.*

(vii) *The Defendant Directors failed to make enquiries in response to a letter of 7 February 1994 from Julian Holy as to which of the majority shareholders had authorised the execution of a Power of Attorney.*

(viii) *The Defendant Directors further failed to consider whether a simple majority of shareholders in any event could authorise the execution of a Power of Attorney by reference to the Articles of Association.*

(ix) *The Defendant Directors failed to obtain any further information after the Power of Attorney had been executed, what had happened to Las Colinas and the proceeds of sale following execution, even after having been requested to obtain the information by the First Defendant in April 1995.*

(x) *The Defendant Directors failed to provide full information to the First Plaintiff in relation to the execution of the Power of Attorney on 9th February 1994 in response to requests dated 10th April 1995 and 31st August 1995 by failing to provide Julian Holy's letter of 7th February 1994 to Bedell & Cristin.*

15. *Further, the Plaintiffs aver that the transfer of Las Colinas for nil consideration was a fraud on the minority in which the Fourth, Fifth and Sixth Defendants participated and/or from which they benefitted.*

PARTICULARS

i. *On or around July 1995, the Fourth Defendant admitted orally to Kamal Khan, husband of the First Plaintiff, that, as in Leisure Enterprises, he held an interest of 34.7% in Beltana.*

ii. *Instructions were given by the Fifth and Sixth Defendants through Julian Holy pursuant to Julian Holy's letter dated 13th December 1993 for the Defendant Directors to issue a proxy in favour of Mr Alfonso Lopez-Ibor Alino and Mr Eduardo Sebastian De Erice Y Malo De Molina, the same two individuals identified in the Power of Attorney executed on 9th February 1994 and referred to at paragraph 6 above. In the premises the Fifth and Sixth Defendants were the other two shareholders who gave instructions to the Defendant Directors and to Julian Holy to issue the said Power of Attorney on 9th February 1994.*

iii. *The written direction of the Fifth Defendant contained in its letter dated 14th December 1993 purportedly exercising the proxy of 20th September 1993 given by the First Plaintiff to the Fifth Defendant was made contrary to the terms of the said proxy.*

iv. The Sixth Defendant failed to act in the interests of the said Kamal Khan as a bankrupt for whom the Sixth Defendant is trustee in bankruptcy by voting for and permitting disposal of the sole asset of Leisure Enterprises for nil consideration where Mr Khan was registered as a shareholder in Leisure Enterprises holding 666,660 £1 shares comprising an interest of 22.22%."

It is well established that I should exercise the power to strike out only if it is plain and obvious that the action will not succeed. The mere fact that the case is weak and not likely to succeed is not sufficient. It must be on its face obviously unsustainable. On the other hand a striking out may ***"often be required by the very essence of justice to be done"*** (per Lord Blackburn in Metropolitan Bank v. Pooley (1885) 10 App Cas. 210, p 221).

Mr. O'Connell submits that the rule in Foss v. Harbottle (1843) 2 Hare 461 makes it plain and obvious that the plaintiffs will not succeed. The classic exposition of the rule upon which Mr. O'Connell relies is to be found in the Privy Council case of Burland v. Earle [1902] AC 83 where Lord Davey stated at page 93:

> ***"It is an elementary principle of the law relating to joint stock companies that the court will not interfere with the internal management of companies acting within their powers, and in fact has no jurisdiction to do so. Again, it is clear law that in order to redress a wrong done to the company or to recover moneys or damages alleged to be due to the company, the action should prima facie be brought by the company itself. These cardinal principles are laid down in the well-known cases of Foss v. Harbottle and Mozley v. Alston ((1847), 1 Ph. 790), and in numerous later cases which it is unnecessary to cite. But an exception is made to the second rule, where the persons against whom the relief is sought themselves hold and control the majority of the shares in the company, and will not permit an action to be brought in the name of the company. In that case the courts allow the shareholders complaining to bring an action in their own names. This, however, is mere matter of procedure in order to give a remedy for a wrong which would otherwise escape redress, and it is obvious that in such an action the plaintiffs cannot have a larger right to relief than the company itself would have if it were plaintiff, and cannot complain of acts which are valid if done with the approval of the majority of the shareholders, or are capable of being confirmed by the majority. The cases in which the minority can maintain such an action are, therefore, confined to those in which the acts complained of are of a fraudulent character or beyond the powers of the company. A familiar example is where the majority are endeavouring directly or indirectly to opriate to themselves money, property, or advantages which belong to the company, or in which the other shareholders are entitled to participate, as was alleged in the case of Menier v. Hooper's Telegraph Works ((1874), 9 Ch. App. 350)."***

Both counsel agree that this principle forms part of the law of Jersey and indeed it has been applied on several occasions.

The so-called "fraud upon a minority" exception has been described as "doubly misleading". The learned editors of Palmer's Company Law state at paragraph 8.813:

"First, "fraud" in this context is not confined to common law fraud, ie deceit, but embraces a wider equitable meaning. Secondly the fraud is not so much committed on the minority as on the company. Hence, where the exception operates, the plaintiff shareholder brings a derivative action for the benefit of his company".

Mr. Thompson for the plaintiffs argued that the applicants' conduct fell within this wider equitable meaning of "fraud". He relied upon the judgment of Templeman J. in Daniels and others v. Daniels and others [1977] Ch 89. The headnote of that case reads:

"The plaintiffs were minority shareholders in the third defendant ("the company"). The first and second defendants were majority shareholders and directors of the company. In October 1970 the company sold certain land to the second defendant for £4,250 on the instructions of the first and second defendants as directors. In 1974 the land was sold by the second defendant for £120,000. The plaintiffs brought an action against the defendants alleging that the price at which the land had been sold to the second defendant was well below its market value and that the first and second defendants knew that that was so, but had purported to adopt the probate value of the land although a probate value was usually much less than the open market value. The defendants applied to strike out the statement of claim as disclosing no reasonable cause of action since it did not allege fraud or any other ground that would justify an action by minority shareholders against the majority for damage caused to the company.

Held - The application would be dismissed. The confines of the rule that minority shareholders could not maintain an action on behalf of the company should not be drawn so narrowly that directors were able to make a profit out of their own negligence. Accordingly, minority shareholders were entitled to bring an action where the majority of the directors negligently, though without fraud, had benefited themselves at the expense of the company."

At page 96 the learned judge stated:

"The authorities which deal with simple fraud on the one hand and gross negligence on the other do not cover the situation which arises where, without fraud, the directors and majority shareholders are guilty of a breach of duty which they owe to the company, and that breach of duty not only harms the company but benefits the directors. In that case it seems to me that different considerations apply. If minority shareholders can sue if there is fraud, I see no reason whey they cannot sue where the action of the majority and the directors, though without fraud, confers some benefit on those directors and majority shareholders themselves. It would seem to me quite monstrous particularly as fraud is so hard to plead and difficult to prove, if the confines of the exception to* Foss *v Harbottle were drawn so narrowly that directors could make a profit out of their negligence. Lord Hatherley LC in Turquand v Marshall opined that shareholders must put up with foolish or unwise directors. Danckwerts J in Pavlides v Jensen accepted that the forebearance of shareholders extends to directors who are 'an amiable set of lunatics'.

> ***Examples, ancient and modern, abound. But to put up with foolish directors is one thing; to put up with directors who are so foolish that they make a profit of £115,000 odd at the expense of the company is something entirely different. The principle which may be gleaned from Alexander v Automatic Telephone Co (directors benefiting themselves) from Cook v Deeks (directors diverting business in their own favour) and from dicta in Palvides v Jensen (directors appropriating assets of the company) is that a minority shareholder who has no other remedy may sue where directors use their powers intentionally or unintentionally, fraudulently or negligently in a manner which benefits themselves at the expense of the company."***

It is arguable on the pleadings that the applicants were negligent or acted in breach of duty. But that is not in my judgment sufficient by itself to bring their conduct within the scope of the exception.

Mr. O'Connell relied upon Palvides v Jensen and others [1956] 2 All ER 518. In that case a minority shareholder brought an action against the defendant directors following the sale of an asbestos mine for £182,000. The sale was not submitted for the approval of the company in general meeting. It was alleged that the defendant directors had been grossly negligent because the true value was about £1 million. Fraud was not alleged. The plaintiff claimed on behalf of himself and all other shareholders except the defendant directors a declaration that the directors were guilty of a breach of duty and the payment of damages by them to the company. It was held that the action was not maintainable by the plaintiff because, the sale of the mine not being ultra vires and no acts of a fraudulent character being alleged by the plaintiff, the sale could be approved or confirmed by a majority of the directors. Danckwerts J stated, at page 523:

> ***"On the facts of the present case, the sale of the company's mine was not beyond the powers of the company, and it is not alleged to be ultra vires. There is no allegation of fraud on the part of the directors or appropriation of assets of the company by the majority shareholders in fraud of the minority. It was open to the company, on the resolution of a majority of the shareholders, to sell the mine at a price decided by the company in that manner, and it was open to the company by a vote of the majority to decide that, if the directors by their negligence or error of judgment had sold the company's mine at an undervalue, proceedings should not be taken by the company against the directors. Applying, therefore, the principles as stated by Lord Davey, it is impossible to see how the present action can be maintained."***

This extract was referred to with approval by Templeman J in Daniels v Daniels. The learned judge stated, after citing the above extract:

> ***"Counsel for the defendants relies very strongly on this decision as showing that, whatever the exceptions to Foss v Harbottle may be, mere gross negligence is not actionable, and he says all that is pleaded in the present case is gross negligence at the most. But in Pavlides v Jensen no benefits accrued to the directors. Counsel for the plaintiffs asks me to dissent from Pavlides v Jensen but the decision seems to me at the moment to be in line with the authorities, in what is a restricted exception to the rule in Foss v Harbottle."***

It is not suggested by the plaintiffs that the applicants derived any benefit from their actions. On the contrary it is alleged that the benefit accrued to one or more of the fourth, fifth and sixth defendants. Did the actions of the applicants then bear the hallmark of dishonesty or want of probity? The applicants "purported" (to borrow a word from the Order of Justice) to act upon the instructions of the majority shareholders, as they had been mandated by all the shareholders including the plaintiffs to act, in executing a power of attorney in favour of the Spanish lawyers. I make no finding as to whether they acted negligently, in breach of duty or in breach of trust in so doing. But it seems plain to me that they did not act "fraudulently" however wide and equitable a meaning one ascribes to that term. The epithet must carry some connotation of obloquy. For my part I cannot find that the applicants' conduct merits that kind of description. In my judgment the allegations against the applicants cannot be brought within the "fraud on a minority" exception to the rule in Foss v. Harbottle.

It remains to consider the alternative averment that the applicants acted in a manner unfairly prejudicial to the plaintiffs so as to give rise to relief under the 1991 Law. The relevant part of article 141 of the 1991 Law provides:

"Power for member to apply to court

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

Article 143 confers a number of powers on the court if it is satisfied that an application under Article 141 is well founded.

Here the particulars of the allegedly unfairly prejudicial conduct are those set out above in relation to the alleged fraud upon a minority.

Mr. Thompson referred me to two English cases.

The first was Scottish Co-Operative Wholesale Society Ltd. v. Meyer & another [1958] 3 All ER 66. That was a case where a joint venture company was owned by the appellants and respondents in almost equal proportions. The appellants owned 4,000 shares and the respondents 3,900. The appellants had three nominees on the board of the company and the two respondents were directors. The parties fell out and the appellants began to conduct the same type of business on their own account. The appellants resolved, although they did not tell the respondents, that the company had served its purpose and should be liquidated. The nominee directors adopted a policy of passive support of the appellants by inactivity, allowing the company's trading activities to decline or vanish. It was held that the conduct of the nominee directors was oppressive, albeit amounting only to passive neglect. It was urged upon me by counsel for the plaintiffs that the conduct of the applicants in this case amounted to passive neglect.

The second was Re a company (No 001761 of 1986) [1986] Ch 141. The headnote of that case reads:

"Two shareholders of a company, who together with the respondent were the only shareholders and directors of the company, presented a cross-petition under s 459 of the Companies Act 1985 alleging that affairs of the company had been conducted in an unfairly prejudicial manner and seeking an order that the respondent sell her shares to them. The principal ground of complaint was that the respondent had paid off a loan which the company owed to its bank without informing the company and had taken a transfer of the bank's security. The petition contained a number of other broad allegations of unfairly prejudicial conduct which included, inter alia, allegations that (i) the respondent had interfered in the day-to-day management of the company; (ii) that an ineffective notice for the repayment of a loan had been served on the company; and (iii) that the respondent's personal solicitor had at a board meeting asked the petitioners to transfer their shares to the respondent and to resign as directors. In the present proceedings the respondent sought to have the cross-petition struck out on the grounds that it disclosed no cause of action or alternatively that it was an abuse of the process of the court or that it was bound to fail.

Held - Motion granted and petition dismissed. To obtain relief under s 459 of the 1985 Act it was necessary for a petitioner to show that the unfair prejudice arose from the way in which the affairs of the company were conducted or was attributable to an act or omission on the part of the company, and not from the acts of a shareholder carried out in a personal capacity outside the course of the company's business. On the facts, the repayment by the respondent of the loan which the company owed to its bank could not constitute a ground for relief under s 459 of the 1985 Act as it involved the respondent acting in her personal capacity and was not conduct in the affairs of the company. In addition, this allegation did not involve conduct that was in any way prejudicial as the repayment of the loan and the transfer of the bank's security to the respondent did not alter the position of the company. As the other allegations did not relate to the way in which the affairs of the company were conducted, or did not constitute a ground for finding unfairly prejudicial conduct, the petition would accordingly be struck out."

Mr. Thompson submitted that the prejudice to the company in this case was the disposal of the company's assets for a nil consideration. He submitted that the prejudice was unfair because of the way in which the applicants purported to grant the power of attorney. It seems to me that the short answer to this is that the applicants did not cause the prejudice. The prejudice, if it was caused, resulted from the actions of the Spanish lawyers. It is true that the applicants executed the power of attorney under which the Spanish lawyers acted. But the prejudicial conduct was that of the Spaniards and not of the applicants. I therefore hold that the conduct of the applicants as alleged in the Order of Justice could not be prejudicial and could not therefore justify an order under Article 143 of the 1991 law.

For these reasons I give leave to amend the Order of Justice as requested by counsel for the plaintiffs but grant the application and strike out the Order of Justice so far as the applicants are concerned.

Authorities

Gore-Brown on Companies (44th Ed'n): paragraphs 28.1-28.4.

Palmer's Company Law: paragraphs 8.801-8.817.

Foss -v- Harbottle (1843) 2 Hare 461.

Burland -v- Earle (1902) AC 83.

Prudential Assurance -v- Newman Industries (1982) Ch.204.

Eves & Others -v- St. Brelades Hotel (25th May 1995) Jersey Unreported.

Companies (Jersey) Law, 1991: Articles 141 and 143.

Scottish Co-operative Wholesale Society Ltd. -v- Mayer and Anor. [1958] 3 All ER 66.

Re a Company (No. 001761 of 1986) [1986] Ch. 141.

Re Duomatic Ltd. [1969] 2 Ch. 365.

Associated Leisure -v Associated Newspapers Ltd. [1970] QB 450.

Wallingford -v- Mutual Society (1879) 5 A.C. 685.

Metropolitan Bank Ltd. -v- Pooley (1885) 10 A.C. 210.

Royal Court Rules 1992: Rule 6/12, Rule 6/13.

R.S.C. (1997 Ed'n): Order 18 Rule 19, Order 20 Rules 5 - 8; 18/8/8

Lazard Brothers & Company (Jersey) Limited -v- Bois & Bois, Perrier & Labesse (1987 - 88) JLR 639.

Poole -v- Poole (1987 - 88) JLR N5.

Abdel Rahman -v- Chase Bank (1994) JLR 186.

Baker Ltd. -v- Medway Building & Supplies Ltd [1958] 3 All ER 540.

Hipgrave -v- Case (1885) 28 Ch.D 356.

Pacific Investments Limited -v- Christensen & Others (1995) JLR 250.

Pavledes -v- Jensen & Others [1956] 2 All ER 518.

Daniels & Others -v- Daniels & Others [1978] 2 All ER 89: [1977] Ch. 89.

Smith & Others -v- Croft & Others (Number 2) [1987] 3 All ER 909.

Bishopsgate Investments Management Limited (In Liq) -v- Maxwell (No.2) [1993] BCLC 814.

Royal Brunei Airlines SDN VHD -v- Tham [1995] 3 All ER 97.