

Enforcement of Directors' Liabilities or Members' Rights Through Litigation

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Why Litigate?

- Corporate litigation between the directors and members of a company is a common phenomenon which may have dire consequences for the management of the company.
- However, these conflicts are inevitable as they usually arise from disagreements over the control and management of the company and its resources by the director(s).
- And once the company does not resolve these disputes internally, the aggrieved member(s) may seek redress in the Courts.

The Relevant Principles

- The applicable legal principles governing actions which are commenced to enforce the Directors' Liabilities or Members' Rights may be found in both the common law of Ghana and statute.
- To have a strong grasp of these principles, one must understand:
 - The Rule in Foss v. Harbottle and its application under Ghana law.
 - The Principles Governing Representative Actions.
 - The Principles Governing Derivative Actions.
 - The Principles Governing the Remedies against Oppression.

The Rule In Foss V. Harbottle

- The rule in Foss v. Harbottle[1843] 2 Hare 461;67 ER 169 is a two-pronged common law principle which provides that :
 - The proper person to sue to redress a wrong done to a company or to the property of the company, or to enforce rights of the company is the company itself.
 - Where an alleged wrong is a transaction which might be made binding on the company and all its members by a simple majority of the members, no individual member of the company is allowed to maintain an action against the company.
- The rule is premised on the considerations that a company is a legal person, the majority have a right to rule, the prevention of multiplicity of suits, and the avoidance of ineffective court orders.

The Rule In Foss V. Harbottle: Common Law Exceptions

- There are, however, exceptions to the Rule in Foss v. Harbottle at common law including:
 - Acts infringing the personal rights of shareholders such as the unlawful restriction of a shareholder's voting rights (see *Pender v Lushington* [1877] 6 Ch D 70.)
 - Where the act complained of can only be confirmed by a special or extraordinary resolution. (See *Edwards v. Halliwell* [1950] 2 ALL ER 1064.)
 - Where the act complained of is ultra vires the company (See *Prudential Assurance v. Newman* (1982) Ch. 204)
 - Where there is fraud on the minority (*Estamanco v. Greater London Council* (1982) 1 All ER 437)

The Rule In Foss V. Harbottle: Applicability Under Ghana Law

The common law forms part of Ghana law by virtue of Article 11(1)(e) & (2) of the 1992 Constitution. Thus, being a common law principle, the Rule in Foss v. Harbottle is applicable in Ghana (subject to the statutory modifications.)

The Supreme Court in P.S. Investments Ltd. V. CEREDDEC [2012] 1 SCGLR 618. exhaustively discussed of the applicability of the Foss v. Harbottle principle in Ghana under the old Companies Act. The decision is nonetheless, relevant to the new Companies Act (Act 992). Broadly speaking, the main takeaways from the decision are that:

- The Companies Act, has retained the Rule in Foss v. Harbottle to the extent that it is not inconsistent with the act. (See s 5 of Act 992).
- The Common law exceptions to the Rule in Foss v. Harbottle (already referred to) are applicable in Ghana.
- The Companies Act has in some respects codified the Rule in Foss v. Harbottle.
- The Companies Act has also created statutory exceptions to the Rule in Foss v. Harbottle.

Codification Of The Rule In Foss V. Harbottle

ACT 992 has, to an extent, codified the Rule in Foss v. Harbottle :

- Under s 18 of Act 992, the company has legal personality and, thus, the capacity to sue. This power is generally exercised by the Board of Directors under section 144(3) of the Act 1992.
- But the members in general meeting may sue in the name of the company where the Board of Directors neglects or refuses to do so under section 144(5)(b) of Act 992.
- Thus, in general individual members cannot sue to protect the rights of the company in accordance with the Rule in Foss v. Harbottle.

Representative Actions

Representative actions may be considered as exceptions to the Rule in Foss v. Harbottle. These actions are governed by s 205 of Act 992.

Representative actions are commenced by a member where Act 992 creates a cause of action in the member(s) but requires or permits the member/plaintiff to sue not just for himself but also on behalf of the members of a relevant class.

Representative Actions: Prerequisites

No representative action can be properly commenced if Act 992 does not authorize the commencement of a suit in a representative capacity on behalf of the plaintiff and other persons.

So, it is necessary to ensure that there is a specific provision which entitles the plaintiff to sue in a representative capacity.

Representative Actions: Uses Of Representative Actions

Representative actions serve numerous purposes. They include:

- Proceedings to challenge the legality of dividend payments under section 72 (3) & (4) of Act 992.
- Proceedings by a debenture holder to enforce the security of a series of debentures which the debenture holder does not entirely hold under sections 89(4) of Act 992.
- Proceedings to enforce liabilities for director's breach of duty pursuant to section 199 and 201(a) of Act 992.
- Proceedings to restrain a threatened breach of duty under sections 190 & 192 pursuant to section 200(b).
- Proceedings to recover company property from a director pursuant to section 200(b) of Act 992.

Representative Actions: Some Important Principles

- Though a representative action may inure to the company's benefit, it is not instituted in the name of the company. Rather it is instituted in the name of the plaintiff member or creditor.
- The plaintiff does not need to seek the consent of the company, or the members of the class represented in order to sue.
- The plaintiff cannot name the individual members of the class as parties to the suit without their approval. They may opt to join the suit after commencement if they are interested, but if they fail to do so, the plaintiff has full conduct of the case even though the suit was commenced in a representative capacity.
- Whether or not a member of a class is joined as a party, the decision of the Court will be binding on that member.

Derivative Actions

Derivative actions may be considered as exceptions to the Rule in Foss v. Harbottle. These actions are governed by s 201- 204 of Act 992. There is, however, no clear definition of what a derivative action is under Act 992.

However, an action may be considered to be a derivative action if:

- A director or member of a company or sues in the name of a company or a subsidiary of the company.
- A director or member of a company intervenes in proceedings to which the company or a related company is a party to in order to continue, defend, discontinue the proceedings on behalf of the company or the related company.

Derivative Actions: Prerequisites

- The member/director must apply for leave of the Court to sue or intervene.
- The Application for leave must be on notice to the company or its subsidiary.
- To succeed, the member/director must prove that (a) the company or the related does not intend to sue, continue or diligently defend the suit (b) it is in the interest of the company or a subsidiary of the company that the decision to sue is not left to its directors.

Derivative Actions: Uses

Derivative actions may be commenced in all situations where the company has a right to sue. They also have the advantage of entitling members or directors of companies to protect the interest of related or subsidiary companies.

It is not necessary that a specific provision entitles the member or director to sue. Nonetheless derivative actions may be brought in :

- Proceedings to enforce liabilities for director's breach of duty pursuant to section 199 and 201(a) of Act 992.
- Proceedings to restrain a threatened breach of duty under sections 190 & 192 pursuant to section 200(b).
- Proceedings to recover company property from a director pursuant to section 200(b) of Act 992.

Derivative Actions: Some Important Principles

- Derivative actions may not be settled, compromised, or discontinued without leave- s 204. Otherwise, the majority will simply exercise their powers to discontinue those actions.
- The Court has very wide powers to ensure that the derivative actions are effectively prosecuted- s 203. This ensures that the officers of the company who may have been opposed to the suit may not frustrate it.
- The Court may in appropriate cases order that the costs of the suit be paid by the company rather than the member or director who commenced the suit- s 202. This ensures that costs do not operate to prevent members or directors from instituting derivative actions where necessary.

Remedies Against Oppression

S 219 of Act 992 provides members or debenture holders of a company remedies to the oppressive conduct against them in the name of the company. These remedies may include:

- Mandatory and Prohibitory Orders.
- Orders for the cancellation or variation of a transaction/resolution.
- Orders regulating the future conduct of the company's affairs.
- Orders for the purchase of shares or debentures of aggrieved persons.

Remedies Against Oppression: Prerequisites

To successfully apply for the remedies against oppression:

- The Applicant must be a member or debenture holder of the Company; and
- The Company must be run in a manner oppressive to or in disregard of the proper interests of the members, debenture holders, or officers of the company; or
- There must be an actual or threatened unfair discrimination or prejudice to members or debenture holders from the company or through a resolution from the members or debenture holders or a class of the members or debenture holders.

Remedies Against Oppression: The Judicial Perspective

The ratio in *Pinamang v. Abrokwa* [1991] 2 GLR 384 provides insight into the attitude of the the Courts where remedies against oppression are sought. It must be proved that:

- The action was commenced with the genuine object of obtaining the relief claimed and not for exerting pressure in order to achieve a collateral purpose.
- The matters complained of must affect the person alleged to have been oppressed in his character as a member of the company and not in any other capacity.
- The applicant must adduce evidence seeking to show a chain of events and occurrences of harsh and burdensome conduct which continued up to the date of presentation of the petition.
- The court is, however, precluded from inquiring into matters of internal management or, at the instance of a shareholder, interfering with transactions which though prima facie irregular and detrimental to the company, were capable of being rectified by an ordinary resolution of the company in general meeting. (Note that this is consistent with the rule in *Foss v. Harbottle*)

Prevention Of Ultra Vires & Illegal Acts

Where a company acts in excess of its authority under the registered constitution, the company's acts do not become void—S 19(2), (4) & (7) of Act 992. This ensures that third parties may confidently deal with the company on the presumption that the company acted regularly.

However, as a mitigating measure, the law allows members and debenture holders to prohibit illegal or ultra vires acts. Such applications may be brought under S 19 of Act 992 or S 218 of Act 992 or both where appropriate.

It must be noted that these prohibitions are consistent with the common law exceptions against ultra vires acts.

Prevention Of Ultra Vires & Illegal Acts: S 19 Applications- Prerequisites

- The Applicant must be: (a) member of the company or (b) a debenture holder or a trustee of a debenture holder with a floating charge of the company's asset(s).
- The Act complained of must be contrary to the company's registered constitution.
- The Act complained of must be an act capable of being prohibited by the Court- it must not have already been executed.

Prevention Of Ultra Vires & Illegal Acts S 19 Applications– Special Provisions For Contracts

The law seeks to strike a balance where contractual obligations are involved. Thus, in appropriate s 19 applications, the Court may:

- Set aside a contract and its performance.
- Make appropriate compensatory orders resulting from the setting aside of the contract.

Thus, the court may prohibit the company from performing contracts and also provide reasonable compensation to the company or any other injured party to the contract for the cancellation of the contract.

Prevention Of Ultra Vires & Illegal Acts: S 218 Applications– Prerequisites

- S 218 Applications are similar to S 19 Applications as they are both applications for prohibitory injunctive orders. However, in S 218 applications, the court may declare the acts complained of to be void.
- The following prerequisites must be satisfied:
 - The Applicant must be a member of the company; and
 - The act which the Applicant seeks to prohibit must be illegal, in excess of the company's capacity, or contrary to the company's constitution; or
 - The Applicant must seek to restrain the company from acting on a resolution passed contrary to Act 992 or the Constitution.

Which Originating Process Must Be Used?

- It is not sufficient to understand the substantive requirements of the various causes of actions created under Act 992. It is also necessary to appreciate the procedural rules governing the commencement of those actions, including the rules governing the proper originating process.
- This is because where the law provides a special procedure in order to do an act that procedure must be followed.- *Boyefio v. NTHC PROPERTIES LTD* [1997-1998] 1 GLR 768.

Which Originating Process Must Be Used?

- First, if the law states that the court must be approached by an application (for example, S 218 & 219 action) then the appropriate process is an an originating motion on notice. Please note that most of the actions under Act 992 require an application to the court but a prudent lawyer must not make assumption.
- Second, if the law requires that the court must be petitioned then a petition must be filed. This only appears in s 234(b) in relation to the Registrar of Companies petitioning for the company to be wound up.
- Third, if the provision of Act 992 creating the cause of action does not provide a special procedure, the action must be commenced by a writ of summons in accordance with Order 4 r. 2 of CI 47 since the High Court has original jurisdiction over actions created under Act 992. (See s.383 & 1st Schedule to Act 992.) So, in general, derivative and representative actions are to be commenced by a writ.

Conclusion

Act 992 has whittled down the application of the Rule in Foss v. Harbottle in Ghana by providing members and to some extent debenture holders the legal capacity to enforce their rights and director's liabilities in Courts. These statutory modifications should be welcome as effective tools for ensuring proper corporate governance in Ghana.