IN THE GRAND COURT OF THE CAYMAN ISLANDS
FINANCIAL SERVICES DIVISION

CAUSE NO: FSD 54 OF 2021 (CRJ)

IN THE MATTER OF THE COMPANIES ACT (2021 REVISION)

AND IN THE MATTER OF MADERA TECHNOLOGY FUND (CI), LTD

Appearances:	**Mr. Laurence Aiolfi of Mourant Ozannes (Cayman) LLP for the Petitioner**
	Mr. James Eldridge and Mr. Lukas Schroeter of Maples and Calder (Cayman LLP) for Madera Technology Fund (CI), Ltd
Before:	**The Hon. Justice Cheryll Richards Q.C.**
Heard:	**11th February 2022**
Draft Judgment:	**26th April 2022**

HEADNOTE

Company Law - Winding up petition on the just and equitable ground - summons for directions - orders to be made under CWR O.3 r.12(1) (a) and (b) – joinder of shareholders as respondents to the petition.

JUDGMENT

1. This is a judgment on an application for directions filed by Fideicomiso F/000118, "the Petitioner" pursuant to O.3 r.12 of the Companies Winding Up Rules ("CWR"). On the 5th March 2021 the Petitioner filed a Petition seeking the winding up of Madera Technology Fund (CI) Ltd. ("the Company") under s. 92 (e) of the ***Companies Act (2021 Revision)*** on the just and equitable ground.

2. At the time of the filing of the Petition, the Petitioner filed a summons for directions in accordance with the CWR. This was not heard pending determination of the Company's

application that the Petition be struck out. A ruling in respect of that application was rendered on the 10th November 2021.

3. The Petitioner is a Trust established under the laws of Mexico. It is owned by certain members of the Bours family. The Company is registered in the Cayman Islands as an exempt company. Its directors are Mr. Kristopher Drankiewicz, Ms. Liliana Macias, his wife, and as at March 2021, Mr. Ronan Guilfoyle. Mr. Drankiewicz is also the managing member of the Company's General Partner.

4. By its summons for directions filed on the 14th December 2021 the Petitioner applies for certain orders under CWR O.3 r.12 in respect of its Petition. They include orders for directions as to the progress of the matter and four orders as follows:-

    1. That the Petition shall be treated as an *inter partes* proceeding between the Petitioner and Kristopher Drankiewicz and Liliana Macias as Respondents.

    2. That the Petitioner is granted leave to amend the Petition in accordance with the draft Amended Petition attached to the summons.

    3. Kristopher Drankiewicz and Liliana Macias be added as respondents to the Petition.

    4. The Petitioner is granted leave to serve the Amended Petition on Kristopher Drankiewicz and Liliana Macias out of the jurisdiction.

5. The application for directions is supported by the second affidavit of Daniel Alberto Ferrer dated 10th December 2021. He is the Chief Financial Officer for the Petitioner. He states his belief that the said two directors of the Company are proper and necessary parties to the proceedings and should be added as respondents to the Amended Petition. He further states:

" *10… Kris Drankiewicz was the sole director of the Company at the time it was established. On 1 January 2020, his wife Liliana Macias was appointed as a second director of the Company: Kris Drankiewicz and Liliana Macias were the only directors of the Company during the period which founds the basis for the Petition (and Amended Petition) namely January 2020 to March 2021. A third director, Ronan Guilfoyle of Calderwood, was appointed in March 2021, however his appointment post-dates the claims in the Petition and the Petitioner does not seek to add him as a party.*

11. The misconduct of the Directors is central to the Petitioner's application to wind up the Company. As set out in Ferrer-1 and Laborin-1, the Petitioner has justifiably lost confidence in the probity with which the affairs of the Company are being conducted and further, seeks the appointment of independent liquidators to investigate the affairs of the Company…

12. The Company acted through the Directors in relation to the above matters and it is the misconduct of the Directors including acting in breach of duty to the Company and to protect their position as directors, that gives rise [to] the basis for the winding up of the Company. The need for these proceedings could have been avoided had the Directors acted properly in accordance with their own duties and in accordance with the Company's constitutional documents."

6. Mr. Ferrer also states that should the proceedings remain as against the Company, the costs of the proceedings would fall substantially on the Petitioner rather than against the directors if they are found to have acted in wilful default of their duties.

THE BACKGROUND

7. The background facts as to the structure of the Company and the allegations are obtained from the Petition and the filed affidavits. A number of affidavits were filed with respect to the strike out application and the Court was referred to these earlier affidavits in the course of this hearing. This background is set out in the earlier judgment of the Court.[1] It is summarised and repeated below in order to indicate the nature of the proceedings and the substance of the allegations which have been made.

8. The Company was registered in the Cayman Islands on the 6th November 2014 and commenced operations on the 1st January 2015. It operates as a feeder fund to Madera Technology Master Fund Ltd, which is also registered in the Cayman Islands. It is part of a master feeder structure through which it invests almost all of its assets. It offers investments in a number of share classes, one of which is Class A, Accolade E-1 Sub-Class which are solely invested in Accolade Inc.

9. In August 2018, the Petitioner invested some US$5.5 million in the Company towards the purchase of Accolade E-1 Shares. It obtained what was reported to it to be an ownership interest of approximately 29.5% together with various rights including rights to information and to vote.

10. The investment was made following an introduction to the Company by a member of the Bours family, Mr. Mario Bours Laborin ("Mr. Bours"). Mr. Bours then worked for an affiliate of the Investment Manager. He worked alongside Mr. Drankiewicz and also served as a liaison between the Petitioner and the Company.

11. From about September 2019 the relationship between Mr. Bours and the affiliate of the Investment Manager deteriorated culminating in him filing proceedings against it in New York in May 2020.

12. The relationship between the Petitioner and the Company also deteriorated, worsening as a series of events unfolded which events each viewed in a different light. The fact of the

[1] Judgment dated 10th November 2021

occurrence of the events is not disputed. On the one hand the Company alleges *inter alia* normal commercial activity, and/or defensive responses to the Petitioners 'hostile' conduct and the Petitioner on the other alleges misconduct and oppressive conduct by the Company.

13. The first in the sequence of events is two capital calls of a total of US$311,112.78 which were made by the Company of the Petitioner in August 2019 and April 2020. The Petitioner paid the first call in September 2019 and the second after inquiry and with some expressed reluctance in June 2020. The Company later accepted that it had no legal basis to make these calls and that the Petitioner had no obligation to pay them.

14. The Petitioner says that arising therefrom it began seeking detailed explanations of the expenses claimed in relation to the calls and it repeated earlier requests for information as to its proportionate shareholding. It sought information as to the legal basis on which the Company purported to make the calls, the timing and breakdown of the expenses claimed in relation to them, an itemized breakdown of the Company's investment activity, operational expenses and working capital requirements, how the Petitioner's portion of the second capital call was calculated, a quarterly breakdown of the Company's management fee periods and copies of the agreements relating to the Petitioner's investment in the Company. Some responses were received but the Petitioner expresses dissatisfaction with these responses and describes them as limited and lacking in detail.

15. The Company says that the Petitioner was provided with the information to which it is entitled and characterizes the information requests of the Petitioner as either seeking information to which it was not entitled, had already received or was information which could not be provided because of United States security laws. In response to the request for a breakdown of share percentage information, the Company refused to provide this information and indicated that the Petitioner was provided with the same information as other investors. In March 2020 in response to further requests, the Company declined to provide copies of formal share certificates stating that such are not issued by a private fund. A request by the Petitioner to exercise a right with respect to the register of members was met with the response that s.44 of the ***Companies Act*** does not apply to the Company.

16. On the 25th June 2020 an email from Mr. Bours to one of the attorneys of the Petitioner was inadvertently copied to Mr. Drankiewicz. It stated in part as follows:-

> *"Moreover, the overall goal of the Trust is to gain more control and oversight over its Investment primarily (in [our] own view) through three sequential lines of action:i) exercising our rights to receive information on the state of our investment and the partnership, ii)determining the proportional equity stake that the Trust holds in order to ascertain our corporate rights (pursuant the majority thresholds set in the corporate documents), iii) If a majority stake is indeed confirmed at the fund and/or share class levels, to explore the possibility and merits of appointing an independent inspector at the very least and/or designating additional directors to gain more control over the investment and/or removing the sole director altogether, possibly forcing a wind down (the nuclear option). The main purpose of pursuing these actions is to gain control over redemption rights, so that we can exit the investment at our discretion or to at least get comfortable with the state in the investment by having more of a say over its destiny. We believe we can achieve this either judicially or through negotiation with the fund's principal and GP."*

17. The inadvertent disclosure of this e-mail appears to have led to further events and increased levels of lack of trust between both.

18. On the 29th June 2020, the Company sought to compulsorily redeem the Petitioner's shares in exercise of a power conferred by article 12.1 of the Company's Memorandum and Articles of Association ("MAA"). The Compulsory Redemption Notice made reference to the "privileged" email from Mr. Bours and described it as detailing the Petitioner's intention to gain control over the Company and force its wind down.

19. There were various calls between representatives of the Petitioner and the Company. On the 7th July 2020 Mr. Ferrer assured Mr. Drankiewicz that the Petitioner had no intention of taking over control of the Company but was simply seeking information to which it was entitled as a

shareholder. The Company thereafter proposed that it would withdraw the Redemption Notice but in tandem that it would convert the Petitioner's shares to non-voting shares. The Petitioner objected. The Company indicated that the conversion would apply to all shareholders. This says the Petitioner gave rise to the further concern that the conversion was not raised in advance and was not put to shareholders for a vote to amend the MAA. Other shareholders were not notified and it appeared to unfairly target and be discriminatory towards the Petitioner.

20. On 9th July 2020 the Petitioner filed Writ proceedings in the Grand Court against the Company. It obtained an ex parte injunction which restrained the Company from proceeding with the Compulsory Redemption. Thereafter the Company confirmed that it would not proceed as per the Redemption Notice. An attempt to reach a settlement agreement failed.

21. The Petitioner alleges that the Compulsory Redemption Notice was issued for an unlawful and improper purpose and was therefore in breach of the common law and/or an implied term of the MAA. Mr. Ferrer asserts his belief that the Compulsory Redemption Notice was invalid and or unlawful and as evidencing that the Company's directors acted in breach of their duties.

22. According to Mr. Drankiewicz, in his affidavit filed on behalf of the Company, the inadvertently disclosed email chain included statements made by Mr. Bours which acknowledged that there was a limited right to information. The information requests therefore appeared to be an attempt to exert pressure on the Company. The email expressed an intention to "potentially hijack the fund" and gave rise to concerns which led to the giving of the Notice of Redemption on 9th July 2020.

23. On the 27th August 2020, the Company wrote to the Petitioner and indicated formal withdrawal of the redemption notice and the potential for the execution of existing long term plans to redeem the Petitioner's shares after a lock-up period ended.

24. On the 12th January 2021, the Petitioner responded affirmatively to the Company's proposal to redeem its shares in Accolade on the basis that this was to be a full redemption. This was later clarified by the Company to be only a partial redemption. The Petitioner says that

"notwithstanding the difference in understanding, and without further correspondence the Company proceeded with the partial redemption on 15 January 2021."

25. On the 28th January 2021, the Petitioner and two other shareholders, JI Family Holding Limited and Juan Gonzales Diaz Brown sought to convene an Extraordinary General Meeting ("EGM") of the Company in the belief that in accordance with the Confidential Explanatory Memorandum, ("CEM") provided to them on investment that together they held not less than one half of the votes entitled to be cast at the meeting. The purpose of the meeting was to debate a proposed resolution to appoint four (4) new directors nominated by the Petitioner. On the 9th February 2021 the Company responded advising that the Petitioner and the other two shareholders did not hold a sufficient number of shares to be able to call such a meeting. In a further letter on 16 February 2021 the Company informed the Petitioner that it and the other two shareholders held less than 35% of the number of voting shares.

26. On 19th February 2021, the Petitioner sought the intervention of the Court by way of an Originating Summons seeking an Order to require that the Company convene an EGM or alternatively to provide such information as would allow contact to be made with other shareholders. The Summons was served on the Company. The assertion of the Petitioner is that in refusing to convene an EGM, the Company had "resiled from the representation made in the CEM" which was provided to it in July 2018 and in the more recent Confidential Explanatory Memorandum of March 2020.

27. On the 23rd February 2021, the Company issued notice that it would redeem 50% of the Petitioner's shares. The Petitioner sought an undertaking from the Company to maintain the status quo until the Originating Summons could be resolved in Court.

28. On the 4th March 2021, the Company gave notice to the Petitioner of the intention to remove the Petitioner's voting rights pursuant to Article 29.3 of the MAA and to convert the Petitioner's shares to non-voting shares. The Notice of Conversion provided to the Petitioner included an offer to redeem the shares of the Petitioner.

29. The Company says that the partial redemption in January 2021 was done in order to secure to shareholders the advantage of the then high trading prices. According to Mr. Drankiewicz the Petitioner then attempted to take over the Company by calling an EGM. The Petitioner's claim to holding a simple majority of the shares failed to take into account the partial redemption which had taken place in January 2021 and the fact that there had been additional investors since August 2018. He further states that in the face of the continued aggression to the Company it resolved to convert the Petitioner's remaining shares to non-voting shares in accordance with Article 29.3 of the Memorandum and Articles which provides as follows:-

> *"In addition, existing Members who have been issued Voting Shares may have such Shares converted to Non-Voting Shares if the Directors determine, at their discretion, that such conversion is necessary or advisable to avoid possible adverse consequences with respect to the Company or a particular Member provided that the Member will be granted the right to redeem such Shares prior to conversion."*

30. The reasons for conversion are said to include that a number of affiliates of the Petitioner are politically exposed persons which was not disclosed to the Company in breach of the terms of the relevant subscription agreement and that the nominees for directorship are all closely tied to the Bours family. The Resolution of the Board of Directors of the Company listed seven reasons for its statement that:

> *"The Board considers that it would not be in the best interest of the Company, and its investors as a whole, for the Company to fall under the effective control of the Bours family and politically exposed persons, through its Nominees."*

THE AMENDED PETITION

31. The Petitioner seeks leave to amend the Petition pursuant to CWR O.3 r.2 (3) and CWR O.3 r.12. The proposed amendments are set out in a draft Amended Petition. With the exception of the orders sought for joinder and characterisation of the Petition the amendments sought are not opposed by the Company.

32. The Amended Petition sets out five summary grounds as follows:-

i. "The Company sought to compulsorily redeem the Petitioner's shares in the Company in breach of the common law obligation and/or an implied term of the Articles of Association to exercise powers for proper purpose;

ii. The Company failed to convene an extraordinary general meeting of the members of the Company in breach of the terms of its Articles of Association and/or contrary to representations in the Company's Confidential Explanatory Memorandum;

iii. The Company converted the Petitioner's shares into non-voting shares in breach of the common law obligation and/or an implied term of the Articles of Association to exercise powers for proper purpose;

iv. The Petitioner has suffered a justifiable loss of faith in the Company's management; and

v. It is necessary for there to be an independent investigation into the affairs of the Company."

33. Paragraph 61 of the Amended Petition refers to the notice of conversion and alleges five matters as follows:-

i. That the Company discriminated against the Petitioner;

ii. In procuring the exercise of the power by the Company, the directors acted in conflict of interest in that they sought to protect and preserve their own personal positions as directors and maintain control of the Company;

iii. The Company sought to alter shareholders' voting rights and thereby the ability of shareholders to pass, or prevent from being passed, relevant

resolutions, including potential resolutions to appoint or remove directors, appoint an independent inspector and to amend the MAA;

iv. The Company sought to deprive the Petitioner of its shareholder voting rights; and

v. In all the circumstances the Company did not exercise the power for proper purpose.

34. Paragraph 62 of the Amended Petition is under the heading 'Financial Irregularities'. It states that there are a number of apparent financial irregularities which have not been satisfactorily explained by the Company including the following:-

i. The basis for the calculations as to the level of expenses allocated to the Accolade shares.

ii. The reimbursement arrangement for investors who joined the Company prior to December 2017 as to whether this favoured the two directors.

iii. Potentially misleading investor statements - with the assertions that the Company appears to have sometimes selected historical valuation dates.

35. Paragraph 63 of the Amended Petition under the heading "Justifiable Loss of Faith in the Management of the Company" states that as a result of the foregoing it is apparent that the Company's affairs have been mismanaged and that the Company has:-

i. "Unreasonably refused to provide information pursuant to the Information Requests.

ii. Acted in breach of the MAA in demanding the Capital Calls.

iii. Acted for improper purpose and/or in breach of the MAA in the compulsory redemption of the Shares.

iv. Acted contrary to the expressed understanding of the Petitioner by proceeding with a partial redemption of the the Shares.

v. Acted in breach of the MAA, contrary to the representations in the CEM in refusing to convene an EGM.

vi. Attempted to obfuscate the flawed basis on which it was refusing to convene an EGM.

vii. Acted for improper purpose and/or breach of the MAA in the removal of the Petitioner's voting rights pursuant to the Conversion Notice.

viii. Provided financial information indicative of apparent financial irregularities."

THE SECOND AFFIDAVIT OF RONAN GUILFOYLE

36. In March of 2021, the Company appointed its first independent director, Mr. Ronan Guilfoyle of Calderwood. It is said that this was done, in an effort to bolster the Company's corporate governance structure. His First Affidavit is dated 3rd June 2021. He provides a Second Affidavit dated 21st January 2022 in which he states that the matters to which he avers are within his own personal knowledge and are based on his review of the Company's books and records. He speaks to two issues, the shareholders of the Company and indemnification of the directors. He states that as at the date of his affidavit, the Company had 27 different shareholders. The Petitioner is one. The Company has issued 38 different classes of shares and the Class A Sub –Class Accolade E-1 Series invested in by the Petitioner is only one class. He also states:-

"6. As at the date of this affidavit Kristopher Drankiewicz and Liliana Macias own only a small proportion of the shares in the Fund (which are held in part in their own names, and in part in the names of nominees, being their retirement funds). Together these shares represent approximately 6.4% of the net asset value of the Fund."

37. As to indemnification of directors, he states that pursuant to Article 52 of the Company's MAA, the directors are by virtue of confirmation in board resolutions entitled to be indemnified by the Company in respect of certain matters. Following information as to the Petitioner's summons, the Company has established an independent committee which is chaired by him for the purpose of reviewing any claims for indemnification from the two directors.

38. Article 52.3 provides as follows[2]:-

> "*The Company shall advance to each Indemnified Person reasonable attorneys' fees and other costs and expenses incurred in connection with the defence of any action, suit, proceeding or investigation involving such Indemnified Person for which indemnity will or could be sought. In connection with any advance of any expenses hereunder, the Indemnified Person shall execute an undertaking to repay the advanced amount to the Company if it shall be determined by final judgment or other final adjudication that such Indemnified Person was not entitled to indemnification pursuant to this Article. If it shall be determined by a final judgment or other final adjudication that such Indemnified Person was not entitled to indemnification with respect to such judgment, costs or expenses and any advancement shall be returned to the Company (without interest) by the Indemnified Person."*

THE COMPANIES WINDING UP RULES

39. CWR O.3 r.11 (1) provides as follows:-

> "*Upon the presentation of the contributory's petition, the petitioner must at the same time issue a summons for directions in respect of the matters, contained in Rule 12".*

[2] Exhibit to the First Affidavit of Daniel Alberto Salazar Ferrer dated 9th July 2020

40. CWR O.3 r.12 provides as follows:-

> *(1) Upon hearing the summons for directions, the Court shall give such directions as it thinks appropriate in respect of the following matters-*
>
> *(a) Whether or not the company is properly able to participate in the proceeding or should be treated merely as the subject-matter of the proceeding;*
>
> *(b) Whether the proceeding should be treated as a proceeding against the company or as an inter partes proceeding between one or more members of the company as petitioners and the other member or members of the company as respondents;*
>
> *(c) Service of the petition upon persons other than the company (as may be appropriate having regard to the directions given under paragraphs (a) and (b) of this Rule.*

41. There is guidance in the Financial Services User Guide FSD User Guide – C 6.1, 2, 3 and 4 as follows:-

> **"C6.1 Presentation of petition and summons for directions**
>
> When presenting a contributory's petition on the just and equitable ground, the petitioner must file the petition, a verifying affidavit(s), the supporting affidavit sworn by the qualified insolvency practitioner nominated for appointment as official liquidator and a summons for directions in CWR Form No.5. The Registrar will assign the matter to a Judge and fix a date for hearing the summons for directions. A date for hearing the petition will be fixed by the Judge as part of the order for directions.

C6.2 Characterisation of the proceeding

At the hearing of the summons for directions the Judge will consider all the matters set out in CWR O.3 r.11. In particular, the Judge must always determine whether the proceeding should be treated as (a) a proceeding against the company, in which case it will be treated as the respondent or (b) an inter partes proceeding between one shareholder(s) as petitioner and another shareholder(s) as respondent. The way in which the proceeding is characterised determines the manner of its future conduct.

C6.3 Directions — proceeding against the company

If the company is treated as the respondent to the petition, it follows that the Judge must always consider how the petition will be drawn to the attention of the shareholders (other than the petitioner) who are entitled to be heard. The Court may direct that the other shareholders be served and/or that the petition be advertised. In the case of a mutual fund, the Court will normally direct that its administrator send copies of the petition and affidavits to the registered shareholders by whatever method of communication is normally used in the ordinary course of business. The Court will fix a date for hearing the petition and set a timetable for the exchange of affidavit evidence.

C6.4 Directions — inter partes proceeding between shareholders

If the company is treated as the subject-matter of the petition (as it will be in any case in which the petitioner alleges that its management is deadlocked, for example), the opposing shareholders will be treated as the respondents and the Court will direct that they be individually served. In these circumstances, it will not be appropriate for the petition to be advertised. The Court will give directions for trial and will consider directing service of pleadings, exchange of affidavit evidence and attendance for cross-examination. Any application for a pre-emptive costs order should be made at the summons for directions."

APPLICABLE PRINCIPLES

42. Both Counsel placed significant reliance on the judgments of the Grand Court in the cases of ***In the Matter of Freerider Limited*** [3] and ***In the Matter of China Shanshui Cement Group Limited***[4]. The earlier case drew an analogy between a petition alleging unfair prejudice under s.459 of the English ***Companies Act 1985*** and the provisions in Cayman Islands legislation for applications for winding up on the just and equitable ground.

43. Both Counsel argued that the principles discussed in these cases support their respective positions. Counsel also referred to a number of earlier English cases. These included the two which are set out below.

44. In the case of ***Re a Company No. 007281 of 1986***[5] Vinelott J on an application to strike out an investment company as a respondent to a petition refused to do so. The learned Judge described the difference between a petition under s.459 of the English ***Companies Act 1985*** and ordinary litigation. In the latter the issues raised affect only those against whom allegations are made. In contrast a petition is more akin to an administrative action where those having an interest in the relief sought should be made parties or be represented. The learned Judge cited with approval a line of English authorities on the point and stated:-

> *"In practice, this means that in the case of a small, private company every member ought to be joined. If, as is usually the case, the relief sought is the purchase of the petitioner's shares by the respondents against whom allegations of unfairly prejudicial conduct are made, or the purchase of their shares by the petitioner, other shareholders would be affected if the articles contain pre-emption provisions which would be overridden by the purchase, or if the balance of the voting rights might be affected to the detriment of other members. If the relief sought is the*

[3] 2009 CILR 604
[4] FSD No 161 of 2018 unreported 21st January 2021
[5] [1987] 3 BCC 375

> *purchase of the petitioner's shares, or of the shares of those members against whom allegations of unfairly prejudicial conduct are made, by the company, the balance of voting rights would, again, almost inevitably be affected. Clearly, if a winding-up order is sought or an order regulating the conduct of the company's affairs in the future, those entitled to vote on a resolution for the winding-up of the company or the appointment of directors, are entitled to be heard.*
>
> *There may be occasions where, it is unnecessary to join all the members of a company, for instance if the articles contain no pre-emption provisions and if some of the members are mere investors who have taken no part in the formation or management of the company – a situation which might arise, for instance, in the case of a public listed company, the affairs of which are under the de facto control of a small group of shareholders. It may be that in such a case it would be unnecessary to make all the members respondents, or to serve the petition on all of them, and that it would be sufficient that they be given notice of the petition so that they may apply to be joined if they so wish. Under the Companies (Unfair Prejudice Applications) Proceedings Rules 1986 (S.I. 1986 No. 2000), on the first hearing of a petition the court is required to give directions as, to the service of a petition on any person who has not been made a respondent. If there is any doubt as, to whether a member or director ought to be made a respondent to, or served with a petition or given notice of the petition, that doubt can be resolved at an early stage."*

45. In the case of ***Re a Company No. 04502 of 1988 ex parte Johnson***[6], the Court had before it an application which sought in part to restrain certain respondents to a petition under s.459 of the ***Companies Act 1985*** from causing the company to be represented and to incur costs save with respect to discovery. The Court described the basis for the application as follows:-

[6] [1991] BCC 234

> *"That application is based upon a line of authority which has been becoming evident in recent years. The principle was drawn to the profession's attention by the decision of Hoffmann J in Re Crossmore Electrical and Civil Engineering Ltd (1989) 5 BCC 37 , where at p. 38G the judge said:*
>
> *"The company is a nominal party to the sec. 459 petition, but in substance the dispute is between the two shareholders. It is a general principle of company law that the company's money should not be expended on disputes between the shareholders …""*

46. The Court considered the general principle and noted that apart from certain circumstances where a company may have a particular interest, a company should usually have no business being involved in a s.459 petition. Following review of a number of cases, Harman J stated:

> *"The train of authority being well established, it seems to me quite clear that, if it is shown that directors of a company have been causing the company's money to be spent on financing the resistance either to a "pure" sec. 459 petition or, according to Plowman J in Re A & BC Chewing Gum and myself in Re Hydrosan, in financing the company's resistance to a member's winding-up petition based on the just and equitable ground, the court should prevent such expenditure. Such expenditure is a misfeasance, there is no excuse for it in law and it is not a question of an arguable case being raised showing that it may be right to permit misfeasances. Misfeasances are not matters that are permitted by the courts and there is no question of an arguable case at all."*

47. The case of ***In Re a Company No. 04502 of 1988 ex parte Johnson*** was cited with approval by the Grand Court in the case of ***Freerider.*** In the latter case the company in question was a quasi-partnership between the petitioner and the respondent who each held 50% of the voting Class A shares of the company. The petitioner who was also a director sought the winding up of the company following the breakdown of the relationship between himself and the respondent. The allegation was that there was a complete deadlock between them.

48. On an application for directions pursuant to O.3 r.11 the Court (Foster J.) directed that the company should be treated as the subject matter of the petition and that the petition be heard inter partes between shareholders. The company remained as a nominal defendant.

49. The Court held that it was evident that this was a dispute between principal shareholders rather than one involving the company and concluded that the company had not discharged the burden on it to show that it was necessary or expedient in the interests of the company as a whole to participate in the hearing.

50. The learned Judge reviewed a line of English cases in which the courts declined to allow companies to actively participate in proceedings for the winding up of a company on the just and equitable ground where the real essence of the dispute was between shareholders rather than a dispute with the company itself[7]. These included the cases of ***Pickering v. Stephenson***[8], ***In re A. & B.C. Chewing Gum Ltd***[9], ***In re Crossmore Elec & Civil Engr. Ltd***[10] and ***In re a Company No, 005685 of 1988 ex. p. Schwarcz***[11]. In each case there had been affirmation of the general principle that the funds of the company should not be spent on litigation where the real dispute was between shareholders.

51. The learned Judge cited with approval the judgment of the Court in ***Re Hydrosan Ltd***[12] referring to the distinction between a claim by a creditor as distinct from that of a shareholder for a just and equitable winding up. Notwithstanding the possibility that a contributory's petition may also give rise to the dissolution of a company, it is not in reality hostile litigation against a company.

52. The learned Judge also referred with approval to the case of ***In re a Company (No. 001126 of 1992)***[13]**.** This was a case in which a company sought directions to permit it to actively

[7] Paragraph 21
[8] [1872] L. R. 14 Eq. 322
[9] [1975] 1 W.L.R. 579
[10] (1989) 5 BCC 37
[11] (1989) 5 BCC 79
[12] [1991] BCC 19
[13] [1993] BCC 325

participate in a petition brought against it under s.459 of the English ***Companies Act***. The test with respect to such participation was identified in the following way:

> *"Having reviewed the cases to which I have already referred, Lindsay, J. concluded that the cases suggested to him that the test of whether such participation (by the company in what was in essence a dispute between shareholders) and expenditure in doing so is proper is whether ([1993] BCC at 333) it is "necessary or expedient in the interests of the company as whole." He went on to say (ibid.):*
>
> *"Fourthly, that in considering that test the court's starting point is a sort of rebuttable distaste for such participation and expenditure, initial scepticism as to its necessity or expediency. The chorus of disapproval in the cases puts a heavy onus on a company which has actively participated or has so incurred costs to satisfy the court with evidence of the necessity or expedience in the particular case. What will be necessary to discharge that onus will obviously vary greatly from case to case.*
>
> . . .
>
> *Finally on the law, I comment that I do not see this analysis as opening floodgates such that the courts will be swamped with applications of the kind before me. In the vast majority of s.459 petitions there will, I think, be no real prospect of satisfying the tests I have mentioned and applications of the kind before me will be so hopeless as not even to be embarked upon."*

53. Foster J. also reviewed the case of ***Arrow Trading & Invs. v. Edwardian Group Ltd (No. 2)***[14].

> *34 The headnote to the decision in the Edwardian Group further indicates (ibid.) that Sir Francis Ferris went on to say that "<u>the essential question was whether it is right to say that [the company] had a separate and</u>*

[14] [2004] BCC 955

<u>independent position on the issue of [the directors'] remuneration."</u> He said that—

> *"the essence of the petitioners' claims was that the petitioners as shareholders had been unfairly treated as a result of the decisions of the majority [shareholders]. Those decisions were essentially the decisions of individuals, whether in their capacity as directors or as shareholders. They were embodied in resolutions and the like which were technically describable as 'acts of the company,' but the reality of the position was that what was complained of was treatment resulting from a decision or series of decisions made which caused [the company] to endorse what was said to be the unfair remuneration policy."*

He further said that—

> *"it did not seem that [the company] had a separate and independent position and it certainly did not seem expedient that it should be allowed to take an active part in the proceedings simply for the purpose of putting before the court the evidence of [two of the directors] in the manner which they personally preferred. What [the two directors] wished to do was to defend [the company's] remuneration policy and thus, in substance if not in intention, support the position of the respondent shareholders."*
>
> *He said "there could be no objection to an order to restrain the company expending its money or assets for the purpose of justifying the remuneration policy in this way" and accordingly an injunction was granted restraining the company from expending its money and actively participating in the petition in the manner in which it had indicated it wished to do."* (Emphasis underlined.)

54. Foster J. rejected the argument that there was a distinction between the English position and the Cayman Islands position despite there being no direct equivalent to s.459 of the

Companies Act in the Cayman Islands. The conclusion was the general principle is still applicable. It was stated:

> *"However, for the reasons I have stated, I do not consider that the fact that this is only a petition for winding up on just and equitable grounds and no more makes any difference to the applicability of the general principle. The principle applies whenever the reality is that the dispute is between shareholders and not a dispute with the company itself."*

55. Foster J. commented that the CWR provisions of O.3 r.12(2) (a) and (b) provide a mechanism which will enable the court at an early stage to carry out the required analysis to determine given the particular circumstances of the case at hand, what should be the level of participation of a company against whom a petition has been brought. The learned Judge also noted that by s.24 (3) of the ***Judicature Act***, the Court has the jurisdiction to award costs against anyone whether or not a party to the proceedings[15].

56. The conclusion was that that the issues raised in the petition and supporting affidavit showed clearly that the dispute was in reality one between the two shareholders rather than one between one shareholder and the company itself. The company was simply the subject matter of the proceedings[16].

> "*In the present case, it is equally true that if a winding-up order is made, the company will be wound up and eventually dissolved but in this case also ([1991] BCC at 21) "the wrongs claimed and the nature of the allegations are of wrongs by those in control of the company against a shareholder rather than by the company itself in any real sense." To suggest, in the circumstances of this case, that the company itself has some separate and independent interest in the proceedings is quite artificial and ignores the reality that what is in issue are the allegations of Mr. Heinen of wrongs by Mr. Le Comte. There is no claim against the company itself except in the most technical and notional sense. The company*

[15] Paragraph 39 of the judgment
[16] Paragraph 44 of the judgment

must, of course, remain as a nominal respondent but it has, in my view, no relevant interest of its own in the proceedings."[17]

57. In the case of ***China Shanshui,*** the Petitioner, Tianrui (International) Holding Company Limited was a shareholder in the company, China Shanshui Cement Group Limited. It alleged that two other shareholders CNBM and ACC had acted unfairly and or oppressively towards it and that they were parties to an agreement to take control of the company to its detriment by diluting its shareholding.

58. The issues before the Court on a Re-Amended Summons for directions were firstly whether there should be the joinder of the two shareholders CNBM and ACC as respondents to Tianrui's Petition. Secondly how the proceedings should be characterised pursuant to CWR O.3 r.12 (2) (a) and (b). The Court concluded that having regard to the grounds upon which the Petition was based and the allegations of misconduct against the two shareholders it was appropriate that the two shareholders be joined. The Court declined to give further directions before hearing from all parties.

59. Following a careful review of the relevant case law and applicable rules of court, Segal J, detailed a number of conclusions arising therefrom. These are summarised as including the following:-

i) The court has jurisdiction to order the joinder of shareholders upon the hearing of a summons for directions.

ii) An order for joinder may be made as a stand-alone order irrespective of whether or not an order is made for the characterisation of the proceedings pursuant to CWR O.3 r. 12 (1) (a) and (b).

iii) Where the court makes an order that the proceedings be characterised as an *inter partes* proceeding between members, a necessary and

[17] Paragraph 45 of the judgment

consequential procedural order would be for the joinder of those shareholders if they were not already a part of the proceedings.

iv) Even where the court makes an order that the proceedings be treated as proceedings against the company, the court may still make an order for the joinder of shareholders where the circumstances justify such joinder.

60. The learned Judge expressed the view that the circumstances where joinder of shareholders as additional respondents to the company would be appropriate include where the petitioner alleges that shareholders are implicated in the misconduct alleged in the Petition.

61. The reason for this conclusion was expressed in this way:-

> *"(n) …Such shareholders would have a proper interest in participating in the proceedings as a party to respond to or defend themselves against such allegations. But joinder may also be appropriate before the Court determines whether to give a direction that the petition be treated as proceeding against the Company or inter partes proceeding between shareholders. If joinder is justified in either case and the Court considers that the relevant shareholders should be joined and given an opportunity to make submissions on the characterization issue, the Court can make an order for joinder and for service of the petition and summons for directions and adjourn the hearing to a later date to allow that to happen."*

62. It was further stated:-

> *"(q) A shareholder whose conduct is relied on and criticized in the petition whose conduct is said to be the basis on which a winding up order is justified should be a party for reasons of procedural fairness, to ensure that they have the rights and benefits of being a party and are able to defend the allegations made against them and to ensure that [the] Court can make appropriate findings with respect to such allegations. It will, of course, be a matter for the shareholder to decide whether to take an active role in the proceedings but the fact that it does not intend or wish to do so does not preclude the Court from making an order for joinder (where the relevant shareholder has had an opportunity to apply to be joined but has not done so, the Court will need to be satisfied that it is appropriate to compel them to become a party, although if joined pursuant to an interlocutory application which was not served on them and on which they*

> *were not heard, they would always have the opportunity subsequently to apply to be removed as a party).”*

63. The learned Judge concluded that an adequate and proper ground for joining a shareholder as a respondent is the fact of a clear allegation against the shareholder and a claim in the petition that the shareholder is a party to the misconduct on which the petition is based[18].

64. With respect to the need for joinder of all the shareholders of a large public company, the learned Judge said this may not be necessary:-

> *“But in the case of a large public company whose affairs are under the de facto control of a small group of shareholders and other shareholders are mere investors who have taken no part in the management of the company, it may be unnecessary to make all the members respondents, or to serve the petition on all of them – it would be sufficient that they be given notice of the petition so that they may apply to be joined if they so wish.”*

65. With respect to the issue of characterisation, the Court accepted the submissions of the company that CWR O.3 r. 12 (1) (a) and (b) although set out in two sub paragraphs address the same question and issue and require the Court to make a choice between the company or shareholders as respondents. Thus it would not be permissible for the Court to make an order that the proceedings be treated as *inter partes* between both the petitioner and the company and the petitioner and the company as well as the two shareholders. On the issue of characterisation, the Court expressed initial views noting that CWR O.24 r. 8 (2 or 4) dealing with cost orders requires to be kept firmly in mind when considering the purpose for characterisation. The Court said that the approach taken by the rule reflects the general principle of company law that is discussed in a number of cases that a company’s money ought not to be spent in disputes between its shareholders:-

> *“authorisation by the directors of the payments by the company of the cost of opposition to the petition constitutes a breach of the directors’ duties and the company will not be required to pay the costs of the petitioner either.”*

[18] Paragraph 32 s.

66. Being mindful of the general principle, the court needs to make an assessment albeit at an interlocutory stage as to whether the company's funds should be spent on the costs of the proceedings. The assessment would be made based on the nature of the dispute in so far as the court is able to determine this from the petition or other evidence filed up to that stage. The court would be endeavouring to identify the real nature of the dispute, with the critical question being whether the company can show that independent of its shareholders it has a real interest in defending the petition. The Court stated:-

> *"The principle applies whenever the reality is that the dispute is between shareholders and not a dispute with the company itself. The dispute will be treated as one between shareholders and not a dispute with the company itself where the Company cannot be said, or to the extent that it cannot be considered, to have an interest of its own which requires protection and justifies its participation in the proceedings and the use of its own funds to pay the cost of such participation. A critical question is whether the company can show that it has a real interest independent of its shareholders in defending the petition (does the company have a separate interest to protect?). As Foster J. said in Freerider at [45], the Court must decide whether the company has any independent interest in the dispute."*

67. The Court concluded that in circumstances where if the allegations of Tianrui were correct that the other shareholders of the company were not independent but support CNBM and ACC, the existence of other shareholders could not be considered to be a sufficient basis to conclude that the company had a separate and independent interest in participating in and defending the petition.

THE ISSUES

68. In the instant case, the summary submissions are as follows. Counsel on behalf of the Petitioner argued that the Court has jurisdiction to make an order for joinder of the "controlling shareholders" and ought to exercise its discretion accordingly. This given that the Petition is based on their misconduct and in light of the general principle which is established in the cited cases above that a company's money ought not to be used to defend a dispute which is in reality one between shareholders.

69. Counsel on behalf of the Company submitted that the Court does not have jurisdiction to make an order for joinder where the applicable rule is that set out in CWR O.3 r.12 and where there is no activity alleged against Mr. Drankiewicz and Ms. Macias in their capacity as shareholders. Counsel argues that their shareholding is incidental to the allegations made and cannot serve as a proper basis to ground the jurisdiction of the Court. Counsel submits further that should the Court conclude that there is jurisdiction, the Court ought not to exercise its discretion to order joinder or characterisation of the proceedings as between shareholders given the real nature of the dispute.

THE SUBMISSIONS

ISSUE 1 – JURISDICTION

70. Counsel on behalf of the Petitioner highlighted the background to and various aspects of the Petition and submitted that the basis for the Petition is firmly grounded upon the misbehavior of the directors. It is also submitted that the interests of the Company are separate and independent to the interests of the two directors, Kristopher Drankiewicz and Liliana Macias. Counsel described these two persons as "controlling shareholders" and submitted that if the allegations are correct, the Company is a victim of their misconduct. It would in these circumstances be wholly wrong and in conflict of their interests and further breach of duty to the Company that these controlling shareholders should cause the Company to defend their personal interests at the Company's expense.

71. Counsel submitted that the Court does have jurisdiction to join the two as respondents and to determine that the proceedings are *inter partes.* Counsel said that the argument of the Company in opposition to this mischaracterizes the nature of the Petitioners' application, fails to have regard to the fact of their status as controlling shareholders, and seeks to define them only by their position as directors.

72. Counsel said that the Court's jurisdiction is clearly engaged by the fact that the two directors are also shareholders which is confirmed by the Second Affidavit of Mr. Guilfoyle and that in light of this, the real issue for the Court is not one of jurisdiction but whether to exercise its

discretion to join the controlling shareholders or otherwise characterise the proceedings as *inter partes*.

73. Counsel referred in detail to the judgment of the Grand Court in ***Re China Shanshui Cement Group Ltd***. and described it as being similar to the instant case. Counsel submitted that the case is authority for the proposition that a party that is responsible for the alleged conduct that gives rise to the basis for a winding up petition is a proper respondent to it. It was accepted therein that a clear allegation made against shareholder who is said to be a party to misconduct is an adequate and proper ground for joinder. Counsel referred to the statements of the Court in that case that even where the Court makes an order that the proceedings are to be treated as a proceeding against the Company, the Court may still make an order for the joinder of shareholders as respondents.

74. It is argued that the instant case can be characterised as a dispute between shareholders with shareholders as the Petitioner and shareholders who are also directors as respondents. The allegation is that they were exercising their power as shareholders improperly through their mismanagement of the Company. As the controlling shareholders about whom allegations are made, they should therefore be respondents in this case.

75. Counsel said that the fact that their shareholding is small or that the allegations arises from their misconduct in controlling the Company through their position of directors does not detract from this position. He urged that they should be joined to give them an opportunity to respond to the allegations of misconduct and if they chose not to actively participate then the Court will be able to draw such inferences as it wishes from their non- participation. If they do actively participate they should be bound by any findings of fact in relation to the allegations of misconduct made against them.

76. Counsel stated that however minor the fact is that they have an interest in the Company as shareholders and that this is what allows the Court to thereafter consider their conduct. Counsel emphasized that at the material time the two directors had complete control of the Company. Counsel said:

"The way they have in this particular case, acted by way of misconduct, is, yes, through their roles as directors, but that doesn't negate the fact that they have an interest as shareholders. It doesn't negate the fact that as a result of their being directors, they have control of the Company.

This is two individuals that have had, at least during the relevant period, complete control of the Company. No independent director at that stage at all. They have a shareholding and they are acting, certainly on the petitioner's claim, to discriminate against other shareholders, the petitioner and the requisitionists, and in every other way to act outside their powers and in breach of the company's own constitution."

SUBMISSIONS OF THE COMPANY

77. Counsel for the Company on the jurisdiction issue submitted that based on the analysis of the Court in the case of ***China Shanshui*** the order for joinder sought by the Petitioner would not be 'valid jurisdictionally'.

78. Counsel was critical of what he described as a seismic shift in the arguments of the Petitioner. He stated that up until the day of hearing, the application of the Petitioner had been to join the two individuals not as shareholders of the Company but as directors. He said that it is difficult to see how individuals who hold a mere 6.4% of the shares of the Company could have control in their capacity as shareholders and be properly described as "controlling shareholders".

79. He said that the shareholding of the two is wholly incidental to this case and that the Petitioner only became aware of this from the Second Affidavit of Mr. Guilfoyle which was recently filed.

80. Counsel said that the circumstances are very different from the cited cases of ***Freerider***, ***China Shanshui*** and ***In re A. & B.C. Chewing Gum Ltd***. Those were cases where the shareholders

in question had large and influential shareholdings and because of their shareholdings also had directorships.

81. He said that an important distinction between those cases and the instant case is that in the instant case there is no pleading that the two individuals exercised their powers improperly as shareholders.

82. Counsel invited the Court to review the supporting affidavit of Mr. Ferrer which clearly sets out the basis for joinder by describing the two individuals as directors of the Company and the misconduct of directors as central to the Petitioner's application.

83. Counsel submitted that there are no allegations of shareholder misconduct in the instant case and no allegation that the two individuals did or could do anything as shareholders. He said that the Petitioner is in fact asking for them to be joined in respect of alleged wrongful actions taken as directors not as shareholders and that this does not mean that they may be properly joined as respondents to the Petition.

84. The submission is that the cases do not support joinder of directors as respondents to the Petition. Counsel said:-

> *"One will find reams of cases. I have included three in the bundle for examples, Re BAF Latam Credit Fund, Re Sterling Macro Fund and Re Washington Special Opportunity Fund, Inc., where the Petition is very similar to the Petition my learned friend put in. This Court is very, very familiar with winding-up petitions in a just and equitable context … where a shareholder brings a winding-up petition and alleges wrong doing against management of the directors. That is well travelled territory in this Court. One will search in vain for the Court having made an order like the one my friend contends for this morning, and the reason for that is it is simply not available, and if it is available it is simply not appropriate."*
>
> *In all of those cases I have mentioned, I could name a dozen more if needed. The Petition was brought by a shareholder and the Company, the Fund defended the Petition. The Court ordered that the Fund defend the Petition.*

In fact my learned friend's own position in March last year was the same. In his first set of submissions back in March, the order sought was that the Company be the Respondent. It's an entirely orthodox order. He was right the first time with respect My Lady. Nothing has changed. His case hasn't changed. His mind has changed but his case hasn't changed.

But in none of those cases do you ever see the Court make an order of the kind for which my learned friend contends. It's simply not available. The Court cannot order the directors, be joined and again to be clear, that is the order being sought, that directors be joined, not members. They may also be members but it's completely by the by. They have done nothing qua member or alleged to have done nothing qua member."

85. Counsel sought to distinguish the case of ***China Shanshui*** which involved three major shareholders of the company, two of whom were alleged to have acted to cause the dilution of the shareholding of the third. Counsel drew the Court's attention to paragraphs 35 and 36 of that judgment:-

"35. The decision as to which orders which should be made pursuant to CWR O. 3 r. 12,(1)(a) and (b) has a direct effect on (and CWR O.3, r.12 (1)(a) and (b) are linked to) the costs orders to be made following the conclusion of the proceeding. The drafting of CWR O.24, r.8(2)(a) and (b) strongly suggests that it was intended and understood by the draftsman of the CWR that the Court has a choice between two alternatives – either the Court directs that the company itself is properly able to participate in the proceeding or that the petition be treated as an inter partes proceeding between shareholders. The implication of the reference to only two possibilities is that where the Court directs that the Company is properly able to participate in the proceeding, the proceeding is characterised and treated as a proceeding against the Company. This interpretation is supported by the explanation provided in the User Guide. As I have noted, at C6.2, the User Guide states that "the Judge must always determine whether the proceeding should be

treated as (a) a proceeding against the company, in which case it will be treated as the respondent or (b) an inter partes proceeding between one of the shareholder(s) as petitioner and another shareholder(s) as respondent."

"36. CWR O.24, r. 8(2) links the Court's decision on characterisation to the costs issue. CWR O.24, r. 8(2) ensures that where the proceedings is characterised as a proceedings against the company, the costs of the successful petitioner are to be paid by the company out of its assets (as a general rule). Where the proceeding is characterised as an inter partes proceeding between shareholders then none of the costs should be paid out of the assets of the company and the unsuccessful shareholders must pay the costs of the successful shareholder (again, as a general rule).

*This approach reflects the general principle of company law (the **Principle**), which was referred to and held to apply to just and equitable petitions in Freerider and was discussed in the other cases referred to by Mr. Lowe Q.C. and Mr. Flynn Q.C., that a company's money should not be spent on disputes between its shareholders. In such a case, authorisation by the directors of the payment by the company of the cost of opposition to the Petition constitutes a breach of the directors' duties and the company will not be required to pay the costs of the petitioner either."*

86. Counsel submitted on the point of jurisdiction that the Court has to look at the substance of the application which in this case is in reality an application to join directors. If that is what it is in substance then there is no jurisdiction to join directors.

87. In written submissions Counsel on behalf of the Petitioner submitted that the Court's power to amend a winding up petition and amend the parties to a petition by joining additional respondents is at CWR O.3 r.2 (3) and CWR O.3 r.12 (1) (k). The latter provides that upon the hearing of a summons for directions the Court shall give direction as appropriate with respect to such other procedural matters as the Court thinks fit.

88. Counsel for the Petitioner also placed reliance on the English case of ***Caldero Trading Limited v. Beppler & Jacobson Limited & others***[19] for his submission that the court's power to join respondents to a petition is a wide one. In that case the English Court considered an application to join two additional respondents to a petition brought on the just and equitable ground pursuant to s.994 of the ***Companies Act 2006*** (the earlier section was 459 of the ***Companies Act 1985***) and s.996 of the Act. The Court said that joinder of a party is governed by the Civil Procedure Rules (CPR) Part 19.2 (2) which provides:

> "*The court may order a person to be added as a new party if— (a) it is desirable to add the new party so that the court can resolve all that matters in dispute in the proceedings; or*
>
> *(b) there is an issue involving the new party and an existing party which is connected to the matters in dispute in the proceedings, and it is desirable to add the new party so that the court can resolve that issue."*

89. The submission made to that Court was summarised as follows:-

> *"Mr Hollington submits that Lawson and Mr Scheklanov have an obvious and fundamental involvement in two of the most important issues in the petition, namely the efficacy and propriety of the agency agreements and the nature of the agreement between Mr Becirovic and Mr Lazurenko as agent for Mr Scheklanov. These agreements are at the root of the alleged unfairness to Mr Becirovic."*

90. The Court concluded:-

> *"Once it is clear that this issue is or may have to be decided in the petition, it seems to me to follow inevitably that Lawson and Mr Scheklanov should be joined as parties under CPR 19.2(2)(b). They have every interest in resisting the finding which is being sought, which will affect them. Moreover it is plainly important that they be bound by the outcome of that issue."*

[19] [2012] EWHC 1609

91. In response to these submissions Counsel for the Company submitted that the reference to other such procedural matters in CWR O.3 r.12 (1) (k) must be read as referring to matters other than those dealt with above. It cannot be referring to characterisation or joinder which is already specifically dealt with. Counsel submitted further that the case of ***Caldero*** refers to a different statutory and procedural framework i.e. the CPR rather than the local CWR. It was also concerned with a petition brought on the ground of prejudice as well as the just and equitable ground. Counsel also notes that the two persons sought to be joined were not directors but were described as an economic stakeholder and a beneficial owner.

92. With respect to the second issue of characterisation, Counsel for the Petitioner submitted that for the same reasons which justify joinder the Court should not only join the controlling shareholders at this stage but also determine that these proceedings are properly characterised as *inter partes* proceedings between shareholders.

ISSUE 2 – EXERCISE OF DISCRETION

93. Counsel for the Petitioner argued that the Court should exercise its discretion to make the orders requested for the following reasons. The two directors were the only directors during the period of the alleged misconduct. They controlled the Company and acted in excess of their powers, for an improper purpose, in breach of their duties to the Company and in order to protect their own interests rather than in the best interests of the company. This says Counsel is the basis for the application for winding up. It is thus the Petitioner's position that they should be joined since it is their misconduct which is the entire subject matter of the dispute.

94. Counsel submitted that if the Petitioner is successful, it will seek costs relief from these controlling shareholders. Should the Company's approach be followed, the Company's funds would be used to defend allegations of the personal misconduct of those individuals. The individuals would in defending the allegations themselves be in breach of their duty to the Company. This Counsel urged would be a "blank cheque approach" which would be given to misbehaving directors. Counsel said:-

> *"It would be wholly wrong in principle if the Petition succeeds for the costs of the controlling shareholders unsuccessful attempt to defend the Petition to be borne by the Company, of course ultimately the Petitioner."*

95. In these circumstances Counsel argued that the Court should exercise its discretion to join the two individuals and to order that the proceedings are *inter partes* so that the issue of their misconduct can be properly determined by the Court and in order that they are bound by any findings of fact made. If appropriate it would then be open to the Court to make costs orders against them. There would be no prejudice in their being joined as if the Petition failed the costs would be borne by the Petitioner.

96. Counsel for the Petitioner drew the Court's attention to the judgment of the Court in the case of ***Freerider*** in which Foster J referred to the case of ***In re A. & B.C. Chewing Gum Ltd*** as follows:-

> *"22 This was a hearing involving two related matters before Plowman, J.: a contributory's petition for winding up on the just and equitable ground and an action by the petitioner against directors of the company and the company itself seeking a declaration that any payment out of the assets of the company of the costs of directors of defending the winding-up petition involved a breach by the directors of the articles of association of the company and a breach of their fiduciary duties as directors. In the circumstances of the case the judge made a winding-up order. In relation to the action for the declaration, it was common ground that the action must succeed and the declaration was granted accordingly. There was apparently no doubt that the company should not be paying for the defence of the winding-up petition in which it had no direct interest of its own and in which the real interest was that of the directors."*

97. Counsel submits that the Company in the instant case can have no direct interest in the case because given the actions set out in the Petition, the Company is a victim of its directors and has no independent position and can have no individual role. There is no issue between the Petitioner and the Company itself bearing in mind the nature of the dispute. The fact that it is

a Petition for a just and equitable winding up does not provide the Company with a separate interest. Referring to the statements made by the English Court in ***In re Hydrosan Ltd.*** Counsel submitted further that the Petitioner's petition is not in reality hostile litigation against the Company, it is a dispute between shareholders and directors. Shareholders are very often directors as in the case of ***Re A. & B.C. Chewing Gum Ltd***. and in other cases referred to in the judgment of the Court in the case of ***China Shanshui***.

98. Counsel submitted that the directions which the Court is required to give is properly informed by an assessment of whether the Company should be liable for costs. While it is not a final determination as to who should bear these, it does provide for fairness that the proper parties are added at the interlocutory stage.

99. By reference to the case of ***Freerider***, Counsel submitted that there is a burden on the Company to show that it is necessary or expedient or in the interest of justice as a whole to show that the company should be an active participant. Such a burden could not possibly be discharged in this case when the nature of the dispute as is set out it in the petition is considered. Counsel said:-

> *"It cannot be necessary or expedient for the Company to defend allegations of misconduct by its own directors, and now alleged to be acting in breach of duty to the Company. In fact it would be inappropriate, not only is it not necessary or expedient, it would be utterly inappropriate for the Company's expenses to be funding that type of litigation."*

100. Counsel for the Company in response submitted that even if the Court does have jurisdiction, it ought not to exercise its discretion to order joinder. Counsel argued that there are no cases which consider member versus director and although some of the cases refer to directors the term is used interchangeably with shareholders, in particular in the cases of ***Freerider Limited*** and ***A. & B.C. Chewing Gum Ltd***. The allegations are that shareholders were appointed directors. Counsel submitted further that in each of the cases there is a similar fact pattern of major shareholdings which were far from incidental. In each case the shareholding was central to the allegations and to the decisions of the Court.

101. Counsel submitted that contrary to the submissions of the Petitioner in the instant case, the real question for the Court is not who is alleged to have done wrong, but who has the real interest and does the Company have its own economic interest. This is set out in the cases of ***Freerider*** and ***China Shanshui***. Does the company have a separate interest to protect?

102. In the case of ***Freerider*** where the two shareholders each held 50% of the voting shares of the Company, the Court concluded that in reality the company was a quasi-partnership and that the dispute was between the two and not a dispute with the Company itself. That Court considered "the real economic interest".

103. Counsel drew the Court's attention to the summary facts of ***In re A. & B.C. Chewing Gum Ltd.*** chewing Gum:-

> *"Since 1967, the petitioner's held one third of the company's shareholding on the basis that they should have equal control with the two individual respondents, who were brothers and directors of the company and owned the other two thirds of the equity..."*

104. Counsel said that in the instant case, there are 27 shareholders in the Company, four of which are the two directors named, one is the Petitioner leaving about 20 shareholders who deserve to be represented in these proceedings through the Company. Counsel urged that the Court ought not to approach an application such as this on the basis that the directors are going to act improperly in defending the Petition, particularly so where there are three directors one of whom is an independent director. In the face of allegations which are unproven, there is no basis to say that the directors are improper in defending this petition, or that they might in future improperly defend the Petition.

105. Counsel also submitted that as a practical matter on costs, the directors have contractual rights which are fully enforceable which provide not only for indemnification but advancement. The indemnities are not optional. The end result said Counsel would mean that the Company would have to initially meet the costs in any event. Additionally, even if they are not named as respondents to the Petition there would still be the option to seek a third party costs order depending on the findings of the Court.

106. As to the Petitioner's submissions about being bound by findings of fact, Counsel for the Company argued that the argument was unsustainable given that the Petitioner has made a choice between a derivative action and a winding up petition. The Petitioner could have made the choice to bring an action against the directors.

DISCUSSION AND CONCLUSION

107. The cases cited suggest that the correct approach is to look at the substance of the allegations, and to consider the real nature of the dispute. The Court should consider whether this is in reality a dispute between shareholders. I asked Counsel for the Petitioner directly whether his position could be sustained if the two directors did not have 6.4% shareholding. His response was that the Court need not consider such a scenario as there was indeed a shareholding however minor.

108. The minority of the shareholding is possibly not a complete answer. There could be cases where a minority shareholder has a dispute with other shareholders. Buy out arrangements which are alleged to be unfair or alleged oppressive conduct would be examples. The essential question is what the dispute in the instant case is about.

109. While Counsel for the Company argued that as the alleged conduct was not qua shareholder it would be jurisdictionally invalid for there to be joinder, accepting this argument would require merging the two aspects of jurisdiction and discretion. In short deciding on the nature of the dispute and reaching a jurisdictional conclusion therefrom.

110. The submission of the Petitioner that Mr. Drankiewicz and Ms. Macias are shareholders which provides a jurisdictional gateway for the application of CWR O.3 r.12 as to characterisation is accepted.

111. On the second issue of discretion both on joinder and characterisation, if the correct approach is that the Court should look beyond the surface, to the reality, then I have to say that it is difficult to accept the submissions of the Petitioner over that of the Company.

112. My own view is that the factual position as described by Counsel of the Company is correct. The Amended Petition itself does not mention the two individuals as shareholders. Indeed it does not mention any activity by them as shareholders. The affidavit filed in support of this summons for directions does not refer to them as shareholders. The first mention of their shareholding is in an affidavit filed by the Company. There is nothing in the Amended Petition or affidavits provided by the Petitioner which suggests that these two were "controlling shareholders". Their role as shareholders and anything done in that capacity is not detailed or referenced except in the submissions of Counsel on behalf of the Petitioner. This perhaps indicates the absence of the shareholding as a feature in the allegations.

113. In summary, having considered the Amended Petition and other materials to which both Counsel have drawn my attention, there is nothing to suggest that this is in fact a dispute between shareholders. It appears to be very much a dispute with the Company and with its directors.

114. Thus I accept the submissions of the Company that the shareholdings which are not mentioned in the Amended Petition are incidental to the alleged activity and are neither the essence of nor central to and do not feature in it. Counsel submitted and I accept that there is no allegation against the two individuals as to activities qua shareholders as distinct from qua directors.

115. I think that there is a material difference between an allegation of mismanagement by directors and issues between shareholders.

116. As to the characterisation of the matter, applying the test, does the Company have a real interest in the matter whether an economic interest or otherwise, the answer is very likely it does. The Company is described as a successful fund. The structure is set out by Mr. Guilfoyle. The Petitioner is only one of 27 investors. It has invested in only one of some 38 investment

offerings. There is no suggestion that the shareholders other than those who joined with the Petitioner for the requisition for the EGM take any position one way or the other.

117. I have set out above in some detail the nature of the dispute as it appears from the Amended Petition and the affidavits to which my attention was drawn. On the one hand the Petition is based on the alleged mismanagement of the directors. On the other hand from the affidavits filed on behalf of the Company, the likely broad scope of the matter appears to be that the Company raises a possible defensive position which asserts that there was perceived to be an intention on the part of the Petitioner to "potentially hijack the fund" and that the Company needed to act "in the best interest of the Company and the investors as a whole."

118. While the general principle as to the non-use of a company's funds in defence of allegations of misbehavior is borne firmly in mind, I do accept the submissions of the Company on this point. I accept that the Company has a separate and independent position and an interest of its own which requires protection. It is thus necessary and or expedient for it to act in the interests of the Company as a whole.

119. The fact of the shareholding may be seen to provide jurisdictional basis. However given the real nature of the allegations herein and considering the two matters separately, I would decline to exercise my jurisdiction to order joinder of the two directors in these circumstances or to order that the Petition be treated as one between shareholders. It should be treated as a proceeding against the Company and the Company should be properly able to participate in it.

120. At the time of the hearing Counsel made submissions *de bene esse* as to possible further directions. Now that a conclusion has been reached as to the substantive issues joined, Counsel may have a further opportunity to make any additional submissions should they so wish.

Dated this the 4th day of May 2022

Honourable Justice Cheryll Richards Q.C.
Judge of the Grand Court