

Joint venture agreements and the conflicting roles of directors and shareholders

Shareholders' agreements commonly impose obligations on the parties which can, in practice, restrict the ability of company directors to manage the affairs of the company in an unfettered manner. This can cause problems, particularly where the shareholders and directors are the same people. The recent High Court decision in *Jackson v Dear and another* has considered these issues in the context of the removal of a director from office, which he alleged was contrary to protections in a shareholders' agreement.

The Facts

In around 2002 Mr Jackson, Mr Dear and Mr Griffith co-founded a business to own, develop and manage various investment funds. The dispute related to Mr Jackson's removal as a director of Tetragon Financial Group Limited (the "Company"), a company in which Polygon Credit Holdings II Limited (the "Shareholder") held all the voting shares. Mr Dear and Mr Griffith were able to control the exercise of the voting rights attaching to those shares.

A shareholders' agreement dated 29 September 2008 (the "Agreement"), signed by the various individuals listed above, stated that unless one of a number of listed "Termination Events" occurred, the Shareholder and the individuals would ensure that Mr Jackson was nominated and re-appointed as a director of the Company at each AGM.

The Company's articles separately conferred a power on the directors to remove a director by notice from all other directors. Using this provision, Mr Jackson was removed from office in January 2011.

Mr Dear and Mr Griffith argued this was not a breach of the Agreement as a "Termination Event" had occurred, as Mr Jackson had breached his fiduciary duties as a director of the Company. Mr Jackson denied this and sought to rely on the Agreement to be re-appointed at the November 2011 AGM. His request was rejected.

The High Court was asked to consider as a preliminary issue whether, assuming the alleged "Termination Event" had *not* occurred, Mr Jackson's removal as a director could stand, notwithstanding the provisions of the Agreement.

Consequences

The High Court found in Mr Jackson's favour on this point. It ruled that the provisions of the Agreement meant that the defendants could not take any steps to remove Mr Jackson as a director unless and until a "Termination Event" occurred.

The court considered the general rule that where a party enters into a contract it must not do anything of its own volition to render its further performance impossible or futile, even if not specifically prohibited from doing so under the contract.

In this context, given that it had been agreed by Mr Dear, Mr Griffith and the Shareholder that – until a Termination Event occurred - the Shareholder’s voting power would be used to procure Mr Jackson’s continued re-appointment as a director at each AGM, it was not necessary for the contract to specifically list every action which Mr Dear and Mr Griffith were then prohibited from taking to frustrate that obligation.

The court also rejected an argument that in failing to use their power under the articles, Mr Dear and Mr Griffith would have been in breach of their fiduciary duties given they genuinely believed it was in the best interests of the company to remove Mr Jackson as a director. In theory it would be difficult to hold directors to an agreement which required them to breach their fiduciary duties. However, the court commented that, particularly given the Agreement contained a “further assurance” clause, Mr Dear and Mr Griffith needed to take other legitimate measures to absolve themselves from, or disapply, their fiduciary duties in this instance and give effect to the provisions securing Mr Jackson’s continued appointment. The court suggested various ways in which this could be done, including procuring that the Shareholder passed a ratification resolution.

The Lesson

This case touches on issues which are common in joint ventures, namely the tensions which exist where parties to the arrangements have a dual role in acting as directors (directly or through their appointees) and shareholders of a joint venture company.

A shareholder generally owes no obligations to others (including the company in which they own shares) in relation to the exercise of rights attaching to their shares, save for those they agree to assume by contract. Conversely, a director will be subject to various duties under the Companies Act which restrict that individual’s ability to act as a director in their absolute discretion. Under English law they will be expected to comply with those duties, regardless of the effect compliance will have on them in their capacity as a shareholder.

Concerns in this area can arise in many different contexts. One common example is the type of quasi-partnership arrangement which existed in this case. Another is private equity or similar investment structures where an investor shareholder takes a seat on the board, or appoints a representative to do so.

English law has still not come up with an entirely satisfactory solution to resolve these difficulties generally. However, this case suggests that the courts will, where possible and within limits, look to uphold arrangements between the parties which have been specifically negotiated and agreed, reaffirming the need to have a well drafted shareholders’ agreement in place.

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