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An Offence to Courtesy – Asserting Minority Shareholder Interests

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Although it might be discourteous, putting your own interests first as a minority shareholder won't always put you in breach of your obligations to your fellow shareholders. The Court of Appeal recently considered the extent of minority shareholder obligations in the case of *Dold v Murphy* [2020] NZCA 313.

Mr Dold, Mr Jacobs and Mr Murphy were parties to a shareholder's agreement. Dold and Jacobs were majority shareholders and Murphy held only 6.2% shares in the company.

A third party offered to buy the company for $112million AUD. When Dold and Jacobs asked Murphy to sign, he demanded an additional share of $4million of the sale proceeds. If he didn't sign, the sale would not have gone through, so Dold and Jacobs felt they had no choice but to agree.

Mr Dold wasn't very happy about being put over a barrel like this and sued Mr Murphy to recover his $2million share of the extra payment. He claimed that Mr Murphy's demand was unlawful as it:

- was a breach of the shareholder's agreement;
- was a breach of a fiduciary duty owed to Mr Dold as a shareholder; and
- amounted to economic duress.

The High Court held that Mr Murphy could keep the money. The Court of Appeal agreed with the High Court.

No breach of shareholder's agreement

The Court noted the absence of a "drag-along" provision in the shareholder's agreement, which would normally compel a minority shareholder to sell at a price acceptable to the majority.

It also found no other breach of the shareholder's agreement had occurred. The Court made the comment that Mr Murphy's behaviour "offended courtesy, rather than contract."

No breach of fiduciary duties

The Court of Appeal also refused to recognise a breach of fiduciary duty.

There are accepted categories of fiduciary relationships which have been recognised at law, including solicitor and client; trustee and beneficiary; partners in partnerships, and agent and principal. The Court had to consider whether a fiduciary relationship existed in this case.

If a relationship is recognised as an 'inherently' fiduciary relationship, the Court must consider whether the alleged fiduciary:

- has been given some powers (usually in relation to property);
- has assumed some representative or protective responsibility over the alleged beneficiary (or their property); and
- has impliedly or expressly agreed to put their own interests second to that of the beneficiary.

The shareholder's agreement did contain an obligation on all shareholders to maximise the returns for the benefit of shareholders. However, there was an express provision stating that the relationship of shareholders was not one of partnership. There was also a clause requiring unanimous agreement when dealing with certain company affairs (including the sale of shares).

There was nothing special arising out of this shareholder relationship that meant Mr Murphy had taken on the role of fiduciary to Mr Dold. The Court reaffirmed that a shareholder-shareholder relationship is not inherently fiduciary. It held that it would have been exceptional to impose fiduciary duties on a minority shareholder, without Mr Murphy having done something further to assume fiduciary responsibilities beyond the obligations described in the shareholder's agreement.

No economic duress

The Court held that (although possibly a bit ungenerous) it was lawful for Mr Murphy to threaten to refuse to enter a contract for the sale of shares. Economic duress usually applies when an unlawful act is committed, and the Court found that a threat not to enter a contract was unlikely to be an unlawful or illegitimate act. In the absence of an overriding obligation to sign, withholding his signature at the eleventh hour unless the proceeds were redistributed was not unlawful. Mr Murphy was entitled to act in his own self-interest.

Pointers:

- Drag along rights are protections worth including in your shareholder's agreements where there are minority shareholders that could hold up or prevent a sale.
- The Courts are reluctant to redraft a contractual relationship that parties have freely entered, so getting your shareholder's agreement correct from the outset is important.
- There is a difference between commercial pressure and illegitimate pressure and this case suggests that the distinction may be nuanced when disputing shareholders are threatening action.

If this case has you wondering about your obligations as a shareholder, or the robustness of your shareholder's agreement, feel free to get in touch with us.

Further Advice

If you'd like further advice on your obligations as a shareholder, or the robustness of your shareholder's agreement, please contact Jenna Riddle at jenna.riddle@gallawaycookallan.co.nz or 027 742 1032 or Jay Pierce at jay.pierce@gallawaycookallan.co.nz.

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