

## Staray Capital Limited - Privy Council

The Privy Council has upheld changes to a BVI company's Articles of Association, despite these changes being motivated by a desire to exclude a minority shareholder. In doing so, the Privy Council has provided a welcome confirmation of the principles applicable to this contentious area and the case provides an instructive worked example of how to apply these principles when amendments to a company's Articles of Association are challenged.

### The Facts

Mr Chen (80%) and Mr Cha (20%) agreed to participate together in a project, with Staray Capital Limited (**the Company**) being the project vehicle. The relationship swiftly broke down and Mr Chen accused Mr Cha of misrepresenting his legal credentials at the outset, including his job title and his qualification to practise in China and New York.

Mr Chen caused Mr Cha to be removed as a director and passed a shareholders' resolution amending the Company's Articles of Association. The amendments gave the Company an option, upon notice, to compulsorily redeem a shareholder who, inter alia, had made '*material misrepresentations (whether fraudulent or negligent) in the course of acquiring its shares.*'

Pursuant to this newly granted power, the Company purported compulsorily to redeem the 20% shares held by Mr Cha on the basis of the alleged misrepresentations concerning his legal credentials. Mr Cha objected and commenced proceedings under section 184I of the *BVI Business Companies Act, 2004* (colloquially known as the unfair prejudice provision) seeking relief including the removal of the amendments to the Articles of Association and the cessation of attempts to compulsorily redeem his shares.

### The Decision

Mr Cha was successful both at first instance and on appeal in the Court of Appeal. When the matter reached the Privy Council, the Board considered in turn (i) whether the amendments to the Articles of Association should be upheld and (ii) if they should, whether they were properly relied upon in the circumstances.

#### (i) The Amendments

The Privy Council applied the summary of principles in *Re Charterhouse Capital Ltd* [2015] EWCA Civ 536. Applying these, the burden falls on the person impugning the validity of the amendment of the Articles of

Association to satisfy the court that there are grounds for doing so. This is not an easy task, having in mind in particular that:

- A power to amend will be validly exercised if it is exercised in good faith in the interests of the company.
- It is for the shareholders, not the court, to say whether an amendment is for the benefit of a company, but it will not be for the benefit of the company if no reasonable person would consider it to be such.
- The mere fact that the amendment adversely affects, and even if it is intended adversely to affect, one or more minority shareholders and benefit others does not, of itself, invalidate the amendment if the amendment is made in good faith in the interests of the company.

At first instance, the Judge, having found that although the amendment was directed at a particular shareholder this was insufficient on its own to invalidate it, took the view that the issue turned on the question of whether the resolution could be attacked as not being bona fide in the interests of the Company:

*'...it seems to me that it is not possible for me to say that a company in general meeting cannot reasonably take the view that shareholders who have acquired their holdings as a result of misstatements, whether fraudulent or negligent, or who have committed acts which may result in the company incurring or suffering disadvantage or negative publicity, should have their shares redeemed at a valuation. By itself the amendment is not so oppressive or extravagant as to cast doubts upon the bona fides of Mr Chen in professing the view that it was in the best interests of Staray that Mr Cha should cease to be associated with it.'*

The Judge accordingly rejected the challenges to the amendments. The Court of Appeal upheld the Judge's reasoning, finding that he had correctly applied the legal principles and that there was no justification for interfering with his conclusion.

The Privy Council agreed, emphasising that the careful evaluation of the Judge, who had the advantage of assessing the evidence, should be respected. The Board did however go further and expressly endorsed the Judge's reasoning, commenting that it was compelling.

## **(ii) Purported exercise of the amended Articles**

Mr Chen argued that there had been material misrepresentations falling with the meaning of the amended wording of the Articles of Association, entitling the Company to redeem Mr Cha's shares compulsorily. This was not a surprising argument as it is to be inferred that the amendments were drafted at a time when Mr Cha's alleged misrepresentations were known and the amendments were designed to produce this outcome.

However, Mr Chen was unable to persuade either the Judge at first instance or the Court of Appeal that the preconditions set out in the amendments had in fact been satisfied so as to entitle the Company to redeem compulsorily Mr Cha's shares.

On further appeal to the Privy Council, the Board doubted whether a misrepresentation had indeed been made, inclining towards the Judge's view at first instance (the Court of Appeal having found an immaterial misrepresentation with the benefit of further evidence adduced). However, the Board did not consider it

necessary to determine the point as it formed the view that materiality was the critical issue.

The Board emphasised that materiality is not to be judged by reference to *'abstract textbook definitions'*, but having regard to the particular context of the clause and the circumstances of the Company. Properly analysed, the Board observed that the clause in question was for the benefit of the Company and therefore the question of materiality fell to be determined less by reference to Mr Chen's subjective reactions to any misrepresentation, but having regard to the practical relevance of any misrepresentation on Mr Cha's expected role with the Company.

On that analysis, the Board was satisfied that the alleged misrepresentations were of no practical significance to the Company, hence were immaterial. This meant that the Company's purported reliance on the amended clause was flawed.

## Outcome

The appeal was therefore dismissed and, although successful in upholding the amendments to the Articles of Association, it was a pyrrhic victory for Mr Chen as the prerequisites for the exercise of the powers under those amendments were found not to have been fulfilled.

To discuss the significance of these decisions further or any queries arising, please do not hesitate to contact the authors detailed below. The foregoing is provided by way of general commentary and should not be relied upon in any specific situation.



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