High Court Holds Shareholders Suffered Unfair Prejudice after Exclusion from Company's Sole Project

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In the case of *Dodson and others v Shield and others* [2022] EWHC 1751 (Ch), the High Court recently concluded that shareholders of a company had suffered unfair prejudice when they were excluded from a project that was the reason for the company's existence.

Facts. Two shareholders, Mr Kevin Dodson and Mr Murry Dodson (the "Petitioners"), brought a petition for unfair prejudice under section 994(1) of the Companies Act 2006 (the "CA 2006"). The business of the company, International Automotive Engineering Projects Ltd ("IAEP"), was defined in a shareholders' agreement as "*the design, sale and implementation of turnkey automotive engineering projects on an international basis*" (the "Shareholder Agreement"). The initial project (and the only project which was ever pursued) concerned the six manufacturing lines used by BMW to manufacture its NG4 engine used in the BMW 3 series, 1 series and Mini premises. The "turnkey" element of the project was that IAEP would ensure that the buyer could commence the manufacture of motor car engines immediately after installation was complete.

The Petitioners' case was that in the latter part of 2013, they were excluded from the project. In particular, the Petitioners alleged that the Respondents had caused unfair prejudice by:

- diverting the project to a third party, namely CGI Automotive Consulting Ltd ("CGI") in which they had no participation;
- procuring that the technical library acquired by IAEP for the purposes of the project was transferred from IAEP to CGI and/or other companies without payment to IAEP; and
- failing to and/or refusing to enter into good faith negotiations to sell the product to IAEP or a third-party buyer, in breach of their duty to do so, as set out in the option agreement.

Decision. The Court held that (i) the diversion of the project to CGI and (ii) the transfer of the technical library to CGI and/or other companies at no cost did cause unfair

prejudice to the Petitioners and also constituted breaches of fiduciary duties by the first to the seventh respondents (i.e. excluding IAEP, the eighth respondent). However, no unfair prejudice was caused by (iii) the failure to negotiate pursuant to the option agreement or the Shareholder Agreement.

A key question in the case in respect of the findings on unfair prejudice was whether IAEP was a quasi-partnership. The Court held that the company was indeed a quasi-partnership even if clause 21 of the Shareholder Agreement provided that "*the parties have expressly agreed that there is no partnership.*" The Court explained that a company cannot, as a matter of law, be a partnership of the shareholders. However, that does not prevent the company from being a "quasi-partnership", as per *Ebrahimi v Westbourne Galleries Ltd* [1973] AC 360. The Court clarified that "*the expression quasi-partnership is more of a metaphor: the company is not a partnership but the relations between those interested in the company are more akin to those of partners.*" The Court identified the following key aspects on the facts which supported the conclusion that the company was a quasi-partnership, namely:

- all the shareholders were entitled to be directors;
- there was no means of forceable buy-out, so if a "*member [was] removed from management, he [could not] take out his stake and go elsewhere*";
- all the shareholders owed duties of good faith to each other under the Shareholder Agreement, so there was a relationship of "mutual confidence";
- the business of the company (as set out in the Shareholder Agreement) was the acquisition of six NG4 lines from BMW and the selling of a turnkey facility to a buyer; and
- none of the shareholders could compete with IAEP on turnkey projects; each shareholder was entitled to "*participate in the conduct of the business*". Moreover, the shareholders were obliged to use reasonable endeavours to promote and develop the project, pursuant to the Shareholder Agreement.

A finding that IAEP was a quasi-partnership was itself not enough to make out a claim under s. 994 of the CA 2006, though. The Petitioners therefore relied on the Judge's finding, as above, that the diversion of the project in breach of the non-competition and business promotion provisions of the Shareholders' Agreement and the transfer of the technical history away from the company for no consideration amounted to unfairly prejudicial conduct against the Petitioner. These also constituted a breach of the directors' fiduciary duty given the conflict of interest which had not been waived by non-conflicted directors.

Delay in Bringing the Petition. The Respondents also argued that the Petitioners' claims regarding the breach of the duty to negotiate under the option agreement, as well as the breaches of fiduciary duties were time-barred, given the delay in bringing the same. In respect of the former, the Court considered that this point was immaterial on the facts given that any breach of the duty to negotiate would have attracted nominal damages at most, in light of the Court's finding of fact that in the second half of 2013, there was no prospect of negotiations being productive. As to the latter, the Court explained that the breaches of fiduciary duties were ongoing. Therefore, they were not statute-barred. Moreover, there was nothing which would amount to acquiescence of the breaches on the Petitioners' part, on the facts.

Comment. The case is a useful reminder that the assessment of whether unfair prejudice has been caused to petitioners is a fact-sensitive one. In circumstances where, the company is a quasi-partnership, the petitioners have been excluded from a project that is the very reason for the existence of the company and management is found to be in breach of its fiduciary duties, it is very likely that unfair prejudice will be found on the facts. The case also provides welcome clarification that a company can be a quasi-partnership even if the agreements at issue expressly provide that there is no "partnership" and even if, as a matter of law, a company cannot be a partnership of the shareholders. It is clear that "quasi-partnership" is "more of a metaphor" to refer to circumstances where the shareholders have, inter alia, a personal relationship of mutual confidence.

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Please do not hesitate to contact us with any questions.

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