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Majority Rule and Minority Protection: A Reflective Analysis of the Nigerian Corporate Practice.

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Abstract

The Company Act 1960 merely incorporated the Common Law position with its shortcomings and that unfortunately form the foundation of Corporate Practices in Nigeria. The Companies and Allied Matters Act 1990[1] introduced useful changes aimed at filling the lacunae inherent in the 1960 Act; which includes but not limited to creating a new regime of corporate governance. It is unfortunate that our corporate practices is still inclined to the Common Law which the repealed Companies Act, 1960 encapsulated; thus, the new regime of Corporate Practice; especially with respect to Corporate Governance brought about by the new Act is hardly taken advantage of shareholders as members of the company have the need to be protected and as amongst the shareholders themselves there arises the need to protect the minority shareholders from the abuses of power by the majority. In view of this fact, the law has established various fora for the resolution of corporate disputes in order to ensure the protection of both the members and investors in the company. These fora are:Shareholders in general meeting, Board of directors meeting,The court and Corporate affairs commission investigations under Section 314 of the Act. The main concern of this work is to evaluate the resolution of companies' disputes through judicial intervention, the common law approach and the Companies and Allied Matters Act[2]. This work will posit that the Companies and Allied Matters Act has introduced a new order that has to a large extent whittled down the rule in ***Foss v. Habottle***[3] *and as such the rule in* ***Foss v. Harbottle*** *can no longer be relied upon as fully representing the Nigerian position.*

Key Word: Majority Rule, Minority Protection, Reflective Analysis

Introduction:

The Concept of Legal Personality and its applicability in Nigeria**:** The term *"Legal Personality"* is a coinage by jurists to differentiate between natural artificial persons. This expression in some jurisdictions includes organizations, funds or even idols. For instance in the Indian case of **Prematha Nath Mullick v. Pradyumma Kuman Mullick**[4], the privy

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[1] Now Cap C20 Laws of the Federation of Nigeria, 2004
[2] Ibid
[3] (1843) 2 have 461, 67 ER. 189
[4] (1925) L.R. 52 Ind. App. 245

Council recognized Hindu idols as legal persons. Moving away from the bracket theory, which was based on the idea that only human beings can truly be subjects of rights and duties, the law recognized association of persons and corporations as also capable of enjoying rights, although the creation of corporations represent only a technical device of having non natural persons as entities capable of enjoying legal rights. This bracket theory as propounded by the German Jurist R. Ihering sees the individual forming the corporation as those who can enjoy rights as against the corporation itself; which is a mere bracket containing the individuals. But the present position of the law is opposed to the bracket theory rather, the rights vested in a corporate body is for the benefit of the corporate which acts through its members. This they seem to have fitted into savigny fiction theory. By this theory, legal personality is attributed to a corporation by way of fiction; thus speaking as if something were the case whereas everybody knows fully well that it is not. The sum total of the resolution of the debate on this subject is that, the recognition of artificial legal personalities is based on the need to protect and facilitate common action by individual human beings. This approach has been encapsulated in Section 37 of the Act, to the effect that once a company is incorporated it becomes a legal entity different from its members[5]. This is in itself a recapitulation of the common law position as was pronounced in the case of **Salomon v. Salomon[6].**

Though a company as an artificial person does not have feelings like natural person and does not possess the intellect and capacity of a natural person to manage its affairs; it does so through its human organs who manage the affairs of the company for the benefit of all the persons with interest in the company. It then goes without saying, that, there is the possibility of mismanagement, high handedness and likelihood of frittering away the company's resources by those appointed to manage the affairs of the company. The extent to which the law creates and regulates corporate management will be viewed both from the common law position as represented by the 1960 Act and the Companies and Allied Matters Act, 2004.

[5] Union Bank (Nigeria) Ltd v. Penny Mart Ltd (1992) 5NWLR (Pt. 240) 228 at 237
[6] (1897) AC 22

Common Law Position

The common law position falls short of providing adequate protection to the minority shareholders who are faced with serious and substantial problems in respect of instituting court actions against the directors for breaches of their duties. It goes without saying that if directors are not checked at all in the exercise of their powers, they would exercise same to the detriment of both investors and creditors. This they could do by failing in their duties through abuse of powers, which may result in frittering away the company's assets to the detriment of shareholders/creditors and investors.

Under the common law there is an inclination towards the majority rule in the enforcement of the company's rights, as the powers of the majority rule extends to every area of the company, such as, power to abrogate or approve the directors acts, power to alter the constitution of the company and power to appoint and dismiss directors. Even though as part of the rule, the majority cannot derogate from the powers of the directors for the day to day management of the company. The point remains that in remedying any wrong done to the company, the proper Plaintiff is the company, and it is for the majority to decide whether the company should sue. This is the so-called rule in **Foss v. Harbottle**[7] which operates to deny locus standi to the individual shareholders to bring an action for wrong against the company. The unjustness of this rule is better imagined than felt, for instance in the case of **Tika-Tores Press Ltd. v. Abina**[8]**,** the Supreme Court held that however wrong the director's action might have been it was open to the shareholders in general meeting to ratify their wrongdoing. Assuming such wrongdoing adversely affects the interest of the creditors and investors no remedy will be available to them once such is ratified. One therefore sees the boomerang effects of the rule, which ought to have been stressed to afford protection to all the company's creditors and investors.

The shareholders would only seek redress if the wrong is such done by the company against the shareholders. This marks a distinction between "Corporate Action" to remedy wrong done to the company and "personal action" to remedy wrong done by the company against the shareholders. It would be parochial to hold the view that the creditors interest are

[7] Supra
[8] (1973) 4 SC 63

only threatened when a wrong is done against them by the company as they stand to suffer untold hardship and prejudice where fraud is being committed by the alter ego. For instance, in a situation where the directors of a company fraudulently sell its property, they would be incapacitated to take legal action against the directors despite their membership of the company[9]. This is moreso when considered from the view point that the creditors look unto the company's assets for the payment of the debts owed them by the company. The court simply regarded this as the management of the company's internal affairs for which the court should not interfere[10]. Thus, the court found the rationale for upholding this rule on the fact that the company being a corporate personality ought to be its own plaintiff. Secondly, the court saw the need to extend the immunity against judicial interference in the affairs of partnership to corporate bodies.

The Nigerian Companies Act of 1968 copiously encapsulated these rules without regard to the inherent hardships. Although certain exceptions to the rule existed under the said Act, the question is to what extent did the exceptions ensure the protection of the minority members of a company? This will be considered by evaluating seriatim the exceptions.

(a) **Illegal or Ultra Acts**:

Shareholders can sue both under the common law and the 1968 Nigerian Companies Act to prevent illegal or ultra vires acts, since the company is incapable of ratifying such acts, thus in the case of **Parke v. Daily News**[11] it was held that if the act of the company is ultra vires or illegal, any member has a right to apply to the court to set it aside. It is commendable to have this as an exception as the absence of it would negate the whole essence of corporate practice and existence.

(b) **Invasion of Personal Rights of Members**:

This is yet another exception that aims at ensuring the protection of the minority. This is a situation where the wrong is done to the individual member of a company and not the company itself. This may occur where the individual is denied the right to vote

[9] See Foss. V. Harbottle Supra
[10] See Morley v. Alston (1847) 1 Ph. 790 and MacDougall v. Gardiner (1875) 1 Ch. D. 13
[11] (1962) ALL ER 929

which is a proprietary right. This issue arose in the case of **Pender v. Lushington**[12] and the court granted injunction in favour of the plaintiff whose right to vote was disallowed. Happily both the first exception and this have been re-enacted in the Companies and Allied Matters Act 2004, in Sections 300(a) and 300(c) respectively.

(c) **Allegation of Fraud by the Minority**

Like the other exceptions, this is also salutary and has been codified into our present Companies and Allied Matters Act in section 300(d). In the case of **Atwood v. Merryweather**[13], an action bought against the majority shareholders in a company who sold their mine to the company in a transaction that was tainted with fraud, was upheld. The court held that not minding the rule in **Foss v. Harbottle**, the transaction will be set aside; otherwise the fraud cannot be prevented. However it must be shown that the wrongdoers control the company[14].

(d) **Where the Company's Property is Expropraited**

This is akin to perpetration of fraud on the minority and where this happens the rule in **Foss v. Harbottle**[15] will be ousted, it does not matter that the expropriation was in good faith.[16] This exception ensures that the company's assets are not disposed or frittered away as such would deny the creditor of the main subject to which he looks for payment of his debts.

(e) **Interest of Justice**: Still Under the Common Law: this constitutes an exception. In the case of **Russel v. Wakefield Water Works Co**.[17] it was stated that:

> Any other case in which the aim of justice require is within the exception…the rule in **Foss v. Harbottle** is a general one but it does not apply to a case where the interest of justice require it to be dispensed with

[12] (1887) 6 Cu. D 70, See also Wood v. Odessa Waterworks Co. (1889) 42 Ch. D 636
[13] (1867) LR EQ. 464n 37 LJ Ch. 35
[14] See Manier v. Hoopers Telegraph Works Ltd (1887) 9 Ch. APP 350. See also Cook v. Deeks (1916) AC 354
[15] Supra
[16] See Alexander v. Automobile Telephone Co. (1900) 2 Ch. 56
[17] (1875) CR 20 LQ. 474 at 482

This appears to be the most important exception as it covers the other exceptions. The whole of the exceptions can be said to be based on interest of justice. It is an available leeway to circumvent the harshness of the rule in **Foss v. Harbottle**[18] and can even be exploited in such a way as to displace the entire rule, depending of course, on the special circumstance each case presents.

The Majority Rule and Minority Protection under the Companies and Allied Matters Act[19]

The Companies and Allied Matters Act at sections 303 to 313 has not only ensured the enforcement of corporate right within the exceptions to the rule in **Foss v. Harbottle**[20] but has also provided a means of remedying wrong done to the company which fall outside the scope of the traditional exceptions and therefore a helpful extension of the exception to the rule in **Foss v. Harbottle**[21]

Section 303 (1) provides thus:

> *Subject to the provisions of subsection (2) of this section an applicant may apply to the court for leave to bring an action in the name or on behalf of a company or to intervene in an action to which the company is a party for the purpose of prosecuting, defending or discontinuing the action on behalf of the company*

The Act further at section 309 defines an applicant as

(a) A registered holder of a beneficial owner and a former registered holder of a beneficial owner of a security of a company.

(b) A director or an officer or a former director or officer of a company.

(c) The commission or

(d) Any other person who in the discretion of the court is a proper person to make an application under Section 303 of this Act.

[18] Supra
[19] Cap 59 Laws of the Federation of Nigeria, 1990 now revised as Cap C20 Laws of the Federation of Nigeria, 2004
[20] Supra
[21] Supra

The qualification to the bringing of this action is clearly stated in section 303(2) to the effect that no action may be brought and no intervention may be made under subsection (1) of Section 303 unless the court is satisfied that:-

(a) The wrongdoers are the directors who are in control and will not take necessary action.

(b) The applicant has given reasonable notice to the directors of the company of his intention to apply to the court under the subsection.

(c) The applicant is acting in good faith.

(d) It appears to be in the best interest of the company that the action be brought, prosecuted, defended, or discontinued.

Thus, in the contemporary Nigerian Company Law, the operation of the exceptions to the rule in the **Foss v. Harbottle**[22] is purely based on the wide discretionary powers of the court and if judiciously utilized would ensure the protection of creditors and investors.

The Act is unambiguous in making the derivative action a "Corporate action"[23] even though it has not abolished the rule in **Foss v. Harbottle**, it has entrenched far reaching exceptions to it as circumvention to the problem of locus standi imposed by the rule; thus removing one of the inhibitions to minority protection.

As a milestone the Act has successfully and clearly distinguished between personal actions[24], the shareholders representative actions[25] and the corporate derivative actions[26]. The beauty of this distinction is clearly put by professor Gower[27], when he stated that the use of the representative procedure to refer to both derivative actions and shareholders personal actions has given rise to a great deal of confusion, which stems from the failure of litigants and the courts to draw a conceptual distinction between the two distinct actions. Another important way the Act has handled the rule in **Foss v. Harbottle**[28] to the advantage of the minority in a company is by providing leeways for nipping in the bud, possible wrongs

[22] Supra
[23] S. 303 (1) CAMA Ibid
[24] S. 301 (1) Ibid
[25] S. 301 (2) Ibid
[26] S. 301 (1) Ibid
[27] Op cit P. 647
[28] Supra

that could give rise to actions against the wrongdoers. This it has done by empowering the applicant to apply to court even before the wrong is committed for the intervention of the court to prevent such perceived wrong. The whole of section 300(a) to (f) is a codification of the exceptions to the rule in **Foss v. Harbottle**. Quite unlike the pre-1990 position, one does not have to wait for the wrong to be committed before seeking recourse in the law court. It thus appears that such an application can be made even upon reasonable suspicion that an injury is about to be caused to the company.

Another innovation of the Act is as enshrined in section 306 to the effect that the derivative action may not be stayed, discontinued, dismissed or settled without the court's approval. In the same vein, the court will not stay or dismiss the application simply because the Act had been rectified by the shareholders[29]. Again, the fact that the Act has shifted the burden of paying the interim costs of the application to the company is encouraging enough to ginger the minority or one of them to take action for his own protection.

There is however the need for judicial activism in the interpretation of the provisions of Companies and Allied Matters Act, in view of the decision reached in such cases as **Transatlantic Shipping Agency Ltd. v. Dantrans Nig. Ltd[30], and Daily Times (Nig.) Plc v. Akindiji[31].**

In the former case, the court held that:

> There was evidence… which established that it was the Managing Director of the company that authorized the institution of the action before the lower court. In view of my above holding that the managing director had got no power to authorize the institution of the legal proceedings in the company's name without the requisite authority from the Board of Directors of Shareholders. The position of the law as spelt out in **Vaswani Trading Co. v.**

[29] S. 305CAMA Ibid
[30] (1996) 10 NWLR (PT. 478) P. 360
[31] (1998) 13 NWLR (PT. 580) P. 22

> **Savalkh** is that no one can put up a castle in the air, it will certainly collapse as it has no foundation[32].

It is submitted with due respect that this is a wrong exposition of the law. Vaswani's case which was decided in 1973 was decided under the 1968 Act which differed greatly from the 1990 Act; the former having drawn life from the common law position and an offshoot of the rule in **Foss v. Harbottle**, requiring the authority of the Board of Directors for the institution of a legal action which position has now been modified by the extant provisions of the Companies and Allied Matters Act[33] already discussed.

In the case of **Daily Times (Nig.) Plc. v. Akindiji**[34] the court held that:

> *The rule in **Foss v. Harbottle**... which is now codified in section 299 of the Companies and Allied Matters Act provides that where the wrong complained of is done to a company, it is only the company itself and not an individual or minority shareholder that can take action to redress or ratify the wrong or irregular conduct.*

It is a submitted, with due respect that this ratio runs contrary to the clear provisions of the Companies and Allied Matters Act discussed above and infact anti-protective of the rights of the minority. The Act has obviously gone a long way in removing the obstacles created by the rule in **Foss v. Harbottle** in respect of actions by the individual or minority against the erring majority.

Conclusion

The innovations of the Companies and Allied Matters Act in the area of minority protection is a welcome development. It has simplified the procedure for taking action against the majority in a company and has indeed converted the minority into corporate police by fully equipping them to stand up and defend the company from possible collapse that may result from the mismanagement of the affairs of the company by the majority.

[32] Supra at P. 360
[33] Ibid
[34] Supra at P. 27