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PRESS SUMMARY

Eclairs Group Ltd (Appellant) v JKX Oil & Gas plc (Respondent); Glengary Overseas Ltd (Appellant) v JKX Oil & Gas plc (Respondent) [2015] UKSC 71
On appeal from [2014] EWCA Civ 640

JUSTICES: Lord Neuberger (President), Lord Mance, Lord Clarke, Lord Sumption and Lord Hodge

BACKGROUND TO THE APPEALS

Under sections 793-797 of the Companies Act 2006 (“the Act”), a company can issue a statutory disclosure notice calling for information about persons interested in its shares. The court can restrict the exercise of rights attaching to shares in the event of non-compliance. JKX Oil & Gas plc, like many companies, has a provision in its company articles (article 42) empowering the board to impose such restrictions where a statutory disclosure notice has not been complied with. Article 42 provides that the board is entitled to treat a response to a disclosure notice as non-compliant where it knows or has reasonable cause to believe that the information provided is false or materially incorrect.

In 2013, the directors of JKX perceived that it had become the target of a so-called “corporate raid” by two minority shareholders, Eclairs (controlled by trusts associated with Igor Kolomoisky and by Gennadiy Bogolyubov) and Glengary (controlled by Alexander Zhukov and Mr Ratskevych). JKX issued disclosure notices between 20-26 March and on 13 May, requesting information from Eclairs, Glengary and Messrs. Kolomoisky, Bogolyubov, Zhukov, and Ratskevych about the number of shares held, their beneficial ownership, and any agreements or arrangements between the persons interested in them. The responses admitted the existence of interests in the shares but denied that there was any agreement or arrangement. On 23 May, Eclairs publicly invited shareholders to oppose the resolutions proposed at the forthcoming AGM on 5 June, including resolutions for the re-election of certain directors. At a meeting on 30 May, the JKX board considered that there were agreements or arrangements between the addressees of the disclosure notices which had not been disclosed in the responses. It resolved to exercise the powers under article 42 to issue restriction notices in relation to the shares held by Eclairs and Glengary, suspending their right to vote at general meetings and restricting the right of transfer.

Eclairs and Glengary challenged the restriction notices, relying on the proper purpose rule at s171(b) of the Act (a director must “*only exercise powers for the purposes for which they are conferred*”). Mann J held that the board’s decision was invalid. The article 42 power could be exercised only to provide an incentive to remedy the default or a sanction for failing to do so. The board had reasonable cause to believe that there was an agreement or arrangement between the addressees. But the board’s purpose was to influence the fate of the resolutions at the AGM. The Court of Appeal allowed the appeal by a majority, holding that the proper purpose rule did not apply to article 42 because the shareholders only had to answer the questions more fully in order to avoid the imposition of restrictions on the exercise of their rights, and because the application of the rule was inappropriate in the course of a battle for control.

JUDGMENT

The Supreme Court allows the appeals by Eclairs and Glengary, holding that the proper purpose rule applies to the exercise of the power under article 42, and that the directors of JKX acted for an improper purpose. The judgment is given by Lord Sumption, with whom Lord Hodge agrees. Lord Mance (with whom Lord Neuberger agrees) agrees that the appeals should be allowed, but prefers to express no view on aspects of the reasoning. Lord Clarke agrees, but prefers to defer a final conclusion on those aspects until they arise for decision and have been the subject of full argument.

REASONS FOR THE JUDGMENT

The proper purpose rule is concerned with abuse of power: a company director must not, subjectively, act for an improper reason. [14-16]

Where the instrument conferring a power is silent as to its purpose, this can be deduced from the mischief of the provision, its express terms and their effect, and the court's understanding of the business context. [30] Under article 42 in this case, the power to restrict the rights attaching to shares is ancillary to the statutory power to call for information under s 793. Article 42 has three closely related purposes: (i) to induce a shareholder to comply with a disclosure notice; (ii) to protect the company and its shareholders against having to make decisions about their respective interests in ignorance of relevant information; and (iii) as a punitive sanction for a failure to comply with a disclosure notice. Seeking to influence the outcome of shareholders' resolutions or the company's general meetings is no part of those proper purposes. [31-33]

The proper purpose rule applies to article 42. It is irrelevant whether Eclairs and Glengary could have averted the imposition of restrictions on their rights as shareholders by giving different answers to the questions. The proper purpose rule is the principal means by which equity enforces directors' proper conduct, and is fundamental to the constitutional distinction between board and shareholder. A battle for control of the company is probably the context where the proper purpose rule has the most valuable part to play. [35-40]

Lord Sumption and Lord Hodge consider that where the directors have multiple concurrent purposes, the relevant purpose or purposes are those without which the decision would not have been made. If that purpose or those purposes are improper, the decision is ineffective. [17-24]

Mann J found that four of the six directors were concerned only with the effect of the restriction notices on the outcome of the general meeting. They acted for an improper purpose. [41, 25]

Lord Neuberger, Lord Mance and Lord Clarke agree that the appeals should be allowed, but decline to express a concluded view on the application of a "but for" test to the proper purpose rule. [46-55]

References in square brackets are to paragraphs in the judgment

NOTE: This summary is provided to assist in understanding the Court's decision. It does not form part of the reasons for the decision. The full judgment of the Court is the only authoritative document. Judgments are public documents and are available at: <http://supremecourt.uk/decided-cases/index.html>