

UK SHAREHOLDER ACTIVISM

Briefing

Pursuing Derivative Claims

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Where certain specified types of wrong are committed by company directors, a shareholder can bring a claim on behalf of the company but in the shareholder's own name; however, he or she can continue with it only with the permission of the court. Such a claim is known as a derivative claim, and it must be brought in accordance with the United Kingdom's Companies Act 2006 as amended (the 'Companies Act').

Derivative Claims

If a shareholder of a company subject to the Companies Act can show that a director has been negligent, in default or committed a breach of his or her duties and/or a breach of trust (but not for any other reason), then that shareholder can bring a derivative claim in the name of the company under the Companies Act, for the wrong done to the company, in order to obtain relief on behalf of the company. The director(s) in question need not have benefited personally for such a claim to be made. The shareholder must file evidence establishing the basis for a claim and obtain the court's permission to continue with it.

What Can Be Brought as a Derivative Claim?

A shareholder can only bring a derivative claim for a cause of action arising from one of the wrongs specified above (a director's negligence, default, breach of duty and/or breach of trust). For such purposes, 'director' includes former directors and shadow directors. A derivative claim can also be brought against third parties who acted as accessories to the director for dishonest assistance in connection with a director's breach of fiduciary duty. There is no requirement to show that the wrongdoer benefited from the breach in question.

Who Can Bring a Derivative Claim?

A shareholder of the company can bring, but must seek permission of the court to continue with, a derivative claim. There is no minimum number of shares that the shareholder must hold, but the court will likely look at the size of the shareholding in deciding whether or not to permit a derivative claim to be continued. Whilst it is immaterial if the cause of action arose before the applicant became a shareholder of the company, the court can take into account matters about which a shareholder knew when he or she became a shareholder in assessing whether to grant permission to continue with a claim.

The Discretion of the Court

Whilst no permission is required to bring a derivative claim, the permission of the court is required to continue with it. If the shareholder cannot show a *prima facie* case the court must dismiss the application. Similarly, the court must refuse permission to continue with a derivative claim if:

- A person acting in accordance with the duty to promote the success of the company under Section 172 of the Companies Act (the statutory duty to promote the success of the company) would not seek to continue the claim; or
- The proposed or past act or omission for which the member wants to bring a derivative claim had been authorised by the company before it occurred or has been ratified since it occurred (though in this regard we note that *ultra vires* acts and unlawful or fraudulent acts cannot be effectively authorised or ratified).

The discretion to grant or withhold permission to continue with a derivative claim is exercised by the court regarding all relevant matters. The court must, however, take into account:

- Whether the member is acting in good faith;
- The importance which a person acting in accordance with the duty to promote the success of the company under Section 172 of the Companies Act would accord to the proposed claim;
- Whether a proposed or past act or omission would be likely to be authorised or ratified by the company;
- Whether the company has decided not to pursue the claim;
- Whether the member has a cause of action that he or she may pursue in his or her own right rather than on behalf of the company; and
- The views of the members of the company who have no personal direct or indirect interest in the matter.

Even if an activist shareholder has a financial interest in bringing a derivative claim (besides the financial benefit that will accrue to it indirectly through its shareholding if the claim is successful), the court can still grant permission if the pursuit of the claim will also promote the success of the company.

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If you have any questions concerning this *Briefing*, please contact your attorney at Schulte Roth & Zabel or one of the following attorneys: [Eleazer Klein](#), [Jim McNally](#) or [Marc Weingarten](#).

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