

The capital structure of a company law company business partnership essay

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Once there is no doubt of a 'class right' being sought or 'varied' or 'abrogated', the procedure to be adopted depends on whether the articles or terms of issue contain an express provision for variation, s630[5]-631[6]. S629-634[7] ensures the protection of "'class rights' of shareholders so that they cannot simply be varied or altered or removed by alteration of the documents in which they are contained, that is, the articles or a resolution passed under the authority of the articles"[8]. The legislature has intervened to protect the holders of shares enjoying class rights with a procedure which has to be followed before the class right can be varied or abrogated. The wording of company's articles determines issue of shareholders' consent required for reduction of capital amounting to variation of class rights[9]. If on one side, the variation of class has a range of class rights which has been judicially extended to offer a greater protection to shareholders, on the other side of the coin, the variation of class rights weaken the protection offered to shareholders on a particular shares by making a distinction between direct and indirect variation of shareholders rights. Thus, it may be ventured out that variation of class has both strengths as well as weakness. However, the question which comes to mind is whether there is a balance between the strengths or weakness or whether one over powers the other. The leading authority for this area of law, that is, variation of class rights is the *Cumbrian Newspaper Group Ltd v Cumberland and Westmoreland Herald Newspaper and Printing Co Ltd*[10]. In this case, the right in issue was a right given to the plaintiff under the defendant's articles, including a pre-emptive right regarding the transfer of any shares in the defendant and the right to nominate a director to the board of the defendant so long as it held 10 per

cent of the issued ordinary shares of the defendant. These rights were held to be class rights, only alterable in accordance with the special procedure set out in now s. 630[11]. It was held that the "rights attached to a class of shares' could only be varied with the consent of class members. It is not necessary for the rights to be attached to particular shares as long as they are given to class members in their capacity as members or shareholders. The plaintiff's rights were class rights and could not be varied without its consent"[12]. This decision means that if particular rights are granted to an individual shareholder they would not be alterable without the consent of that shareholder. Thus the shareholder would form a class of one. A deeper analysis of this case will lead to the fact that there is no difficulty in determining what class rights are, if company shares capital is divided into specific different classes of share, for example, different classes of share or in capital, dividend and voting rights. However, the difficulty lies in other types of non-conventional rights of shareholders, for example, rated voting rights and pre-emption rights, among others. Such rights are found only in the article of private companies. The Cumbrian case had the duty of determining whether such right not conferred on a shareholder as a member of conventional class could be considered as a class right. Scott J justified his judgement by what he perceived as the legislative purpose behind s630[13] which ensure the protection of such rights and by which may at least be subject to removal by simple alteration of the article. Moving on to the strengths of variation of class rights, it can be said that the major strength lies in statutory provisions, namely, s629-634, which ensures the protection as already mentioned above. If class rights are attached by

memorandum and the memorandum and the articles do not contain a provision with respect to the variation of those rights, then those rights may be varied if all the members of the company agree[14]. Under s630(4)[15], the rights may be varied by consent which may be given in writing by holders of at least three-quarters of the nominal value of the issued shares of that class (excluding any held as treasury shares) or by special resolution passed at a separate general meeting of that class of shareholders.

However, it should be noted that these provisions are without prejudice to other restriction upon the existing class rights[16]. In addition, where a variation of class rights in a company with a share capital has taken place in accordance with s630[17], s 633[18] provides for holders of less than 15% of the issued shares (that is, minority shareholders) of the class affected, if they did not provide their consent or voted in favour of the variation, they may make an application to the court to have the cancellation of the variation. The court has discretion to either disallow the variation -if the variation is likely to be unfairly prejudicial to the shareholders of the class represented by the applicant - or if not satisfied, the court can confirm the variation.

Under s633(4)[19], application must be made within 21 days- after appropriate consent was given or the passing of resolution by shareholders appointed- in writing. The court's decision is final and binding, s633(5)[20]. S634[21] confers the right to object to a variation for companies without a share capital. The narrow scope must be taken into consideration, that is, the above provisions only applies to a variation of class under s630-631 and to a genuine ' variation' or ' abrogation' of a class right. In *Carruth v Imperial Chemical Industries Ltd*[22], it was held that a minority shareholder within

the relevant class has a right to challenge a class resolution on the ground of bad faith. Moreover, in *British American Nickel Corporation v O'Brien*[23], the company had issued mortgage bonds secured by a trust deed that provided that a majority of bond holders, representing not less than three-quarters in value, could sanction a modification of the bondholder's rights. But, although the reconstruction scheme of the company was supported by the majority, the court held that one of the bond holders without whose vote the proposal would not have been accepted had been influenced to reject the proposal by a promise of a greater amount of ordinary shares and the vote was thus invalid since the voting for a modification of class rights, it should be beneficial to the class as a whole. Similarly, in *Re Holders Investment Trust Ltd*[24], -whereby the company sought confirmation from the court of a reduction of capital by which it is proposed to cancel the redeemable preference shares and to allot the holders an equivalent amount of unsecured loan stock- it was held that shareholders voting in a class meeting in connection with a reduction of capital must have regard to the interests of a class as a whole. Furthermore, the court stated that the vote was ineffective as the majority preference shareholders had voted in their own interests without taking into consideration what was for the best for the preference shareholders as a class. Another protection is that a variation or abrogation of a class right can clearly be ascertained when the alteration directly conflicts with and purports to override the particular provision under which the right arises, for example, a reduction of a preferential dividend from 10% to 5%. Clearly it involves the variation of the class right. Even if there is a large number of statutory provisions and common law to

safeguard shareholder's rights, the variation of class is not wholly reliable as it does have shortcomings along with shortcomings along with the protection conferred to shareholders. In simpler terms, it can be thrust into prominence that shareholders are not fully protected. One of the weaknesses of variation of class right is that it favours a possible breach of director's duty to act fairly. Moreover, more than once, minority shareholders have lost benefit of their rights without any class meeting held in circumstances where the relevant modification of rights clause seen to have intended to supply protection to them, *Greenhalgh v Arderne Cinemas Ltd*[25]. In this case, the company had two classes of shares: one with a nominal value of 10p and the other with a nominal value of 50p; both shares had the right to one vote per share. The holder of the 10p was able to dominate the company's decisions. To destroy the power of this class of share, the company passed a resolution splitting the 50p shares into five 10p shares, each with a right to one vote per share. The court held this was not a variation of the rights of the holder of the 10p shares and a rateable reduction of all shares, including preference shares was not a variation of the class rights. In addition, there can be no variation by resolution altering the literal term of the class right. Below are two important examples. Firstly, an issue of new shares ranking *pari passu* (that is, equal footing) with a certain class; and secondly, the alteration of the place of payment of dividends from England to Australia causing the fixed preferential dividend payable to a certain class right to be of lesser value because the Australian pound was worth less than the English pound sterling, *Adelaide Electric Supply Co Ltd v Prudential Assurance Co*[26]. In *White v The Bristol Aeroplane Co Ltd*[27], the company's articles

provided that the rights attached to any class of shares might be 'affected, modified, varied, dealt with, or abrogated in any manner' with the sanction of an extra ordinary resolution at class meeting. Lord Evershed MR, suggested " that it was not the class of rights of the complaining class that were varied or abrogated or affected, but merely the ' enjoyment' of those rights"[28]. Another weakness is that preference shares may be issued at detriment if ordinary shareholders, *Re John Smith's Tadcaster Brewery*[29]whereby it was also held that a right unrelated to any shareholding cannot by stretch of imagination be a class right, *Jenkins LJ*. The same principle was applied in *Re Mackenzie and Co Ltd*[30]whereby the preference shareholders were entitled to a dividend of 4% of the amount paid up on their £20. Only the ordinary shareholders voted for a reduction in the company's share capital, including both ordinary and preference shares and the court held that it did not amount a variation of the preference shareholders' rights as the right to a 4% dividend remained the same. Moreover, in *Re House of Fraser plc v ACGE Investments Ltd*[31], whereby preference shareholders were entitled to a dividend of 4 per cent on the amount paid up on their shares. The full nominal value had been paid on each share but a general meeting of the company at which preference shareholders were not entitled to vote approved a reduction of capital which would reduce the nominal value of each share so that the preference dividend would be reduced. This was held not to be a variation of the preference shareholder's rights. However, this protection is a restrictive interpretation of what amounts to a variation, *Greenhalg v Arderne Cinemas*[32]. Nevertheless, with s994[33], added protection there is the

possibility of shareholders claiming that a variation could be successfully contested by a petition against unfair prejudice along with the Shareholders Rights Directives[34]safeguarding the latter's rights. Directive also provides that a company shall ensure that there is equality of treatment for all shareholders who hold the same rights[35]. Furthermore, human rights protection is provided to shareholders regarding social and economics, Grainger v UK[36]These two provisions make it conspicuous the fact that the strengths outweigh the weaknesses with quite a large number of protections is being conferred to safeguards shareholder's rights. In light of a conclusion, it cannot be said that legal provisions are sufficient to protect all shareholders, including minority as there are still drawbacks which need to lessen if not eradicated by legal provisions. Word Count: 2250