



Précis Paper

Oppression of Minority Shareholders and Share Issues

This presentation discusses an interesting recent case that explored issues relating to oppressive conduct in share issues.

Discussion Includes

- Background and material facts
- Oppression of minority shareholders
- Jurisdiction of the Federal Court
- Allegations of misconduct by the majority shareholder
- Share issues made for an improper purpose
- Remedies
- Advising clients about share issues

Précis Paper

Oppression of Minority Shareholders and Share Issues

1. In this edition of BenchTV, Joshua Knackstredt (Barrister, Greenway Chambers, Sydney) and Ian Benson (Solicitor, AR Conolly and Company) discuss the recent case *Corbett v Corbett Court Pty Limited, in the matter of Corbett Court Pty Limited* [2015] FCA 1176.

Background and Material Facts

2. Corbett Court Pty Limited was a family company established by Mr and Mrs Corbett, who were deceased. All of the shares in Corbett Court were, from its incorporation in December 1993 to May 2012, held by eight siblings, the children of Mr and Mrs Corbett. One of the eight children was given 50 percent of the shares in Corbett Court, and the other seven children received approximately 7.1 percent each.
3. The company was originally set up to develop a piece of land in Picton, NSW. Two parcels of land were amalgamated and a building housing a large supermarket was constructed. The company later built the Picton mall on a large parcel of land.
4. The directors were initially the two parents and their son who owned the 50 percent stake in the company. This meant that once both parents died, this son became the sole director of the company.
5. Tensions arose between family members when the company came into financial difficulty. Because of a downturn in the local economy due to the global financial crisis, there was a drop off in the tenants in the Picton mall, and the anchor tenant, Coles, threatened to withhold rent unless tenancies were increased. As a result, Corbett Court determined that it would redevelop part of the mall, and proposed to issue new shares in order to raise money.
6. Because of the tensions that had arisen and a continuing dispute about the parents' estate, there was a distinct lack of trust between the shareholders. The seven minority shareholders did not have access to information about the internal workings of the company and what its financial position was.

Dilution

7. At incorporation, the company had 84 shares on issue. Following the second share offer, the company issued 100,000 additional shares, half of which were issued to the existing 50 percent shareholder, and half of which were issued to his wife, who effectively acquired an

almost 50 percent holding in the company through this action. The share issue diluted the minority shareholders' holdings from around 7% to approximately 0.005% each.

8. One of the minority shareholders brought proceedings in the Federal Court alleging oppression. The Federal Court had jurisdiction pursuant to ss 232 and 233 of the *Corporations Act 2001* (Cth).

The Issues before the Federal Court

9. The central issue was whether the issue of 100,000 shares for \$1.00 each to the majority shareholder and his wife was contrary to the interests of the members as a whole or oppressive, unfairly prejudicial to or unfairly discriminatory against the minority shareholders. The key question was whether the moving purpose of the share issue was not to raise money, but to dilute the minority shareholders' interests.
10. It was also alleged that the company had been incorporated and operated on the basis of an understanding that there would be fixed ownership proportions, according to the share structure put in place by the parents. In some circumstances, a departure from an understanding of this nature can be oppressive.
11. Finally, the plaintiff argued that the share issue contravened provisions in the company's constitution.
12. The respondents alleged that without the money raised by the share issue, the company would be insolvent, and that there was no other source for the money. On this basis, they argued that the dominant purpose was a legitimate one.

The Court's Decision

13. Of the money that was contributed by the majority shareholder and his wife in the share offering, \$900,000 was contributed by way of a loan to the company, secured by a second mortgage and subject to interest payments, and only \$100,000 was contributed as part of the equity issue. In other words, \$100,000 was paid for 100,000 shares issued at par value. There was no attempt to value the company for the purpose of the share issue or explain why the loan of \$900,000 could not have instead been a loan of \$1 million, with no shares issued.
14. The Court held that the share issue was oppressive, had been made for an improper purpose and was commercially unfair.
15. The Court stated that "[t]he moving cause of the Share Issue was John's desire to resolve the impasse with his siblings in the context of the administration of the intestate estate of

his parents" (at [193]). Moreover, the amount provided by the majority shareholder was arbitrary and unconnected with any commercial reality.

16. In relation to unfairness, the Court found that because the majority shareholder and the company had not offered the minority independent advice about the share offers, there had been commercial unfairness.
17. In relation to the purported understanding about fixed ownership proportions, the Court found that there was no real expectation that the ownership proportions would remain fixed, and no evidence that the majority shareholder had agreed to be bound by that understanding.

Orders

18. Courts have wide powers to make orders in oppression cases. Orders can include the amendment of the share register, requiring a shareholder to buy out another, or winding up a company. However, courts are generally reluctant to wind up business that are going concerns unless that is the only option.
19. Here, the plaintiff sought a buy-out order, but advanced as an alternative an application for the Register to be corrected and the share issue to be set aside. Ultimately, orders were made setting aside the share issue and requiring the Register to be rectified.

Lessons for Practitioners

20. Mr Knackstedt advised practitioners that the purpose for the share issue is critically important. If a share issue was caused because of a wish by directors to take control or acquire a majority interest, then careful attention has to be given to the way in which a transaction is structured.
21. Moreover, it is important to ensure that shareholders are treated in a manner that is fair, which may require independent advice. A share issue that has a drastic effect on minority shareholders is open to attack.

BIOGRAPHY

Joshua Knackstedt

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Joshua Knackstedt was called to the Bar in 2007. He specialises in commercial, corporations, real property, equity, and construction and strata law. He has appeared both led and unled in the NSW Supreme Court, NSW Court of Appeal and Full Federal Court, as well as in other courts and statutory tribunals. Joshua has a number of business interests outside of the law, including part-ownership and a directorship in a Sydney-based technology company and an interest in an investment fund manager. He is also a Member of the Australian Institute of Company Directors.

Ian Benson

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Ian Benson is a solicitor at AR Conolly and Company and holds a First Class Honours degree in Law.

BIBLIOGRAPHY

Focus Case

Corbett v Corbett Court Pty Limited, in the matter of Corbett Court Pty Limited [2015] FCA 1176

Benchmark Link

https://benchmarkinc.com.au/benchmark/composite/benchmark_10-11-2015_insurance_banking_construction_government.pdf

Judgment Link

<http://www.austlii.edu.au/au/cases/cth/FCA/2015/1176.html>

Legislation

Corporations Act 2001 (Cth)