

## Episode 48: Summary

**Episode name:** Springing into (Derivative) Action - Derivative Actions under the *Corporations Act 2001* (Cth)

**Guest(s):** James d'Apice

**What area(s) of law does this episode consider?**

Derivative actions brought by shareholders on behalf of the company in which they hold shares, under s 237 of the *Corporations Act 2001* (Cth).

**Why is this topic relevant?**

When the members and the officers of a company disagree on whether the company should bring litigation, the *Corporations Act* affords those members an opportunity to bring that litigation themselves, as a derivative action.

A company's directors may decline to pursue a claim where that claim is against the directors themselves; or the company may be unable to resolve to pursue a claim because of a deadlock between the company's owners. Derivative actions are therefore often pursued in the event of disputes between shareholders.

**What legislation is considered in this episode?**

*Corporations Act 2001* (Cth)

**What cases are considered in this episode?**

*Charlton v Baber* [2003] NSWSC 745

- Charlton, a shareholder and former director of Newcastle Auto Air, alleged that Baber, the other director, had breached his duties to the company by paying himself excessive remuneration and dividends, and entering into uncommercial lease arrangements and loans. The company was a 'quasi-partnership' and was incapable of pursuing the claim against Baber itself. Thus, Charlton sought to bring action against Baber on behalf of the company, under Pt 2F.1A of the *Corporations Act*.

*Carpenter v Pioneer Park Pty Ltd (in liq)* [2004] NSWSC 1007

- A shareholder and former director of Pioneer Park, a company in liquidation, sought to pursue a derivative action. In order to prove that there was a serious question to be tried, the shareholder relied upon a lengthy legal opinion from senior counsel, tendered without a waiver of privilege. This was accepted as probative evidence of there being a serious question to be tried.

*Chapman v E-Sports Club Worldwide Ltd* [2000] VSC 403

- Chapman was the plaintiff in a derivative action brought on behalf of E-Sports Club Ltd in relation to an alleged infringement of intellectual property by E-Sports Club Worldwide Ltd, by reason of an allegedly unauthorised transfer of the intellectual property from one company to the other. The Court declined to grant Chapman leave to bring a derivative action, not being satisfied that Chapman was acting in good faith, that the proceedings would be in the best interests of the company, nor that there was a serious question to be tried.

The Court also found that, given that the holders of 90 percent of the shares did not want to bring the litigation, and Chapman only held the remaining 10 percent of the shares, a more appropriate course was for Chapman to seek relief in relation to oppressive conduct under s 233, if such oppressive conduct could be made out on the evidence.

*In the matter of Global Advanced Metals Pty Ltd* [2019] NSWSC 1804

- A minority shareholder in Global Advanced Metals, Metallurg, sought leave to take action against the directors of Global Advanced Metals for breach of directors' duties in relation to a sale they made in 2016: the directors agreed to sell a company assets for \$60 million, which the shareholder believed was worth between \$245 million and \$900 million at the time. Metallurg indemnified the company for the cost of the prospective litigation. While the minority shareholders were found to be acting in good faith, the Court was not satisfied that the proceedings were in the Company's best interests. Although the indemnity from Metallurg cured the detriment that might be suffered by the company from an adverse costs order, the proceedings would impose other detriments on the company, such as the distraction of the litigation for GAM's executives and directors. These detriments were weight against the prospects of success of the proceedings in reaching the conclusion that the proceedings were not in the company's best interests.

#### What are the main points?

- To take derivative action to pursue a company's claim, you first must seek leave from the Court to act on the company's behalf under section 237 of the *Corporations Act*. This requires satisfaction of the following elements:
  - the applicant is acting in good faith
  - there is a serious question to be tried
  - the applicant has given the requisite notice of the application to the company (14 days notice before making the application for leave)
  - the proceedings are in the best interests of the company
  - it is unlikely that the company will itself bring the action.
- The typical case is where the directors have allegedly breached their duties to the company, so the directors would be unwilling to cause the company to take action; or where the company is run as a quasi-partnership and its board and members are so deadlocked that the company cannot resolve to bring the action.
- In shareholder disputes, alternatives to bringing a derivative action include corporate oppression proceedings under section 232 and 233 of the *Corporations Act* or an application for the winding up of the company on just and equitable grounds.

#### What are the practical takeaways?

- When advising a member or officer who wishes to pursue legal action on behalf of a company, it is important that they are made aware that even if they are successful in the proceedings, the judgment amount or settlement sum will be paid to the company, not to the shareholder bringing the action. This means that shareholders bringing derivative actions are often bearing the cost of the action, and the risk of an adverse costs order (the usual rule that costs follow the event still applies to derivative actions brought by shareholders), but

are only entitled to a fraction of the potential benefit. The claim the shareholder wishes to seek must therefore not only have good prospects of success, but must be of a sufficient quantum to justify the costs exposure.

**Show notes**

[Chamberlains' article 'Winding Up On Just & Equitable Grounds: Quasi-Partnerships'](#)

[Ian Ramsay's research report 'Litigation by Shareholders and Directors: an Empirical Study of the Statutory Derivative Action'](#)

[James d'Apice's YouTube channel 'Coffee and a Case Note'](#)