

Shareholder activism in Guernsey

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Shareholder activism refers to the use of ownership position in order to influence a company's policy and practices and is a very live issue in the current economic climate. It has risen exponentially over the last few years, fuelled by economic pressures and a robust merger and acquisition environment.

Whilst shareholder activism can be no more than simply a gentle suggestion by a shareholder in relation to the direction of a company, in general, the term shareholder activism usually connotes more extreme action by a proactive shareholder seeking to effect change in a company (often publicly).

This note aims to set out some of the main powers available to activist shareholders in relation to publicly traded Guernsey companies, together with some of the potential pitfalls which need to be avoided when taking such action. It also looks at how companies can mitigate against the risk of an aggrieved shareholder.

Powers of the Activist Shareholder

[Requesting a copy of the share register](#)

Any member of a company has a right to inspect the company's register of members under section 127 of the Companies (Guernsey) Law, 2008 as amended (the "2008 Law"). A common tactic used by the activist shareholder is to request a copy of the register of members in order to contact other shareholders in an attempt to garner their support.

[Powers at general meetings](#)

Shareholders have the power to vote at each annual general meeting. The directors' report in relation to the Company's financial statements is tabled at the annual general meeting. Under section 220 of the 2008 Law, the members may raise any matter arising out of the directors' report at the meeting, enabling them to voice any concerns they may have. However, it should be noted that shareholders do not have the power to reject or 'vote down' the directors' report.

Another tactic available to shareholder activists at the annual general meeting is to vote against the re-election of any directors retiring by rotation, leading to a change in the board of the company.

[Power to require circulation of a written resolution](#)

Under section 183 of the 2008 Law, shareholders in a Guernsey company holding at least 5% (or a lower percentage stipulated in the company's Articles) of its voting shares can require the directors to circulate a written shareholders' resolution to eligible members (and can require the circulation of a written statement with the proposed resolution).

Following a request under section 183, the directors must send copies of the resolution to eligible members (and any written statement) within 21 days, and if a company fails to comply they are guilty of an offence. However, if the company believes that the rights conferred by section 183 are being abused, the company can apply to the Court and seek an order that they need not circulate the members' statement.

For a listed company, it may not be possible to obtain sufficient signatures to pass the written resolution. Nevertheless, the circulation of a statement and resolution can be used to exert pressure on the directors.

Power to require directors to call a general meeting

Shareholders in a Guernsey company who hold more than 10% (or a lower percentage stipulated in the company's articles) of its voting shares can require the directors to call a general meeting under section 203 of the 2008 Law. Although there is no prescribed form of words for a requisition, it must state the general nature of the business to be dealt with at the meeting and it may include the text of a resolution that may properly be moved at the meeting.

Under section 204 of the 2008 Law, directors in receipt of such a request must call a meeting within 21 days after the date on which they receive the request, and the meeting must be held not more than 28 days after the date of the notice convening the meeting.

If the directors fail to call the meeting in accordance with sections 203 and 204, the members requesting the meeting can call the meeting themselves at the company's expense (provided that the meeting is called within 3 months of the directors becoming required to call the meeting).

Shareholders often use the power to convene a general meeting in order to propose changes to the board of directors of the company. Under the 2008 Law, a person ceases to be a director if he is removed from office in accordance with the company's memorandum or articles, and a person can be appointed as a director by an ordinary resolution requiring a simple majority vote (unless the company's memorandum or articles provide otherwise). A company's memorandum and articles will usually state that the members of the company can remove and appoint directors by ordinary resolution. Therefore, if a disgruntled shareholder can obtain the support of members by a majority vote in general meeting, he can effect changes to the board of directors.

Legal proceedings

In extreme cases, a disgruntled shareholder may commence legal proceedings, such as a derivative action or a claim for unfair prejudice.

If a shareholder is able to demonstrate that a director (or a former director) has breached his fiduciary duties, they may be able to maintain a derivative claim against that director on behalf of the company. Although derivative actions are becoming more common in Guernsey, the success of such an action is based on the facts of each particular case.

Alternatively, the remedy of unfair prejudice permits a shareholder to apply to the court for an order for relief where the affairs of a company are being conducted in a manner that is unfairly prejudicial to the interests of members generally or of some part of its members (including at least the applicants), or an actual or proposed act or omission is or

would be so prejudicial. The most common order made by the court as a consequence of a successful unfair prejudice action is an order for the shares of such member to be bought by the other shareholders or by the company. An unfair prejudice claim is difficult to pursue, as a shareholder must prove not only that the conduct complained of was unfair, but also that it caused (or would cause) him prejudice.

Other activist weapons

Together with the more traditional means of shareholder activism described above are a whole range of both more and less aggressive strategies which can be employed by a dissatisfied shareholder.

At one end of the scale is a gentle suggestion from a shareholder of the direction the company should take, which may or may not be accompanied by the threat of the exercise of statutory powers available to him if his concerns are not addressed. At the other extreme is a shareholder who attempts to garner the support of other shareholders by voicing his concerns publicly, through the use of the press or social media.

We have had experience of activists requisitioning meetings in order to pass resolutions which would have the effect of directing the directors how to run a company. However, it is important to note the UK decision of *Gramophone and Typewriters Ltd v. Stanley* [1908] 2. K.B. 89, which held that "... even a resolution of a numerical majority at a general meeting of the company cannot impose its will upon the directors when the articles have confided to them the control of the company affairs." For Guernsey companies this principle is reinforced by the fact that, under Guernsey law, the directors derive their powers from statute and not by delegation from the shareholders. Shareholders may be able to impose limits on the powers of directors, but they cannot dictate the actions that directors must take.

"Bear hug" letters

A "bear hug" letter is a letter to the directors of a company containing a preliminary offer to acquire the company, typically proposing a friendly transaction but threatening a hostile one if the offer is rebuffed (often threatening to take the deal directly to the shareholders if the directors do not negotiate). The offer will be at a price which is significantly above market price, thus making it an offer that the directors will find difficult to reject (therefore, a "bear hug").

There is no set format for "bear hug" letters and therefore they can be used by a disgruntled shareholder to exert pressure on the directors to address their concerns, making it clear that such concerns and proposals will be publicly put to the remaining shareholders in the event that the directors do not take appropriate steps. Whether such a "bear hug" letter will be effective typically depends on the nature of the shareholder's concerns, together with the level of shareholder support referenced in the letter.

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In order for a “bear hug” letter to be effective, the directors need to believe that the shareholder has the means and the inclination to follow through with the offer if required.

Potential pitfalls for a Shareholder Activist

Shareholders considering taking activist action should be sure to obtain legal advice to ensure that they do not encounter any of the potential pitfalls identified below, which can have major consequences both for the company and for the shareholder concerned.

Takeover code

The UK City Code on Takeovers and Mergers (the “Takeover Code”) applies in Guernsey in the same way as it applies in the UK, and therefore shareholders must take care to ensure that a mandatory cash bid is not triggered under the Takeover Code by the formation of a concert party group (i.e. a group of shareholders holding in aggregate in excess of 30% of the shares). In addition, obligations arise under the Takeover Code if a party makes a statement indicating that a takeover offer will be made. This is a complicated area and further advice should be sought by shareholders if they have concerns.

Jurisdiction and Tax Residency

One particular area of concern, in particular for Guernsey investment vehicles, is to ensure that there are no unintended consequences resulting from shareholder activism causing changes to the board of directors. Shareholders must ensure that any replacement of the directors with directors not based in Guernsey does not prejudice the tax status of the company.

Directors’ Conflicts of Interest

Any directors appointed by an activist shareholder need to remember that their duties as a director are to the company, and not to the activist shareholder. Such directors should be mindful that they will not always be able to comply with the shareholder’s wishes or to provide company information to such shareholder.

Market Abuse and Insider Dealing

Another strategy often employed by disgruntled shareholders is to enter into short selling positions, but this brings with it a risk of the shareholder activist engaging in market abuse and insider trading if it is combined with other forms of activism which could affect the share price of the company.

Defamation

Activist shareholders using the press to garner support need to be mindful to ensure that any statements made do not amount to defamation.

Minimising the Risk of Shareholder Activism

The key consideration is minimising the risk of an activist shareholder for a company is for that company to maintain good relationships with its majority shareholders, ensuring that it addresses any concerns of the shareholders on an ongoing basis and maintaining effective communication.

Directors should ensure that the company has good standards of corporate governance and that they conduct regular reviews in order to identify potential areas of vulnerability which may be challenged by activists.

In the event that a company is faced with an activist shareholder, how the company deals with such a situation can have serious implications for the reputation of the company and how it communicates with its shareholders going forward. If an activist situation arises, the company should take steps to understand the shareholders’ concerns and how these might be addressed.



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