THE REPUBLIC OF UGANDA

IN THE HIGH COURT OF UGANDA AT KAMPALA

(COMMERCIAL COURT DIVISION)

HCT-00-CC-CS-0602-2004

JOEL ODONG AMEN

JUDITH ODONG AMEN……..PLAINTIFF

VERSUS

DR. OCERO ANDREW

DR. JANE ACENG OCERO……..DEFENDANT

BEFORE: HON. JUSTICE LAMECK N. MUKASA

RULING:

In this suit the plaintiff Joel Odong Amen and Judith Odong are husband and wife. The defendants Dr. Ocero Andrew and Dr. Jane Aceng Ocero are also husband and wife. All the four were the only shareholders in M/s Rhino Communication Company Ltd, a limited liability company. The plaintiffs jointly owned 40% of the shares of the said company while the defendants jointly owned 60% of the shares.

The plaintiff's claim as pleaded in paragraph 4 of the plaint is briefly that the shareholders of Rhino Communication Company Ltd agreed to sell the company to Jackson Senyonga and Evelyn Senyonga at Ugshs 50,000,000/=. An agreement, annexture "A" to the plaint, was made to that effect. That on receipt of the sales proceeds the defendants refused to hand over the 40% of the share of sales proceeds belonging to the plaintiffs and of the account balances in Kampala and Lira Bank accounts of the company. The plaintiffs brought this suit, inter alia, to the recover 40% of the sale proceeds, 40% of the money on the company's Kampala Bank account and 40% of the money on the company's Lira Bank account and general damages for breach of trust.

Representation was Mr. Hamu Mugenyi for the plaintiffs and Richard Obonyo for the defendants.

The plaintiffs adduced their evidence and closed their case. When the defence was due to open its evidence Mr. Richard Obonyo raised a preliminary point of law that the plaintiffs as shareholders of M/S Rhine Communication Company Ltd do not have a cause of action in this matter against the defendants. Counsel contended that it should have been the Company Rhino Communication Company Ltd to institute the suit if there was any breach. He argued that the alleged breaches, if at all committed, were committed against the company and not the plaintiffs. Counsel argued that:-

1. In paragraph 3 of the plaint the plaintiffs claim 4% of the account balances at Centenary Rural Development Bank.
2. In paragraph 4 (e) the plaintiffs contend that the proceeds of the sale of the company were managed by M/S Ocen & Co Advocates without authorisation.
3. In paragraph 4 (h) the plaintiff's claim that they were not given proper accountability of the sales proceeds and account balances of the Company.

Counsel further argued that the cause of action is founded on the sale of the Company's assets, revenue and account balances as exhibited in the Sale Agreement- annexture A to the plaint. He submitted that since the alleged wrongs were committed against the company the proper plaintiff to seek redress should have been the company itself. Counsel referred to Foss Vs Harbottle (1843) 2 Hare 461 cited by Justice James Ogoola in Allied Bank International Ltd Vs Sandru Kara & Abdul Kara HCT-00-CC-Cs 0191-2002 for the general rule that for derivative actions the proper plaintiff in an action to redress an alleged wrong to a company is the company itself . This is what is referred to as the famous rule in Foss Vs Harbottle. As of this rule it is stated in Gower's Principles of Modern Company Law 4th Ed page 641 that if a complaint is made that the directors have broken their duties of loyalty, care or skill the company is the proper plaintiff in an action against them

In his submission Mr. Hamu Mugenyi argued that there are exceptions to the rule in Foss Vs Harbottle (supra). Counsel cited Gowers (supra) pages 642 – 643 where the learned auditor spells out the following exceptions to the rule:-

(i) When it is claimed that the company is acting or proposing to act ultra vires.

(ii) When the act complained of though not ultra vires, the company could be effective only if resolved upon by more than a simple majority vote, say where a special or extra ordinary resolution is required and (it is alleged) has not been validity passed.

(iii) Where it is alleged that the personal rights of the plaintiff shareholder have been infringed or are about to be infringed at any rate if the wrong to the plaintiff could not be rectified by an ordinary resolution of the company.

(iv) Where those who control the company are perpetrating a fraud on the minority,

(v) Any other case where the interests of Justice require that the general rule, requiring suit by the company, should be disregarded.

The learned author then states:-

> "Apart from this fifth except, in so far as it exits, all these excepts could be reduced to one by saying that an individual shareholder can always sue, notwithstanding the rule in Foss Vs Harbottle when what he complains of could not be validity effected or ratified by an ordinary resolution."

In the instant case there are only four shareholders in the company. The plaintiffs are the minority shareholders with 40%, while the defendants are the majority shareholders with 60% thus with more control of the company. The defendants just like the plaintiffs are spouses. In the plaint the breach complained is alleged to have been committed by or with the sanctioning of the defendants. A suit by a company can only be sanctioned by a resolution of the company. In the above circumstances it would be quite impossible for the company to pass a resolution to file a suite against the defendants who are in its control for the breaches allegedly committed by them.

The fifth exception is in line with Article 126 of the Constitution which provides:

"126 (2) In adjudicating case of both civil and criminal nature, the Court shall, subject to the law, apply the following principles:-

(a) Justice shall be done to all irrespective of their social and economic status,

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(e) Substantive justice shall be administered without undue regard to technicalities "

In Allied Bank International ltd Vs Sadru Kara 4 Another (Supra) Justice Ogoola, P.J. pointed out that there are exceptions to that general rule, the parameters of which have been carefully crafted and strictly defined. He cited from Modern Company Law (2nd Ed) page 528 for the rationale for exception as thus:-

"If there were no such exceptions, the minority would be completely in the hands of the majority. Even the limitations imposed by the substantive law would be stultified, for as long as the company remained a going concern no action could effectively be brought to enforce them."

In Salim Jamal & Others Vs Uganda Oxygen Ltd & Another S.C, C. A, No, 64 of 195. Oder JSC stated:

"Two recent decisions in our jurisdiction will, I think suffice to illustrate that courts will go behind the corporate veil in the interest of justice, on grounds of fraud, to enforce compliance with contractual obligations or enforce economic realities obtaining under a holding company and its subsidiaries."

His Lordship then named and discussed National Enterprises Corporation Vs Nile Bank Civil Appeal No 17/94 (SCU) unreported and Fam International & Another Vs Ahamed Halid el Fathi Civil Appeal No. 6/93 (SCU) unreported.

Substantive Justice demands that where the minorities rights cannot be enforced by an action because of the majorities making it impossible for the company to institute a suit then a shareholder can himself file the suit if he can bring himself within the ambit of the exceptions to

the Foss Vs Harbottle rule. The pleadings in the instant case show that the plaintiffs were in the circumstances within that ambit.

However, Counsel for the defendants submitted that for a shareholder to file a suit within the exception he must by his pleadings show that his case was within the exceptions to the general rule. He argued first that in the plaintiffs' pleadings there was nothing to indicate that fraud had been committed by the defendants and further that there were no particulars of fraud pleaded. Secondly that in such an action the company against which the alleged wrong had been committed should have been made a party. He submitted that this is a strict requirement which had not been satisfied. Thirdly the plaintiffs must have filed the suit in a representative capacity. They should have shown by their pleadings that they were suing on behalf of the company but that they had sued in their names having failed to obtain a company resolution to file a suit in the company's name. and further that the wrongs complained of could not be ratified by the general meeting of the company.

In Allied Bank International Ltd Vs Sadru Kara & Other (supra) Justice James Ogoola stated:-

> "What is abundantly obvious however is the obligation for the particular shareholder to bring himself squarely within the ambit of the exception to Foss Vs Harbottle. The criteria for this have been clearly established by among others, Gowers Principles of Modern Company Law (3rd Edn). The principles were recited, with approval, by Order JSC in the Uganda Oxygen Case supra at page 137 thus."
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> '(i) Normally, the wrong complained of must be such as to involve fraud on the minority, which could not been validly waived by the company in a general meeting, such conduct include:

(a) Expropriation of the property of the company or in some circumstances that of the minority;
(b) Breach of the directors duties of subjective good faith;
(c) Voting for company resolutions not bonafide in the interest of the company;

(ii) It must be shown that the alleged wrongdoers control the company.

(iii) The company must be a defendant in the action – the company is the true plaintiff and if a money judgment is recovered against the true defendants – the wrong doing directors or controllers – this will be in favour of the company and not in favour of the individual shareholder who is nominal plaintiff. The company cannot, in fact be the plaintiff because neither of its organ – the board of directors and the general meeting will authourise suit by it. As the next best thing the court insists upon its being made nominal defendant (see Spokes Vs Grosvenor Hotel (1897) 2 Q B 124)

If the company has ceased to exist and cannot be resuscitated --- it seems that no action can be brought: Clarkson Vs Davies (1923) AC 100

(iv) The shareholder must sue in a representative capacity or on behalf of himself and the other members other than the real defendant--- for it ensures that all the other shareholders are also bound by the result of the action (i.e. resjudicata).

All the above forms a compact summary and encapsulation of the law on derivative actions. ---"

I will now deal with each one of the above principles:-

(i) Fraud on the minority

In the plaint it is stated that the defendants without consulting and without permission of the plaintiffs appointed M/s Ocen & Co Advocates as the advocates for the sale of Rhino Communications Company Ltd who instructed the purchasers Jackson Senyonga and Evelyn Senyonga to channel the sales payment through the said law firm. Secondly, that on receipt of the sale proceeds through their advocates, the defendants refused to hand over the plaintiffs' 40% of the shares of the sales proceeds belonging to the plaintiffs. Further that the defendants refused to hand over 40% of the sums of the money on Centenary Rural Development Accounts at Kampala and Lira branches. Thirdly, that the defendants claimed that they had used all the money to clear off the debts of Rhino Communication Company Ltd without the authority and

permission of the plaintiffs and had failed to show the plaintiffs the vouchers of those payment for verification.

Without going into the merits of the case at this stage the above allegations show a claim of fraudulent expropriation of the company's funds and the plaintiffs share interests in the proceeds of the sale of the shareholders shares in the company. The plaintiffs are the minority shareholders. The plaintiffs further plead that the defendants conduct was untenable and a breach of the trust the plaintiffs has placed on the defendants as the majority shareholders of the company,

(ii) Wrongdoers being in control of the company - the defendants were the majority shareholders with 60% shareholding. Evidence so far adduced shows that the first defendant, Dr. Ocero Andrew was the Managing Director in the company and the second defendant Dr. Jane Aceng Acero was also a director in the company. They are the alleged wrongdoers and in the circumstances had control of the company.

(iii) The company must be a defendant. The requirement to make the company a party to the proceedings as a nominal defendant has not been satisfied in the instant case. However, the underlying intention of derivative actions is to enable the minority redress a wrong brought upon the company by the miscreant majority. To ensure justice to the minority this Court can invoke the provisions of 0.1 rule 9 CPR which provides:

> "No suit shall be defeated by reason of mis joinder or non rejoinder of parties and the Court may in every suit deal with the matter in controversy so as far as regards the rights and interests of the parties actually before it."

The plaintiffs also have a right under 0.1 rule 13 CPR at any stage to make an application for leave of Court to add the company as defendant. And if found necessary this court can pursuant to its inherent powers under section 98 of the Civil Procedure Act order the company to be added as a defendant in order to promote the ends of justice or to prevent abuse of the process of Court.

(iv)The shareholder to sue in a representative capacity or on behalf of himself and other members other than the defendants - There were four shareholders in the Company Two of the four are the defendants and the two plaintiffs are the only other members. Therefore, this requirement is satisfied.

As to the requirement to specifically plead fraud, in cases of this nature fraudulent dealing can be regarded as synonymous to wrong doing.

In Gower (supra) at page 588 the learned author talks of a "wrong" done to the company interchangeably with "fraud" and then specifically list examples of such "fraud" as including expropriation, breach of directors duties, voting resolutions that are not bonafide the interest of the company. I therefore find the requirement not so strict in case of this nature. The plaintiff's pleadings have disclosed the defendants' complained of wrongdoing which satisfies that requirement.

It was also argued by counsel for the defendants that the agreements attached to the plaintiffs' pleadings were in subsistence executed by the persons named therein without the capacity to bring this suit. In the Uganda Oxygen Ltd case (supra) Justice Oder, JSC, quoting from Moir Vs Waller Steiner (1975)/ All ER 849, stated:-

> "– Derivative action is a suit by a shareholder to enforce a corporate cause of action. The corporation is a necessary party and the relief which is granted is a judgment against a third party in favour of the corporation. An action is derivative when action is based upon a primary right of the corporation but is asserted on its behalf by the shareholder because of the corporations failure, deliberately or otherwise, to act upon the primary right."

Annexture A to the plaint is the sale Agreement. The sellers are therein named as "Dr. Ocen Andrew, Judith Rose Odongo, Jane Ruth Oceng Ocero and Joel Odong Amen being shareholders of Rhino Communication Company Limited" It is stated therein that "the sellers are the true and registered shareholders of all the shares in Rhino Communications Company Limited and the said company is the holder of a Broadcasting licence ---" Further that "the

sellers are desirous of selling all their shares in the said Rhino Communication Company Ltd and in transferring/divesting all their interest in the said licence issued in respect of Rhino Communication Company Limited –" By the agreement it is stated in clause 1 thereof that " the sellers HERBY TRANSFER CONVOY and DIVEST ABSOLUTELY ALL their share interest in the company (including its back accounts, assets and the equipment annexed hereto as appendix A) and Licence herein before mention ."

The agreement upon which the plaintiffs' claim is founded was entered into by the plaintiffs and the defendants on the one part thereof as the sellers of their shares and interests in the company and its properties. In otherwards they were selling the company as a going concern. The plaintiffs' grievances against the defendants are with regard to their 40% share in the proceeds of the sale and the funds available on the company's accounts. The suit is essentially not based on the right of the company but on the plaintiffs' individual rights as holders of the shares.

The three essential elements to support a cause of action are that:-

(i) The plaintiff enjoyed a right
(ii) The right has been violated
(iii) The defendant is liable.

The law is that if any of the above essential elements is missing the plaint is a nullity and no amendment can be made as there is nothing to amend. Auto Garage & other Vs Motokov No 3) (1971) EA 515.

In the agreement, annexture A to the plaint, the plaintiffs and the defendants are selling their share in the company. In the pleading the plaintiffs contend that they are holders of 40% of the shares of the company and such have a 40% interest in the proceeds from the sale of the shares. The plaintiffs claim in paragraph 4(f) (g) and (h) is that the defendants on receipt of the sale proceeds have refused to hand over the 40% share of the sale proceeds belonging to the plaintiffs. Further it is claimed that the defendant's have thereby breached the trust the plaintiffs had placed on them.

The basis of the defendant's preliminary objection is that as shareholders of M/s Rhino Communications Company Ltd the plaintiffs did not have a cause of action, that the plaintiff should have been the company. The plaintiffs claim against the defendants is in respect of their entitlement to the proceeds from the sell of their respective shares. Having sold their respective shares in the company pursuant to the agreement, annexture A, both the plaintiffs and the defendant ceased to have any claim or interest in the company and /or its assets. However, they each had an interest and claim to the proceeds from the sale of the shares. The plaintiffs had a 40% right in the proceeds of the sale which they claim the defendants have violated by refusing to handover to them their share of the proceeds from the sell of the shares. A cause of action is thus disclosed by the plaintiffs, in their own right against the defendants.

The preliminary point of law is therefore overruled. Cost to be in the cause.
I so order.

Hon. Mr. Lameck N. Mukasa
Judge
1/12/2006