MULTIPLE DERIVATIVE CLAIMS AND POTENTIAL DEFENDANTS WITHIN THE FRAMEWORK OF UK LAW*

Birleşik Krallık Hukuku Çerçevesinde
Çoklu Türev Davalar ve Muhtemel Davalılar

Güray ÖZSU**

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ABSTRACT

Shareholders are not permitted by law to bring a claim on behalf of the company. Such an action can only be carried out by the company itself through its board of directors. However, in practice, there may be difficulties in bringing an action against wrongdoers on behalf of the company. When the wrongdoers are directors, and are therefore in a position to decide whether to bring an action on the company's behalf, the board of directors may avoid initiating proceedings against the wrongdoers.

This legal framework was considered by the courts to cause injustice, and therefore, over time, the right to bring a claim against wrongdoers on behalf of the company, known as a 'derivative claim,' was granted to shareholders. Subsequently, another type of derivative claim, called a 'multiple derivative claim,' was created by common law. Multiple derivative actions are brought in relation to corporate groups. These actions can be initiated by a member of a parent company on behalf of a direct or indirect subsidiary where the corporate group is under the control of the wrongdoer. Additionally, it aims to preserve the integrity of business administration by deterring directors from engaging in misconduct.

Key Words: Multiple derivative claims, parent company, board of directors, civil liability.

ÖZET

Dünyada genel olarak şirket paysahipleri, kanunen şirket adına dava açma yetkisine sahip değildir. Bu tür bir dava, yalnızca şirketin yönetim kurulu aracılığıyla

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** Dr., Rapporteur, Presidency of the Republic of Türkiye, e-posta: ozsuguray@gmail.com, ORCID ID:0000-0001-6842-6321

şirket tarafından açılabilmektedir. Ancak pratikte, şirket adına bu tip davaların açılmasında zorluklar yaşanabilmektedir. Şirket aleyhine olarak zarar doğurucu haksız fiilde bulunan kişiler yönetim kurulu üyeleri olduğunda ve bu nedenle aynı kişiler şirket adına dava açılıp açılmayacağına da karar verebilecek bir konumda olduklarında, yönetim kurulu söz konusu haksız fiilde bulunanlara karşı dava başlatmaktan kaçınabilmektedir.

Bu yasal çerçevenin adaletsizliğe yol açtığı değerlendirilmiş ve bu nedenle zamanla, 'türev dava' olarak bilinen, şirket aleyhine haksız fiilde bulunanlara karşı şirket adına dava açma hakkı paysahiplerine de verilmiştir. Ardından, teamül hukuku ile 'çoklu türev dava' adı verilen bir başka türev dava türü oluşturulmuştur. Çoklu türev davalar, şirket toplulukları ile ilgili olarak açılmaktadır. Bu davalar, şirket aleyhine haksız fiilde bulunanın kontrolündeki bir şirketler topluluğu söz konusu olduğunda, bir ana şirketin paysahibi tarafından, doğrudan ya da dolaylı bir bağlı ortaklık adına açılabilmektedir. Bu davalar, yöneticiler üzerinde caydırıcı etkiye sahip olup, işletme yönetiminin dürüstlüğünü korumayı da amaçlamaktadır.

Anahtar Kelimeler: Çoklu türev davalar, ana şirket, yönetim kurulu, hukuki sorumluluk.

INTRODUCTION

Under the general principles of company law accepted worldwide today, a company as a legal entity has a separate legal personality and thus can sue on its behalf to protect its rights, can claim damages and can be sued directly against it for its breaches.[1] In this respect, as a general rule, it is not allowed by the law to file a claim by shareholders on behalf of company. This legal action can only be taken by the company itself through the board of directors which is authorised to manage the company.[2] In other words, it is the company itself being able to claim damages arising from wrongdoings against the wrongdoers. However, in practice there might be some circumstances which include difficulties in bringing action against wrongdoers. For instance, where the wrongdoers are currently directors and are therefore also in a position to decide whether to bring an action on behalf of the company to claim compensation for wrongdoing or in other similar situations where relationships and interests are decisive, the board of directors might avoid lodging proceedings against wrongdoers on the company's behalf.[3]

This legal framework was considered to cause injustice by the courts and therefore over time, right to claim against wrongdoers on behalf of the company which

1 Alan Dignam and John Lowry, *Company Law* (11th edn, OUP Oxford 2020) 178

2 Andrew Keay, 'Assessing and rethinking the statutory scheme for derivative actions under the Companies Act 2006'(2016) Journal of Corporate Law Studies, 16 1, 39,39

3 ibid 39.

is called 'derivative claim' or 'derivative action' were granted to shareholders.[4] In other words, derivative actions can be regarded as a legal remedy granted to shareholders to recover the company's loss where the board of directors takes no step against wrongdoers. Also, this remedy grants shareholders power and authority to ensure integrity and lawfulness of the directors' conduct.

Subsequently, the other type of derivative claim named 'multiple derivative claim' is created by common law. It is also called 'common law derivative claims' and is brought in respect of corporate groups.[5] These claims can be brought by a member of parent company on behalf of direct or indirect subsidiary for director's breach of duty owed to direct or indirect subsidiary, where the corporate group is in wrongdoer's control.[6]

As discussed below multiple derivative claims can be brought against the directors of the subsidiary like ordinary derivative actions. It can also be brought against former directors and "de facto directors". Also most importantly, multiple derivative actions can be filed against "shadow directors". Shadow directors, apart from de jure directors, are those who can control the company's activities and therefore should be held liable for corporate actions in certain cases. Undoubtedly, the persons who can bring multiple derivative actions and the persons against whom multiple derivative actions can be brought depend on the applicable law. In other words, the applicable law should be determined and then examined to see the appropriateness of multiple derivative actions.

This essay critically discusses and tries to answer the research questions of whether in common law countries and especially in the UK, multiple derivative actions are allowed to be brought for the breach of duties towards the company by directors, and if so, whether shareholders can file a multiple derivative claims against shadow directors.

This article proceeds as follows:

Section 2 examines the general legal framework for derivative claims and in this context addresses the concept 'derivative claims' and the types of derivative claims. Section 3 deals with multiple derivative claims in corporate groups including the aim of these actions and looks for the answer of the question **'**against whom can multiple derivative actions be brought?' Section 4 examines the issue of applicable law in multiple derivative actions regarding transnational corporate groups, emphasizing the importance of choice of law in terms of availability of multiple derivative actions. Section 5 concisely summarizes the conclusions reached.

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4 ibid 40. See S. H. Goo, 'Multiple Derivative Action and Common Law Derivative Action Revisited: A Tale of Two Jurisdictions' (2010) Journal of Corporate Law Studies 10 1 255, 258

5 Dignam and Lowry (n 1) 186.

6 Keay (n 2) 47; Dignam and Lowry (n 1) 186.

A. General Framework for Derivative Claims

1. The Concept 'Derivative Claims'

It is generally accepted worldwide that under company law, a company has separate legal personality and thus can bring an action on its behalf to protect its rights and also can be sued directly against it for its wrongdoings.[7] In this respect, normally, it is not allowed by a company law to bring a claim by shareholders on behalf of the company. This could only be carried out by the company itself through the board of directors which is authorised to manage the company under the relevant law.[8] In other words it is the company itself being able to claim damages resulting from wrongdoings against the wrongdoers. This principle has been known as 'proper claimant rule' for a long time.[9] However, in practice there might be some obstacles to bringing an action against wrongdoers. Where the wrongdoers are directors and are therefore also in a position to decide whether to bring an action on behalf of the damaged company, or where the wrongdoers are at the same time controlling shareholders of the company, or where personal relationships and interests are decisive in this regard, the board of directors might choose not to initiate proceedings against the wrongdoers on the damaged company's behalf.[10]

This legal status was considered by the courts to produce injustice, and therefore, over time, the legal right to claim against wrongdoers on behalf of the company, called a 'derivative claim' or 'derivative action', was granted to shareholders in the UK and other common law countries.[11] This should not be confused with the shareholders' personal claims. When a shareholder's right, such as the payment of a dividend, is infringed by the board of directors, the shareholder can sue the wrongdoers directly, because in this case, the damage is suffered by the shareholder, not the company.[12]

It should also be noted that every loss incurred by a shareholder doesn't constitute shareholder loss. According to the 'no reflective loss' principle arising from *Prudential Assurance v Newman Industries*[13], decline in the value of shares or in dividends resulting from a loss incurred by the company arising from a wrongdoing is inseparable from the damage incurred by the company

7 Dignam and Lowry (n 1) 178.

8 Keay (n 2) 39.

9 Dignam and Lowry (n 1) 179.

10 Keay (n 2) 39.

11 Keay (n 2) 40.

12 Dignam and Lowry (n 1) 181.

13 *Prudential Assurance Co Ltd v Newman Industries Ltd (No 2)* [1982] Ch 204

and, therefore, is not recoverable by shareholders.[14] In such cases, one of the actions that shareholders can take is to bring a derivative action on the company's behalf against the wrongdoer, such as a director, for an act or omission involving negligence, breach of duty, or breach of trust by the directors. Any proceeds arising from the claim brought by the shareholder will belong to the company due to the 'proper claimant rule'.[15]

To sum up, derivative actions can be regarded as a legal remedy granted to shareholders to recover the company's loss, based on the possibility that the board of directors may take no action against wrongdoers. Also this remedy grants shareholders power and authority to ensure integrity and lawfulness of the directors' conduct. In other words, it has a deterrent function on the management, which can enforce the fiduciary duties of directors, penalize violations, and recover the company's losses.[16]

2. Types of Derivative Claims

Today, derivative claims are divided into two groups in terms of the source of claims as 'statutory derivative claims' and 'common law derivative claims'. Statutory derivative claims, as the name implies, are provided in statutes. For instance, in the UK, statutory derivative claims are provided between section 260 and 269 of Companies Act 2006.[17] In section 260 of Companies Act 2006 derivative claims are defined as proceedings initiated by a shareholder of the wronged company in respect of a cause of action vested in the company, seeking relief on behalf of the company. There is a similar provision in section 265 which applies to proceedings in Scotland.

The other type of derivative claim, known as a 'multiple derivative claim', is created by common law. These claims arise in relation to corporate groups and are also referred to as 'common law derivative claims'.[18] Multiple derivative claim is defined as a derivative claim that can be brought by a member of a

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14 See *Sevilleja (Respondent) v Marex Financial Ltd (Appellant)* [2020] UKSC 31 On appeal from [2018] EWCA Civ 146 [9]

15 Antony Corsi and Nicola Birney, 'Shareholder claims and the "no reflective loss" rule' (*Norton Rose Fulbright,* December 2018)<https://www.nortonrosefulbright.com/en-gb/knowledge/publications/0688bcea/shareholder-claims-and-the-no-reflective-loss-rule> accessed 9 September 2024.

16 John C. Coffee Jr. and Donald E. Schwartz, 'The Survival of the Derivative Suit: An Explanation and a Proposal for Legislative Reform' (1981) 81 Columbia Law Review 261, 302.

17 The concept 'derivative claim' was originally derived from common law principles. See Andrew Smith and Leontia McArdle, 'How do you obtain permission to bring a derivative action?' <https://www.dlapiper.com/en/uk/insights/publications/2020/02/saatchi-v-gajjar-and-another-2019-3472-ewhc-ch-and-derivative-actions/> accessed 9 September 2024.

18 Dignam and Lowry (n 1) 186.

parent company on behalf of the direct or the indirect subsidiary for a breach of duty owed to a direct or indirect subsidiary, where the corporate group is in wrongdoer's control.[19] According to *Universal Project v. Fort Gilkicker* decision, multiple derivative actions, like the 'ordinary derivative actions', are 'designed to serve the interests of justice in appropriate cases calling for the identification of an exception to the rule in *Foss v Harbottle'*[20] which establishes the general principle that the only person/entity having right to pursue a claim on behalf of a company is the company itself.[21] Briefly, in this decision, the Court ruled that even though there is not statutory provision in Companies Act 2006, multiple derivative actions are considered acceptable to protect the minority rights where the corporate group is under the control of wrongdoers. In *Abouraya v Sigmund* decision, the Court endorsed the *Universal Project v. Fort Gilkicker* decision in terms of reasoning and conclusions regarding multiple derivative actions.[22]

B. Multiple Derivative Claims in Corporate Groups

1. Aim and Scope

Multiple derivative action was created in common law and still exists, even though statutory provisions in Companies Act 2006 do not expressly include it. In *R (Rottman) v Commissioner of Police for the Metropolis* Case the Court held that '*it is a well-established principle that a rule of the common law is not extinguished by a statute unless the statute makes this clear by express provision or by clear implication*.'[23] In *Universal Project v. Fort Gilkicker* decision the Court states that *'the 2006 Act did not do away with the multiple derivative action. ... As a matter of language, section 260 applied Chapter 1 of Part 11 only to that part of the old common law device thus labelled, leaving other instances of its application unaffected*.'[24]

Multiple derivative actions aim to abolish the potential injustice and grant a remedy to shareholders of holding company where the wrongdoers are in control of the corporate group.[25] Also it aims to ensure the integrity of business

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19 *Universal Project Management Services Limited v. (1) Fort Gilkicker Limited (2) Mr Ian Pearce (3) Fort Gilkicker Properties Limited* [2013] EWHC 348 (Ch) para 26; Keay (n 2) 47; Dignam and Lowry (n 1) 186.

20 *Foss v Harbottle* (1843) 2 Hare 461; *Universal Project v. Fort Gilkicker,* para 26.

21 *Foss v Harbottle* (1843) 2 Hare 461

22 *Waleed Abouraya v. (1) Ms Anja Sigmund (2) Triangle Metals & Minerals Trading Limited (3) Triangle Metals & Minerals Limited* [2014] EWHC 277 (Ch) para 14.

23 *R (Rottman) v Commissioner of Police for the Metropolis* [2002] 2 AC 692 para 75

24 *Universal Project v. Fort Gilkicker,* para 44, 45.

25 *Universal Project v. Fort Gilkicker,* para 44; See Keay (n 2) 40

administration by deterring the directors from engaging in misconduct.[26] In our view, by granting permission to members of a holding company to pursue derivative claims, common law aims to prevent the abuse of controlling power in corporate groups and ensure the accountability of the board of directors.

As explained above, multiple derivative actions can be brought in relation to corporate groups. They can be initiated not only by a shareholder of a parent company on behalf of a subsidiary (known as a 'double derivative action'), but also by a shareholder of a parent company of the parent company of a subsidiary (known as a 'triple derivative suit').[27]

2. Potential Defendants in Multiple Derivative Actions

2.1. The Directors of Subsidiary

Multiple derivative actions can be brought against the directors of the subsidiary just like in the case of ordinary derivative actions. The conditions for derivative claim in common law are explained in *Prudential Assurance Co. Ltd v Newman Industries & ors,* stating that in order to be able to file a derivative claim, the claimant must demonstrate that (i) the company is entitled to the relief claimed, and (ii) the claim falls within an exception to the rule in *Foss v Harbottle*.[28] Also, in this decision, it was expressed that 'what has been done amounts to fraud, and the wrongdoers are themselves in control of the company. In this case, the rule is softened in favour of the aggrieved minority, allowing them to bring an action. The reason for this is that, if they were denied that right, their grievance could never reach the court because the wrongdoers, being in control, would not allow the company to sue'.[29] This explains the reasoning behind the conditions of derivative claims.

To make it clear, under common law, shareholders are entitled to bring a multiple derivative action under the conditions of fraud by directors and control by wrongdoers. In *Universal Project v. Fort Gilkicker* decision it is established that wrongdoer control can even arise where the aggrieved members and the wrongdoers are in 50/50 control, because even %50 control may prevent the company from suing, and also that '*fraud includes a variety of forms of equitable wrong, including breach of fiduciary duty, although not mere negligence*'.[30] Accordingly multiple derivative claims can be filed against the directors of subsidiary for their breaches.

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26 See Keay (n 2) 40

27 Dignam and Lowry (n 1) 186.

28 *Prudential Assurance Co. Ltd v Newman Industries & ors (No. 2)* [1982] Ch 204, 211 A-B

29 *Prudential Assurance Co. Ltd v Newman Industries & ors (No. 2)* [1982] Ch 204, 221H-222B

30 *Universal Project v. Fort Gilkicker,* para 18.

The term 'Director' is defined as '*any person occupying the position of a director, by whatever name called*' in section 250 of the Companies Act 2006. De facto director is a person who have not been officially appointed, but who nevertheless act as director.[31] Accordingly, the duties owed by a director of a company are also owed by a de facto director in the same way and both directors are legally responsible to the extent that a properly appointed director would be.[32] In other words, a de facto director will owe the same common law and statutory duties to the company, shareholders, and creditors, and, in the case of a multiple derivative action, to the shareholders of the holding company, as a de jure director does.[33]

In addition, multiple derivative actions should be able to be brought against former directors for their wrongs committed while they were directors, as well as for breaches of duties related to the post-directorship period, as specified by the law, such as those concerning conflicts of interest.[34]

2.2. Shadow Directors

a. General Remarks

'Shadow directors' can be defined as those who can issue instructions to the directors of a company and therefore have a significant influence over the company's affairs, even though they have not been appointed to the board of directors and are not official or de jure directors.[35] In other words, shadow directors, distinct from de jure directors, are those who have a decisive influence over the company and can control the company's activities, and therefore should be held liable for corporate actions in certain cases.[36] In the section 251 of Companies Act 2006 it is also defined as a person in line with whose directions or instructions the directors of the company are accustomed to act. A shadow director cannot directly carry out the duties of directors themselves; instead, they act behind the scenes.[37]

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31 Lee Roach, *Company Law* (1st edn, Oxford 2019) 174

32 CompaniesAct2006ExplanatoryNotes,para308<https://www.legislation.gov.uk/ukpga/2006/46/notes/division/5/30?view=plain> accessed 9 September 2024.

33 See Mark Ratcliff, 'D&O: de facto directors and policy implications' (Womble Bond Dickinson, 18 October 2019) <https://www.womblebonddickinson.com/uk/insights/articles-and-briefings/de-facto-directors> accessed 9 September 2024.

34 Dov Ohrenstein, 'Reflective Losses & Derivative Claims' (*Radcliffe Chambers*) <https://radcliffechambers.com/wp-content/uploads/2019/11/Reflective_Losses_and_Derivative_Claims-DO.pdf> accessed 9 September 2024; see Li Xiaoning, 'A comparative study of shareholders' derivative actions' (PhD Thesis, University of Groningen 2006) 78

35 Simon Witney 'Duties owed by shadow directors: closing in on the puppet masters?' (2016) Journal of Business Law 4 311,312 < http://eprints.lse.ac.uk/66225/> accessed 11 September 2024.

36 Roach (n 31) 175.

37 Institute of Directors, 'De facto directors and their liabilities' (*Institute of Directors,* 22August2019)<https://

In Section 251 of the Companies Act 2006, the term 'person' includes both individuals and legal entities, meaning that a company can also be regarded as a shadow director.[38] However, it also provides that a body corporate will not be regarded as a shadow director of its subsidiaries for the purposes of Chapter 2 (general duties of directors), Chapter 4, and Chapter 6. Therefore, in our view, under UK law, it seems unlikely that a parent company in a corporate group would be held liable as a shadow director for the wrongdoings committed against the subsidiary. Also, in our opinion, there is a conflict of interest in bringing a multiple derivative claim by a shareholder of a holding company against the holding company of which s/he is already a shareholder.

b. Dominant individuals in the Corporate Groups

In the structure of corporate groups, there might be some persons who can exercise decisive influence over subsidiaries' board of directors and can play dominant role in the management of the group of companies. These persons, as stated in the Companies Act 2006, are those whose directions or instructions the directors of the subsidiary and all group companies customarily follow. For instance, in family owned corporate groups, family members usually prefer to sit on the board of directors of holding company and control day to day operations of the group[39], but they may not be sitting on the board of subsidiaries. In practice, some families form informal 'Shareholder Councils' to represent the family in dealings with the boards. This establishes a connection between the shareholders and the board.[40] In these cases, even though family members, who are the dominant shareholders of the corporate group, are not directors of the subsidiary, they can still influence the subsidiary's board of directors and determine its course of action.

Since family members who are dominant shareholders in corporate groups do not carry out these duties themselves but act behind the scenes, these family members who are 'dominant individuals' in the parent company and the corporate group could be categorized and regarded as shadow directors.[41] Consequently, in our view, minority shareholders of a parent company can bring a multiple derivative claim against dominant individuals in a corporate group for the wrongdoings they commit against the subsidiary.

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www.iod.com/resources/factsheets/company-structure/de-facto-directors-and-their-liabilities-2/#:~:text=A%20shadow%20director%20is%20'a,seen%20as%20a%20shadow%20director> accessed 11 September 2024.

38 ibid

39 Lizzie Hill, 'The family holding company' (*Deloitte* 28 February 2018)<https://www2.deloitte.com/uk/en/blog/deloitte-private/2018/the-family-holding-company.html> accessed 11 September 2024.

40 ibid

41 See Ratcliff (n 33)

c. Parent Company's Directors and Chief Executive

Section 251(3) of the Companies Act 2006 provides that a holding company cannot be a shadow director by reason "only" that the directors are used to act in line with its directions or instructions for certain purposes. However, there is not any legal obstacle to hold the directors of a holding company liable as a shadow director.[42] If the directors of a parent company exercise decisive influence over the board of directors of a subsidiary, and the subsidiary's board perceives that they should follow the instructions of those directors, a minority shareholder of the parent company can bring a derivative action against the parent company's directors as shadow directors, as well as against the subsidiary's directors as de jure directors.

In *The Commissioners for Her Majesty's Revenue and Customs and another v. Holland*, the Court held that it is not necessary for a shadow director to be someone who 'lurks in the shadows'.[43] This decision also indirectly confirms that the directors of parent companies could be shadow directors. Moreover, it specifically establishes that the chief executive of a group of companies who directly gives instructions to the board of a subsidiary on which he does not sit could be a shadow director.[44]

d. Creditors as Shadow Director

The other group of persons who can be held liable as shadow directors are creditors, such as banks or other types of lenders. When a company faces financial difficulties, it may have to comply with the instructions of the bank it borrowed from, and therefore, the creditor bank may be considered a shadow director.[45] It is accepted that the liability of creditors as shadow directors arises in exceptional circumstances, particularly in the context of debt restructuring where creditors exercise decisive influence over the management of the subsidiary.[46]

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42 Claire Banks and Francesca Jus-Burke, 'Shadow Directors: What Are They and What Liability Do They Have?' (Greenwoods Legal, 23 February 2024) <https://www.greenwoods.co.uk/article/shadow-directors-what-are-they-and-what-liability-do-they-have/> accessed 11 September 2024.

43 *The Commissioners for Her Majesty's Revenue and Customs and another v. Holland,* [2010] UKSC 51 para 109.

44 ibid para 109.

45 CMS Law-Now, 'Shadow and de facto directors - a reminder of the risks' (CMS Law-Now, 22.01.2004) <https://www.cms-lawnow.com/ealerts/2004/01/shadow-and-de-facto-directors-a-reminder-of-therisks?cc_lang=en> accessed 11 September 2024.

46 Clifford Chance, 'Lender As A Shadow Director' (University of Oxford, 02 Jun 2017) <https://www.law.ox.ac.uk/business-law-blog/blog/2017/06/lender-shadow-director> accessed 11 September 2024.

However, where creditors do not get involved in the 'managing and executing of the business activities' of the debtor company, but instead monitor and demand compliance with the facility agreement in defense of their legitimate interests, they are not considered shadow directors.[47] There must be continuous and significant interference by the creditor in the decision-making process of the debtor company, such as controlling income and payments, for the creditor to be considered a shadow director with control over the debtor company.[48]. In such circumstances, the directors of the company are not able to exercise their own discretion.[49] Additionally, there must be a causal connection between the acts of the subsidiary's directors that cause damage to the company and the instructions of the creditor for the creditor to be held as a shadow director.[50]

Accordingly, a minority shareholder of a parent company in a corporate group can bring a derivative action against a bank or another creditor which is involved in decision-making process of debtor subsidiary or which controls and exercises decisive influence over the insolvent debtor subsidiary due to the loss and damages incurred by subsidiary these creditors cause.

C. The Matter of Applicable Law in Multiple Derivative Actions Concerning Transnational Corporate Groups

1. General Remarks Concerning Applicable Law in Derivative Actions

Today, since commercial transactions involve multiple jurisdictions and legal systems, this may create uncertainty regarding the applicable law in disputes. Such issues arising in transnational commercial transactions are addressed by applying conflict of laws rules, which function to refer a dispute to a specific national law.[51]

In the context of transnational corporate groups, where claimants and the defendant company are of different nationalities, the issue of conflict of laws inevitably arises in derivative actions. The issue of conflict of laws may arise in single derivative actions but becomes more significant in the case of international multiple derivative actions. If the applicable law does not allow the filing of multiple derivative actions, then shareholders cannot benefit from

47 ibid

48 ibid

49 *Buzzle Operations Pty Ltd (In Liquidation) v Apple Computer Australia Pty Ltd [2010] NSWSC 233*) para 247.

50 ibid, para 247.

51 A. N. Yiannopoulos, 'Conflict of Laws and Unification of Law by International Convention: The Experience of the Brussels Convention of 1924' (1961) Louisiana Law Review 21 3 553,553

this legal remedy as they would in wholly domestic disputes.[52] For instance, when a German minority shareholder in a German parent company brings a multiple derivative action against the directors of an English subsidiary in an English court, the issue of choice of law arises. In such a case, the court must first address the issue of applicable law to determine whether the shareholder of the parent company has the right to bring a multiple derivative action against the directors of the subsidiary.

2. The Choice of Law in Multiple Derivative Actions

The issue of choice of law and conflict of laws can frequently arise in the context of multiple derivative actions, just as it does in ordinary derivative actions. The choice of law in multiple derivative actions is crucial in determining whether the claimant has the right to bring such an action. In other words, the choice of law answers the question, 'Which state's law should apply to the rights of the claimant in multiple derivative actions?' and helps to determine whether the applicable law grants a shareholder of the parent company the right to bring a multiple derivative claim.[53] In short, choice of law is directly impactful and determinative to the success of the proceeding.

In English law, there is no precedent specifically addressing choice of law in the context of multiple derivative actions. However, in some common law precedents on choice of law, the law of the place of incorporation has been applied to derivative actions. This is because such disputes are regarded as 'internal affairs' between shareholders and the company, and therefore, it is considered that they should be governed by the law of the place of incorporation.[54]

On the other hand, when the parent and subsidiary are incorporated in two different jurisdictions, the choice of law in multiple derivative actions can be more complicated compared to ordinary derivative actions. In this respect, in common law countries, the laws most commonly chosen are the law of the place of incorporation of the subsidiary and the law of the place of incorporation of the parent company.[55] It is argued that, since the relationship between directors' duties and the law of the state of incorporation is closely connected, and most common law jurisdictions apply the law of incorporation for breaches of fiduciary duties, which is also the most common cause of action in derivative actions, the governing law in multiple derivative actions should be the law of the place of

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52 King Fung Tsang, 'International Multiple Derivative Actions' (2019) Vanderbilt Journal of Transnational Law 52 1 75, 77-78

53 ibid 86.

54 ibid 86-87; See Yaad Rotem, 'The Law Applicable to a Derivative Action on Behalf of a Foreign Corporation - Corporate Law in Conflict,' (2013) Cornell International Law Journal, 46 2 321, 326.

55 Tsang (n 52) 89.

incorporation of the subsidiary. However, some courts prefer to emphasize the rights of shareholders stemming from their ownership of the parent company's shares.[56] In multiple derivative actions brought before English courts so far, the issue of choice of law has not been raised. The court applied English law to these cases without addressing the choice of law question.[57]

In addition to the choice of law in multiple derivative actions, it is also important to determine whether multiple derivative actions are a matter of procedural law or substantive law, as procedural issues will be governed by the domestic law of the court handling the dispute.[58] English law views all aspects of rights concerning multiple derivative actions as procedural issues. Since, under English law, the availability and all related preconditions to initiate multiple or ordinary derivative actions are considered procedural issues, multiple derivative actions are essentially governed by the *lex fori*.[59] This interpretation will make multiple derivative actions available to all minority shareholders in England, even if the laws of the place of incorporation do not allow for such actions. On the other hand, in some jurisdictions, courts treat the availability of derivative actions and litigation conditions as substantive, while other requirements are considered procedural.[60] When aspects of multiple derivative actions are regarded as a substantive issue, the choice of law rules determine the applicable law. However, if they are considered procedural, the *lex fori* will govern the dispute.

Finally, in our view, considering that English law regards multiple derivative actions as a procedural issue, the applicable law for multiple derivative actions will be English law as *lex fori*. Therefore, common law rules and the Companies Act 2006 will be applied. In this respect, according to Section 260 of the Companies Act 2006, multiple derivative actions could be brought against dominant individuals in a transnational corporate group, a parent company's directors or chief executive, or creditors such as banks acting as shadow directors, in addition to the members of the board of directors as de jure directors.

CONCLUSION

Under the general principles of company law, a company has a separate legal personality and can therefore sue in its own name to protect its rights. In this respect, shareholders are not permitted by law to bring a claim on behalf of the company. Such an action can only be carried out by the company itself through its board of directors.

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56 ibid 92, 95.

57 *Abouraya v Sigmund*, Para 13.

58 Tsang (n 47) 103.

59 ibid 105.

60 ibid 105 ff.

However, in practice, there may be difficulties in bringing an action against wrongdoers on behalf of the company. When the wrongdoers are directors, and are therefore in a position to decide whether to bring an action on the company's behalf, the board of directors may avoid initiating proceedings against the wrongdoers.

This legal framework was considered by the courts to cause injustice, and therefore, over time, the right to bring a claim against wrongdoers on behalf of the company, known as a 'derivative claim,' was granted to shareholders. Subsequently, another type of derivative claim, called a 'multiple derivative claim,' was created by common law. Multiple derivative actions are brought in relation to corporate groups. These actions can be initiated by a member of a parent company on behalf of a direct or indirect subsidiary where the corporate group is under the control of the wrongdoer. Additionally, it aims to preserve the integrity of business administration by deterring directors from engaging in misconduct.

Multiple derivative claims can be brought against the directors of a subsidiary. A 'director' is defined as 'any person occupying the position of director, by whatever name called' in section 250 of the Companies Act 2006. A de facto director is a person who has not been validly appointed but nevertheless acts as a director. Accordingly, the duties owed by every person who is a director of a company are also owed by a de facto director in the same way and to the same extent as they are by a properly appointed director. In other words, a de facto director owes the same common law, fiduciary, and statutory duties to the company, its shareholders, creditors, and, in the case of a multiple derivative action, to the shareholders of the holding company, as a de jure director does.

In addition, a multiple derivative action should be able to be brought against former directors for wrongs committed during their time as directors and for breaches of obligations related to the post-directorship period, such as non-compete obligation.

This essay also concludes that shadow directors can be held liable in multiple derivative actions for breaches of duties owed to a subsidiary. Shadow directors are those who have a decisive influence over the company and can control the company's activities; therefore, they should be held liable for corporate actions in certain cases. Dominant individuals in a transnational corporate group, directors and the chief executive of the parent company, and creditors of the subsidiary may be subject to multiple derivative actions brought by minority shareholders of the parent company.

The choice of law in multiple derivative actions plays a key role in determining whether the claimant has the right to bring a derivative action. In other words, the choice of law answers the question, 'Which state's law should apply to the

claimant's rights in multiple derivative actions?' It helps establish whether the applicable law grants the shareholder of the parent company the right to bring a multiple derivative claim. It also matters to determine whether multiple derivative actions are a procedural law issue or a substantive law issue, as procedural issues will be governed by the domestic law of the court handling the dispute. Since English law views all aspects of rights concerning multiple derivative actions as procedural issues, and the availability and related preconditions for initiating such actions are also considered procedural matters, these actions are essentially governed by the *lex fori*.

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