2 The board of Mersey plc has authorised the allotment of shares to the public in contravention of the statutory pre-emption rights of Mersey's shareholders. What is the legal position as regards the allotment?

A It is invalid and the allottees have no right to compensation.
B It is valid and the shareholders can ask for compensation from the directors and the company.
C It is invalid and the allottees can ask for compensation from the directors and the company.
D It is valid and the original shareholders have no right to compensation.

3 The shareholders of Test Ltd are Ann who holds 600 shares, Barbara who has 100 shares, and Clare and Diana who have 250 shares each. The shares carry one vote each. A resolution to exclude the statutory pre-emption right of the shareholders of Test Ltd, given that all members attend the meeting and that voting is by poll, requires the minimum support of:

A Ann alone.
B Ann and Barbara.
C Ann and Barbara and Clare.
D Ann and Barbara and Clare and Diana.

4 Under the provisions of the Companies Act 2006, where there is to be an allotment of unissued share capital for cash the notice of the offer to existing shareholders must remain open for not less than:

A 28 days **B** 21 days **C** 15 days **D** 14 days

5 Which of the following resolutions requires the directors of a private company to give a statutory declaration of solvency? A resolution to:

A Commence a creditors' voluntary winding-up.
B Reduce the company's share capital.
C Approve the giving of financial assistance for the purchase of its own shares from distributable profits.
D Approve a contract for the purchase of its own shares out of distributable profits.

6 What is the minimum percentage of shareholders required to make an application to the court to set aside an alteration of the objects clause of a company?

A Not less than 15 per cent of the total number of shareholders.
B Those holding not less than 15 per cent in nominal value of the issued share capital of the company or any class thereof.
C Not less than 15 per cent of the total number of shareholders or any class thereof.
D Those holding not less than 15 per cent in nominal value of the issued share capital of the company.

The answers to test your knowledge questions appear on p. 616.

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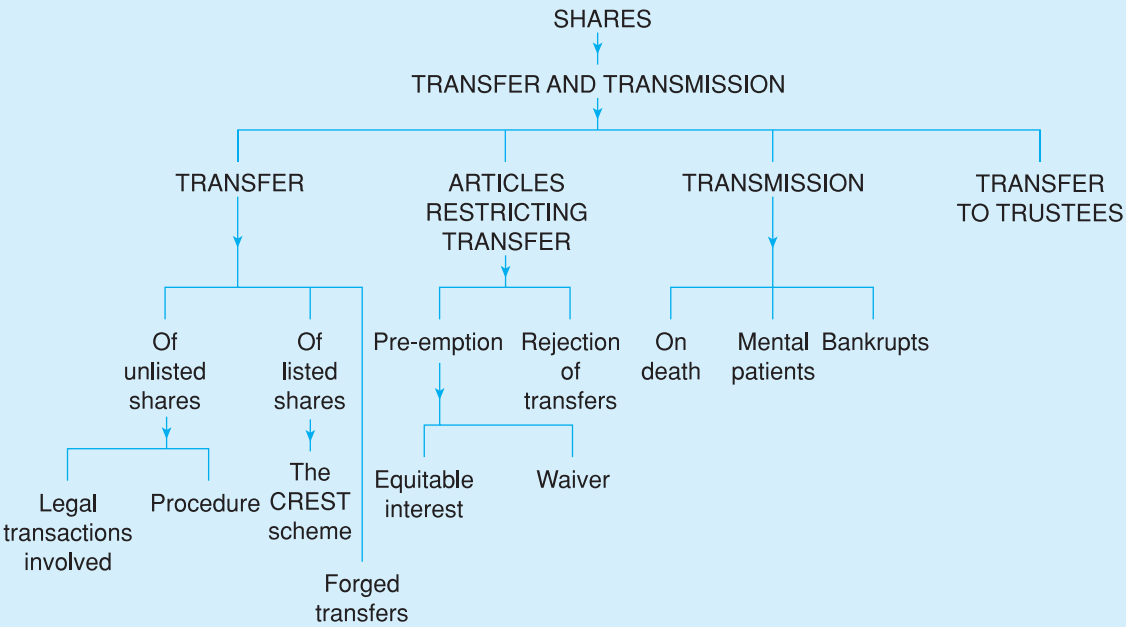
12 Shares – transfer and transmission



This chapter is concerned with the way in which shares are transferred from one person to another. It is necessary to distinguish between the transfer of unlisted shares and shares which are listed on an investment exchange such as the Stock Exchange. Basically the material in this chapter covers the transfer of shares in a private company which cannot have a listing on an investment exchange. The rules, however, could apply to a plc which had not sought a listing on an investment exchange.

Transfer of unlisted shares

As we have seen, shares are personal property and are transferable subject to any restriction contained in the articles. A company cannot register a transfer of shares or debentures unless a proper instrument of transfer, duly stamped, has been delivered to the company and executed by or on behalf of the transferor (CA 2006, s 770). No formal transfer is required when a company purchases its own shares, though stamp duty is payable. Thus an article which provided for the automatic transfer of shares to a director's widow on his death was held invalid (***Re Greene*** [1949] 1 All ER 167). The directors usually have power under articles such as *Table A* to decline to register the transfer of a share, other than a fully paid share, to a person of whom they do not approve, e.g. a minor or person of unsound mind who cannot be bound by the contract; and also to decline to register the transfer of a share on which the company has a lien, e.g. for calls made but not paid. Any power of veto on transfer vested by the articles in the directors must be exercised within two months after the lodging of the transfer for registration and the transferee notified. If not, the company may be compelled to register the transferee as a member.

Re Swaledale Cleaners [1968] 3 All ER 619

On 3 August 1967 the shareholding of the company was: H (deceased) 5,000; S 4,000; A (deceased) 500; L 500. S and L were directors of the company which was a private one. The company's articles provided that the quorum of directors should be two although a sole continuing director had power to appoint an additional director. At a combined board meeting and annual general meeting held on 3 August 1967, L retired by rotation and was not re-elected a director. The personal representatives of H and A had executed transfers of H and A shareholdings in favour of L, but S as director refused to register them purporting to exercise a power of refusal contained in the articles. There was no resolution either of the board or of the shareholders on the matter of refusal to register the transfers. On 11 December 1967 L began proceedings for rectification of the register, and on 18 December 1967 S appointed an additional director and the two directors formally refused to register the transfers.

Held – by the Court of Appeal – the register must be rectified to show L as the holder of the shares of H and A. The power to refuse a transfer must be construed strictly because a shareholder ordinarily has a right to transfer his shares. Furthermore, the delay in exercising the power of refusal, i.e. four months, had been unreasonable and the power was no longer capable of being exercised.

Comment

The above case was followed by the High Court in *Re Inverdeck Ltd* [1998] 2 BCLC 242. This later case stresses the need for directors in private companies as Inverdeck Ltd was to observe the

relevant corporate formalities in their day-to-day transactions. The power in private companies to refuse to register a transfer is a valuable one in that it can be used to prevent persons from acquiring rights in the company which the directors believe are contrary to its interests. Failure to observe formalities can lead to this valuable power being lost.

Court's power to rectify the register where no instrument of transfer

It was held by the Court of Appeal in ***Re Hoicrest Ltd*** [1999] 2 BCLC 346 that the power of the court to rectify the membership register of a company could be used to effect a transfer where there was no instrument of transfer so that the company had not had an opportunity to refuse the transfer. Although CA 2006, s 125 has traditionally been used in disputes between a would-be shareholder and the company where following transfer the company refuses registration, the section was not confined to that situation and could be used to settle a dispute as to the ownership of shares between two members.

The legal transactions involved

The purchase and sale of shares involves the following separate and distinct legal transactions:

(a) An unconditional contract is agreed between the transferor and transferee. The transferor then holds the shares as a trustee for the transferee (who has an equitable interest) until registration but is still a member of the company and retains the right to vote as he chooses.
(b) The transferee pays for the shares. The position remains as in (a) above except that the transferor must now vote as the transferee directs. An unpaid transferor has the right to vote the shares free from any obligation to comply with the transferee's requirements (***JRRT (Investments)*** **v** ***Haycraft*** [1993] BCLC 401).
(c) The position remains as in (b) above while the transfer is approved by the directors and the transfer is stamped.
(d) The transferee's name is entered on the register of members. At this stage the transferor ceases to be a member of the company. The transferee becomes the member and acquires the legal title to the shares. Since membership and membership rights are only effective when the transferee is on the register of members, it may be necessary to ask the court to rectify the register of members under CA 2006, s 125 where the company is refusing to register the transferee, *but only if this is contrary to the powers of the board*.

The rights of persons to obtain registration or to claim under an equitable title are set out in Chapter 13 See p. 259. Section 127 of the Insolvency Act 1986 declares void any transfer of shares after the commencement of winding-up by the court, unless the court otherwise orders.

Form of transfer

Schedule 1 of the Stock Transfer Act 1963 introduced a new transfer form – a *stock transfer form*, which is for general use with unlisted shares.

Registrars are required to accept for registration transfers in the form introduced by the Act because it overrides any contrary provision regarding transfer, whether statutory or not. Thus, the 1963 Act overrides any other provisions relating to the *form* of transfer in the

company's articles. The signature of the transferor need not be witnessed, and the transferee need not sign the transfer, nor need it be in the form of a deed.

It should be noted that the 1963 Act does not override provisions in the articles relating to the rights of the directors to refuse registration.

The stock transfer form is not available to transfer partly paid shares or shares in an unlimited or guarantee company. If such companies are encountered, reference should be made to the articles for the form of transfer to be used.

Procedure on transfer of unlisted shares

The method of transferring fully paid shares or stock is as follows.

The shareholder executes (signs) a stock transfer form in favour of the purchaser, and hands it to the purchaser or his agent, together with the share certificate. The purchaser, or his agent, sends the stock transfer form along with the certificate to the company for registration. The purchaser need not sign the stock transfer form, nor need it be in the form of a deed. The company secretary, following approval by the board, deletes the transferor's name from the register of shareholders and replaces it with the transferee's name and, within two months, sends the share certificate to the transferee.

Transfer of listed shares

Transfers of shares with a listing on the London Stock Exchange are covered by the Uncertificated Securities Regulations 2001 (SI 2001/3755). This area of the law is rather specialised and only an outline of the system called CREST is given here.

The regulations provide for the system to be run by an approved operator which is CRESTCo Ltd, a private company owned by a number of firms connected with all sectors of the equities market. CRESTCo merged with Euroclear Bank in September 2002.

The system, which is known as CREST, is an electronic system which allows shareholders to hold and transfer their securities in dematerialised form, i.e. without a share certificate. A statement not unlike a bank statement reveals purchases and sales by the intermediaries concerned.

CREST does not impose dematerialisation of shares on shareholders. Shareholders who wish to become or remain uncertificated are able to do so. Institutional shareholders, such as insurance companies, that are frequent traders will go for dematerialisation but less sophisticated shareholders will in many cases opt for the paper certificate regime, follow the method of transfer described above and be on a separate register of members.

Uncertificated shareholders will appoint a custodian broker to hold the shares. The broker will appear on the electronic register of members but can only deal with shares in accordance with the customer agreement between the shareholder and the custodian broker. Shareholders who wish to retain paper certificates in listed companies may be forced to appoint custodian brokers as nominees because of the Stock Exchange three-day rolling settlement system under which an entire share transfer transaction must be completed in three days. This is difficult to achieve under a paper certificate regime but easy under an electronic transfer regime. It is possible to opt for a ten-day settlement regime though it will be necessary to find a stockbroker who operates it – some do.

Once a nominee is installed, the shareholder will receive dividends and benefit from capital growth but rights will be lost such as the right actually to attend meetings unless the nominee can make arrangements for this, nor will the shareholder receive the annual report and accounts unless the nominee asks for enough to send out to all his members, but this would be a concession not a right.

The regulations make dematerialisation lawful and disapply CA 2006, s 769 under which a share certificate must be provided to the transferee within two months after allotment or transfer where the uncertificated regime applies, but not in the paper certificate regime. Companies that wish to allow their shares to be transferred via CREST will have to change their articles to add a relevant provision.

Finally, a company any of whose securities can be transferred through CREST must subdivide its register of members (or debenture holders) to show how many of those securities each person holds in uncertificated form and certificated form respectively. An issuer of securities can only rectify a register of securities in relation to uncertificated units with the consent of CRESTCo or by order of the court.

Certification of transfers: unlisted shares

The above procedure assumes that on completion of the sale of registered unlisted shares the seller delivers his share certificate to the purchaser together with the instrument of transfer. Where he is selling all the shares represented by the certificate the seller will do this, but if he is selling only part of his holding, or the whole of his holding but to more than one person, he will instead send the share certificate and the executed transfer of the shares which the purchaser is buying to the company so that the transfer may be certificated.

The company secretary or registrar or transfer agent will compare the share certificate and the transfer with the register of members and if it appears that the seller is the owner of the shares mentioned in the certificate and some of those shares are comprised in the transfer, the secretary, registrar, or agent, as the case may be, will write in the margin of the transfer a note that the share certificate has been lodged and will sign it on behalf of the company.

The certificated transfer is then returned to the seller, the share certificate being retained by the company or the transfer agents. The seller will complete the sale by delivering the certificated transfer to the purchaser who will accept it as equal to delivery of an uncertificated transfer accompanied by the share certificate. The purchaser will then lodge the transfer with the company or its transfer agents for registration and the company will issue a new share certificate to him for the shares he has bought and a new certificate showing the seller as the registered holder of the balance of the shares which he retains if he retains any. Obviously, the seller will not get a new certificate where he has sold his whole holding but to more than one person.

Liability arising out of certification

This is covered by CA 2006, s 775 and although a certification is not a warranty by the company that the person transferring the shares has any title to them, it is a representation by the company that documents have been produced to it which show prima facie title in the transferor.

Where, therefore, the company or its agent fraudulently or negligently makes a false certification, a purchaser who acts upon the false certification may sue the company for any loss he may have incurred as a result.

For example, if the company certifies a transfer without production of a certificate, it may be that the certificate has been used to make an uncertificated transfer to another purchaser. If so, two purchasers now exist and both are eligible for entry on the register of members. If the later purchaser achieves registration first, he will establish priority over the certificated transferee who will not then be registered and the company will be liable in damages to the certificated transferee for the loss he suffers thereby. However, if the company registers the certificated transferee and refuses the other purchaser, it will not be liable to the latter because the share certificate does not operate as an estoppel except as on the date of issue, which will have been some time ago.

Forged transfers

If a company transfers shares under a forged instrument of transfer, the transferor whose name has been forged must be restored to the register, and in so far as this puts the company to expense or loss, it can claim an indemnity from the person presenting the transfer for registration, even though he is quite innocent of the forgery.

Sheffield Corporation* v *Barclay [1905] AC 392

Two persons, Timbrell and Honnywill, were joint owners of corporation stock. Timbrell, in fraud of Honnywill, forged a transfer of the stock and borrowed money from the respondents on the security of the stock. The respondents sent the transfer to the corporation asking for registration, and they were duly registered. Later the respondents sold the shares and the corporation issued certificates to the purchasers who were also registered. Honnywill, after the death of Timbrell, discovered the forgery, and the corporation replaced the stock which was the best course open to them, because if they had taken the ultimate purchasers off the register of stockholders, they would have had to pay damages to them by virtue of the doctrine of estoppel. The corporation now sued the respondents for an indemnity on the grounds that they had presented the forged transfer.

Held – by the House of Lords – the corporation succeeded. The person presenting a transfer warrants that it is good, and the fact that he is innocent of any fraud does not affect this warranty. The corporation, therefore, was entitled to recover from the respondents the value of the stock replaced, leaving them to such remedies as they might have against Timbrell's estate.

Comment

(i) Where a person requests the registration of a share transfer which a company is under a duty to effect there is implied in that request a warranty that the transfer is genuine. The rule applies whether the transfer is in favour of the person presenting it or someone else, as where a broker presents a transfer on behalf of a client.

(ii) The company's loss, for which it needs an indemnity, will normally consist in buying in or issuing for no consideration new shares to recompense the original holder. The innocent transferee will stay on the register of members by reason of the rules relating to estoppel that are described above. The indemnity may be made by the fraudster if he presents the transfer but it may be presented by a broker on behalf of the fraudster where the company is listed. In these circumstances the broker must give the indemnity, even though he may be innocent of the fraud, leaving him to claim against the fraudster. This was the situation in the ***Barclay*** case and in ***Royal Bank of Scotland plc* v *Sandstone Properties Ltd*** (1998) *The Times*, 12 March, where the facts were similar and the *Barclay* case was followed.

If the company issues a share certificate to the transferee under a forged transfer, the company is not estopped from denying his title to the shares, but it may become estopped if it issues a new certificate to a non-owner as part of a subsequent transfer transaction.

A company may inform the transferor that a transfer has been received for registration so as to give him a chance to prevent a fraudulent transfer but a transferor is not prejudiced by the fact that he has received notice, and may still deny the validity of the transfer.

Death of a holder in a joint account

A transfer is not needed to a surviving joint holder or holders on the death of one. In such cases, it is usual for the company to receive a death certificate certified by the Registrar of Births and Deaths. Photocopies are not official documents but some companies will accept them if presented by a person of professional standing. Sometimes a grant of probate or administration may be received and this is satisfactory evidence of death. The necessary alterations in the register of members are made on the basis of these documents and not on the basis of the conventional instrument of transfer. The procedure is a form of transmission of shares which is considered later in this chapter.

Companies whose articles restrict transfer

In the case of a company whose articles restrict transfer a transfer must be submitted to and approved by the board and any restriction must be the decision of the directors.

Re Smith* v *Fawcett [1942] Ch 304 (Court of Appeal)

Article 10 of the articles of association of a private company provided: 'The directors may at any time in their absolute and uncontrolled discretion refuse to register any transfer of shares, and cl. 19 of *Table A* shall be modified accordingly.' The issued capital of the company consisted of 8002 ordinary shares of which the two directors of the company, J F and N S, held 4001 each. J F died, and his son as his executor applied to have the testator's shares registered in his name. N S refused to consent to the registration, but offered to register 2,001 shares and to buy 2,000 at a fixed price. The executor applied to the court by way of motion that the register of members of the company might be rectified by inserting his name as the holder of the 4,001 shares. Lord Greene MR observed:

> The principles to be applied in cases where the articles of a company confer a discretion on directors with regard to the acceptance of transfers of shares are, for the present purposes, free from doubt. They must exercise their discretion bona fide in what they consider – not what a court may consider – is in the interests of the company, and not for any collateral purpose. They must have regard to those considerations, and those considerations only, which the articles on their true construction permit them to take into consideration, and in construing the relevant provisions in the articles it is to be borne in mind that one of the normal rights of a shareholder is the right to deal freely with his property and to transfer it to whomsoever he pleases. When it is said, as it has been said more than once, that regard must be had to this last consideration, it means, I apprehend, nothing more than that the shareholder has such a prima facie right, and that right is not to be cut down by uncertain language or doubtful implications. The right, if it is to be cut down, must be cut down with satisfactory clarity. It certainly does not mean that articles, if appropriately framed, cannot be allowed to cut down the

right of transfer to any extent which the articles on their true construction permit. Another consideration which must be borne in mind is that this type of article is one which is for the most part confined to private companies. Private companies are in law separate entities just as much as are public companies, but from the business and personal point of view they are much more analogous to partnerships than to public corporations. Accordingly, it is to be expected that in the articles of such a company the control of the directors over the membership may be very strict indeed. There are, or may be, very good business reasons why those who bring such companies into existence should give them a constitution which confers on the directors powers of the widest description.

The language of the article in the present case does not point out any particular matter as being the only matter to which the directors are to pay attention in deciding whether or not they will allow the transfer to be registered. The article does not, for instance, say, as is to be found in some articles, that they may refuse to register any transfer of shares to a person not already a member of the company or to a transferee of whom they do not approve. Where articles are framed with some such limitation on the discretionary power of refusal as I have mentioned in those two examples, it follows on plain principle that if the directors go outside the matters which the articles say are to be the matters and the only matters to which they are to have regard, the directors will have exceeded their powers.

Mr Spens, in his argument for the plaintiff, maintained that whatever language was used in the articles, the power of the directors to refuse to register a transfer must always be limited to matters personal to the transferee and that there can be no personal objection to the plaintiff becoming a member of the company because the directors are prepared to accept him as the holder of 2,000 of the shares which have come to him as legal personal representative of his father. Mr Spens relies for his proposition on observations in several authorities, but on examination of those cases it becomes clear that the form of article then before the court by its express language confined the directors to the consideration of the desirability of admitting the proposed transferee to membership on grounds personal to him . . .

There is nothing, in my opinion, in principle or in authority to make it impossible to draft such a wide and comprehensive power to directors to refuse to transfer as to enable them to take into account any matter which they conceive to be in the interests of the company, and thereby to admit or not to admit a particular person and to allow or not to allow a particular transfer for reasons not personal to the transferee but bearing on the general interests of the company as a whole – such matters, for instance, as whether by their passing a particular transfer the transferee would obtain too great a weight in the councils of the company or might even perhaps obtain control. The question, therefore, simply is whether on the true construction of the particular article the directors are limited by anything except their bona fide view as to the interests of the company. In the present case the article is drafted in the widest possible terms, and I decline to write into that clear language any limitation other than a limitation, which is implicit by law, that a fiduciary power of this kind must be exercised bona fide in the interests of the company. Subject to that qualification, an article in this form appears to me to give the directors what it says, namely, an absolute and uncontrolled discretion.

Held – affirming Simonds J – that Article 10 gave the directors the widest powers to refuse to register a transfer, and that, while such powers are of a fiduciary nature and must be exercised in the interests of the company, there was nothing to show that they had been otherwise exercised.

In practice these restrictions are normally found only in the articles of private companies. Most plcs have their shares listed, or quoted, on a recognised investment exchange such as the Stock Exchange, and the rules of the listing or quotation agreement do not permit restrictions on transfer following sale. Consideration will be given to the right of pre-emption in private companies and the general rules relating to rejection of transfers.

The right of pre-emption: generally

This means that when a member of a private company wishes to sell his shares, he must, under a provision in the articles, first offer them to other members of the company before he

offers them to an outsider. The price is usually to be calculated by some method laid down in the articles, e.g. at a price fixed by the auditors of the company. In this context it should be noted that the auditor can be sued by the seller of the shares if the valuation is lower than it should be because of the auditor's negligence. This is an important claim because the seller will not normally be able to avoid the contract of sale because that contract usually makes the auditor's valuation final and binding on the parties.

However, a distinction must be made where the accountant or valuer has not merely made a mistake in the valuation of the shares, but has not done what he was appointed to do. In such a case the court can intervene and set the contract of purchase aside. Thus, in ***Macro* v *Thompson*** [1997] 2 BCLC 626 an accountant/valuer was asked to value the shares in two private companies for the purpose of a pre-emption purchase. In reaching conclusions as to the valuation of company A's shares, he mistakenly transposed the assets of company B, which was less valuable. This transposition appeared in the judgment of an earlier decision of the court in these proceedings. The contract to buy the shares of company A at the lower price was set aside by the court even though the purchaser had paid for the shares. The accountant/valuer had been asked to value the shares of company A but by mistake had valued the shares of company B, which represented not merely an error in the valuation, but an error in terms of his instructions.

If the other members do not wish to take up the shares, the shares may then be sold to an outsider. The other members must apparently be prepared to take *all* the shares that the vendor member is offering (***Ocean Coal Co Ltd* v *Powell Duffryn Steam Coal Co Ltd*** [1932] 1 Ch 654).

The right of pre-emption can, if appropriately worded, be enforced as between the members (***Rayfield* v *Hands*** [1960] Ch 1), and also by the company, which may obtain an injunction against a member who is not complying with the articles in this matter (***Lyle & Scott Ltd* v *Scott's Trustees*** [1959] 2 All ER 661). The decision in ***Lyle & Scott Ltd*** could make it very difficult for a takeover bidder to take over a private company because if there is a pre-emption clause the board can ask the court for an injunction requiring a member to offer his shares to another member rather than to the bidder.

Effect of transfer of equitable interest in shares

A method of effectively transferring control over the shares without triggering a pre-emption clause can be seen in the following case.

Scotto* v *Petch (2001) *The Times*, 8 February

The company owned Sedgefield racecourse, and an offer to buy all the shares in the company was made by Northern Racing Ltd. Mrs Scotto, a 21 per cent shareholder, refused to sell. The other shareholders were willing to do so. The victim company had a pre-emption clause in its articles under which pre-emption rights in other shareholders were triggered if a shareholder 'intends to transfer shares'. The shareholders other than Mrs Scotto made an agreement under which they would remain on the register as legal owners of their shares but the equitable interest would belong to Northern Racing. The agreement went on to say that if they were ever required to transfer the legal interest, it would be to another member, i.e. it would be a permitted transfer under the article. The arrangement gave Northern Racing effective control since under the agreement the shareholders, who were parties to it, would obviously vote as Northern Racing required. Mrs Scotto said that the arrangement triggered the pre-emption clause so that the shares had to be offered to her.

Held – by the Court of Appeal – the pre-emption clause was not triggered. There had been no transfer of the legal interest in the shares and if ever there was, it would be to other members and would, therefore, be a permitted transfer under the articles.

Pre-emption: members' waivers

The other members of the company may be prepared to give written waivers of their rights to pre-emption, bearing in mind that a private company will normally have articles giving the directors power to reject a transferee. However, where shares are transferred in breach of a pre-emption clause without unanimous waiver of the other members, the directors have no power to register the transfer and no question of discretion arises. A person wishing to sell his shares in a private company with a pre-emption clause will normally notify the company secretary, who will advise the other members of the wish to sell.

Rejection of transfers

Where the articles give the directors power simply to refuse or approve the registration of transfers, that power must be exercised in good faith, and this may be tested in the courts if it appears that the directors have rejected a transfer for purely personal reasons as where they simply do not like the proposed transferee (and see ***Re Accidental Death Insurance Co, Allin's Case***, 1873, below); but where the power to reject is exercisable for reasons specified in the articles, the transferee need not be told which is the reason for this rejection if the articles so provide (see ***Berry and Stewart* v *Tottenham Hotspur FC***, 1935, below). The position is the same where the articles merely provide that the directors may reject a transfer 'without assigning reasons therefor'. These provisions are much stronger because the directors cannot be required to give reasons and therefore it is difficult, if not impossible, to prove before a court that they acted in bad faith.

Re Accidental Death Insurance Co, Allin's Case (1873) LR 16 Eq 449

The company's deed of settlement provided that when a shareholder wished to transfer his shares, he should leave notice at the company's office, and the directors should consider the proposal and signify their acceptance or rejection of the proposed transferee. If they rejected the proposed transferee, the proposed transfer would still be considered approved unless the directors could find someone else to take the shares at market price. The company arranged to transfer its business to the Accident and Marine Insurance Corporation Ltd. The shareholders acquiesced in an arrangement to exchange their shares for shares in the corporation, but the company was not wound up. A year later, the former directors of the company reversed the procedure, and the company proposed to resume its former business. Notice of this was given to shareholders, and shortly afterwards the corporation was wound up. Under an arrangement to release certain shareholders of liability, Allin transferred 200 shares in the company to Robert Pocock for a nominal consideration. He gave notice to the directors at a meeting at which he was present, and the transfer was agreed. Later the company was wound up.

Held – by the High Court – the transfer was invalid, and Allin must be a contributory. The clauses were not intended to be in operation for the purpose of enabling individuals to escape liability when the company had ceased to be a going concern.

Berry and Stewart* v *Tottenham Hotspur FC Ltd [1935] Ch 718

Berry held one ordinary share in Tottenham Hotspur and he transferred his share to Stewart, both of them subsequently trying to register the transfer. Registration was refused, and Art 16 of the company's articles specified four grounds on which this was allowable, and also stipulated that the directors were not bound to divulge the grounds upon which registration was declined. The claimants brought an action for a declaration that the company was not entitled to decline to register the transfer, and sought interrogatories directed to find out which of the four grounds was the basis of the refusal.

Held – by Crossman J – Article 16 excused the directors from the need to disclose this information, and this was binding not only on Berry, as a member, but also on Stewart who was applying to be a member. An action coupled with a demand for interrogatories could not be used to oust the agreement.

Comment

A more recent example of the use of this much stronger power of rejection is to be found in ***Popely* v *Planarrive Ltd*** [1997] 1 BCLC 8. Article 14 of the articles of association of Planarrive Ltd (P Ltd), a private company, gave its directors the power 'in their absolute discretion and without assigning any reason therefor' to 'decline to register the transfer of a share'. If the directors took such an action, they were required, under Art 25, to notify the transferee of their refusal to register his interest within two months after the date on which the transfer was lodged. Darren Popely validly transferred 15 shares in P Ltd to his father Ronald. The directors of P Ltd exercised their powers under Art 14 and refused to register the transfer. Ronald Popely then applied to the Chancery Division under s 359 of the Companies Act 1985 for an order rectifying the register of members of P Ltd by registering him as the owner of the shares transferred by his son. It was not disputed that notice of the refusal to register had not been sent to Mr Popely within the time set out in Art 25. Counsel for Mr Popely attempted to argue that this breach made the whole decision void. Mr Justice Laddie said that it did not nullify the decision although it might expose the directors to some civil or criminal liability (see s 183(6)). With regard to the actual refusal to register the transfer, Mr Popely's counsel said that this refusal was based on the strong feelings of hostility felt by the directors towards his client. However, the judge said that such feelings did not render the decision invalid. Where directors have such wide powers as these in the articles, the only restriction placed on them was that they must act bona fide in the best interests of the company and not outside their powers. Mr Popely was refused his application.

When is a transfer rejected?

Where there is an equality of votes, a transfer cannot be deemed rejected, but must be accepted (see ***Re Hackney Pavilion Ltd***, 1924, below), though it is usual for the chairman to have a casting vote which he can use to decide the issue. Similarly, a transferee can ask the court to rectify the register so that his name is included on it where one director, by refusing to attend board meetings, is preventing a directors' meeting from being held to consider the registration because of lack of quorum (***Re Copal Varnish Co***, 1917). In addition, the powers vested in directors to refuse to register a transfer must be exercised within a reasonable time (see ***Re Swaledale Cleaners***, 1968).

Re Hackney Pavilion Ltd [1924] 1 Ch 276

The company had three directors, Sunshine, Kramer and Rose, each of whom held 3,333 shares in the company. Sunshine died, having appointed his widow as his executrix. Her solicitors wrote to the company, enclosing a transfer of the 3,333 shares from herself as executrix to herself in an individual capacity. At a board meeting at which Kramer, Rose and the secretary were present, Rose proposed that the shares be registered, but Kramer objected in accordance with a provision in the articles. There was no casting vote. The secretary then wrote to the solicitors informing them that his directors had declined to register the transfer.

Held – by the High Court – the board's right to decline required to be actively expressed. The mere failure to pass the proposed resolution for registration was not a formal active exercise of the right to decline. The right to registration remained, and the register must be rectified.

Unless the articles otherwise provide, rights of pre-emption and rejection apply only on a transfer by a member, and do not arise on transmission through death or bankruptcy. Neither do they arise where the shares are still represented by a renounceable letter of allotment.

Re Pool Shipping Ltd [1920] 1 Ch 251

The applicants were shareholders of the company which had capitalised £125,000, part of a reserve fund, for distribution among the registered shareholders or their nominees, at the rate of one share for every four shares issued. All but one of the shareholders renounced their right to allotments, and requested the company to allot the shares to Coulson who had agreed to accept them. The managers refused to issue the shares or register them to him when he presented the letters of renunciation in his favour, so the applicants moved for rectification of the register by the insertion of Coulson's name. The company had no directors but was controlled by Sir R Ropner & Co Ltd, who were described as managers and who relied on various clauses in the articles as grounds for refusal.

Held – by the High Court – letters of renunciation do not amount to transfers of shares so as to come within the provisions of the articles of association dealing with the transfer of shares already registered. The managers were wrong in thinking they could refuse to register Mr Coulson, and the register must be rectified.

Special articles may allow rejection of executors' transfers to themselves as members pending the winding-up of the estate as an alternative to dealing with them in a representative capacity, and where this is so, they will *not* be able to vote the deceased's shares. A trustee in bankruptcy in the same situation will at least be able to direct his living debtor on how to vote.

A restriction in a company's articles upon the transfer of shares covers only the transfer of the legal title, i.e. a transfer in the title of the person on the register of members, and does not include transfer of the beneficial interest. Thus, if A and B are the only shareholders in a company and B has a majority holding, then if on the death of B his executor, C, who has obtained registration, holds the shares on trust for beneficiaries, X and Y, and C proposes to vote in accordance with the wishes of X and Y so that X and Y will control the company, then A cannot claim that there has been a transfer of the shares of B entitling A to the implementation of a pre-emption clause under which A might require the shares held by C to be offered to him (A) (see ***Safeguard Industrial Investments Ltd*** **v** ***National Westminster Bank*** [1982] 1 All ER 449).

Of course, if C had been refused registration under a provision in the company's articles allowing this, he could not vote and so the above situation would not apply.

Transmission of shares

This occurs where the rights encompassed in the holding of shares vests in another by operation of law and not by reason of transfer. It occurs in the following cases.

(a) Death of a shareholder

The shares of the deceased shareholder vest, in terms of the rights they represent, in executors (or administrators if there is no will) who can sell or otherwise dispose of them, e.g. to a beneficiary, without actually being registered, subject to any restrictions on transfer which the articles may contain. CA 2006, s 774 provides that the company must accept probate of the will, or in the case of administrators, letters of administration, as sufficient evidence of the title of the personal representatives notwithstanding anything in its articles.

Personal representatives can insist on registration as members in respect of the deceased's shares unless the articles otherwise provide. Under *Table A*, Reg 30, the directors have the same power to refuse to register personal representatives as they have to register transfers, provided the shares are not fully paid, i.e. Reg 24 applies and they may refuse the transfer on the grounds that the personal representative is a 'person' of whom they do not approve. The company cannot insist that personal representatives be registered as members, but Reg 30 of *Table A* allows them to elect to be registered subject to the above restriction. If they are registered as members, they become personally liable for capital unpaid on the shares with an indemnity from the estate, but they do receive the benefit of being able to vote the shares at general and class meetings and to participate in written resolutions. *Table A*, Reg 31 excludes voting rights unless personal representatives are registered. They receive all the benefits attaching to the shares without registration except voting rights. Where, under the articles, they are refused registration, they may now apply to the court for relief, e.g. an order to the company to register them under CA 2006, s 994 on the grounds of unfair prejudice.

(b) Mental Health Act patients

Transmission also occurs to a receiver appointed by the Court of Protection to the estate of a person becoming a patient under the Mental Health Act 1983. The authority of the receiver is established by production of the protection order of the court appointing him. The position of the receiver is similar to that of personal representatives.

(c) Bankruptcy of a shareholder

On the bankruptcy of a member, the right to deal with the shares passes to the trustee in bankruptcy, and he can sell them without actually being registered or he can elect to register subject to any restrictions in the articles. Regulation 30 of *Table A* allows him to elect to register. He would then be personally liable to pay any calls on the shares subject to a right of indemnity against the estate. When the trustee sells the shares, the sale is effected by production to the company of the share certificate together with the Department of Trade and Industry's certificate appointing the trustee and a transfer signed by him. A trustee cannot

vote unless he is registered but can direct the bankrupt on the way he must vote (***Morgan* v *Gray*** [1953] 1 All ER 213).

A trustee in bankruptcy has a right of disclaimer under which he may disclaim shares as onerous property where there are calls due on them and they would have little value if sold. This power is given by s 315 of the Insolvency Act 1986. Disclaimer is effected by the trustee serving upon the company a notice in writing disclaiming the shares, and he is then not personally liable to pay any calls if registered and the estate of the bankrupt member is no longer liable as such. The company may claim damages, which in the case of shares of little value, which was the reason for the disclaimer, are unlikely to be as much as the calls due but unpaid (***Re Hallet, ex parte National Insurance Co*** [1894] WN 156). Shares disclaimed may be reissued as paid up to the extent to which cash has been received on them. However, the company would have to ask the court for an order temporarily vesting the shares in the company so that it could reissue them. Section 320 of the Insolvency Act 1986 applies. This is because on disclaimer the shares vest in the Crown (Treasury Solicitor) as *bona vacantia* (property without an owner). The situation is one of legal difficulty and doubt and legal advice would have to be sought from a firm specialising in insolvency practice.

Trustees

The shares, if trust property, are transferred to the trustees by the settlor (in a lifetime trust), or by his personal representatives where the trust is by will. If new trustees or replacement trustees are appointed once the trust has begun, the shares must be transferred to the new trustees by the surviving former trustees in the usual way, i.e. by stock transfer form. There is no transfer by operation of law on the appointment of the new trustee, nor under s 40 of the Trustee Act 1925 where the trustee is appointed by deed.

Section 40 provides for the automatic transfer of property without a transfer or conveyance to include a new trustee where his appointment is by deed. However, the section specifically excludes company shares, which must be transferred into the joint names of the trustees including the new one(s) in the ordinary way.

Essay questions

1 Edward owns a small number of shares in Severn Ltd, a private company. He wishes to transfer these shares to a charity but fears that the directors may object.

For what reasons may the directors refuse to register such a transfer and for how long may they delay their decision? (*The Institute of Chartered Accountants in England and Wales*)

2 Write explanatory notes on TWO of the following:

(a) The doctrine of *ultra vires*.

(b) Promoters.

(c) Certification of transfer forms.

(d) Ways in which shares may be mortgaged. (*Kingston University*)

3 (a) What is the procedure for varying the rights attached to a class of shares if the memorandum and articles are silent on the matter? What safeguards are there for a minority of that class?

(b) Explain the liability of a person who presents a forged share transfer to the company for registration and is registered accordingly. Can the company ever be liable in this situation?
(*The Institute of Chartered Secretaries and Administrators*)

4 Sprouts Ltd wishes to change its name to Greenstuff Ltd and trade under the name of Brassica Wholefoods. What steps must be taken to achieve this result?
(*The Institute of Company Accountants*)

5 Write notes on TWO of the following:

(a) The name clause of the memorandum.

(b) The transfer of shares.

(c) Variation of class rights.

(d) Promoters. (*The Institute of Chartered Secretaries and Administrators*)

Test your knowledge

Four alternative answers are given. Select ONE only. Circle the answer which you consider to be correct. Check your answers by referring back to the information given in the chapter and against the answers at the back of the book.

1 When is it necessary to certify a transfer of shares?

A Where there are pre-emption rights in the articles.
B When a part holding of shares is being transferred to the transferee(s).
C When shares are being transferred to an existing member.
D On all transfers of unlisted shares.

2 What is the legal position of a person who buys shares on the faith of a share certificate issued by a company to a transferee on the basis of a forged transfer?

A The person gets an equitable interest in the shares.
B The transfer is valid and the person gets a good title if he has acted in good faith.
C The transfer is void and the person cannot claim against the company.
D The transfer is void but the person has a claim for compensation against the company.

3 Conwy Ltd has a provision in its articles which allows a transfer of shares to be made orally. This provision is:

A invalid.
B valid.
C voidable.
D valid if the transfer is to an existing member.

4 Botham dies and leaves all his shares in Thames Ltd to Gower. Under the articles the shares in Thames 'can only be transferred by the directors'. What must Botham's executor do to pass the shares to Gower?

- **A** Become a member and sign a transfer deed.
- **B** Sign a transfer in the form of a deed.
- **C** Sign a stock transfer form.
- **D** Become a member and sign a stock transfer form once on the register of members.

5 Maurice has become bankrupt. What is the legal effect of his bankruptcy on his shareholding in Mersey Ltd?

- **A** Maurice retains his title and control of the shares but his trustee can file a stop notice.
- **B** Maurice retains his title but the control of the shares is transmitted to his trustee in bankruptcy.
- **C** The title to the shares passes to Maurice's trustee in bankruptcy.
- **D** Maurice retains his title and control of the shares.

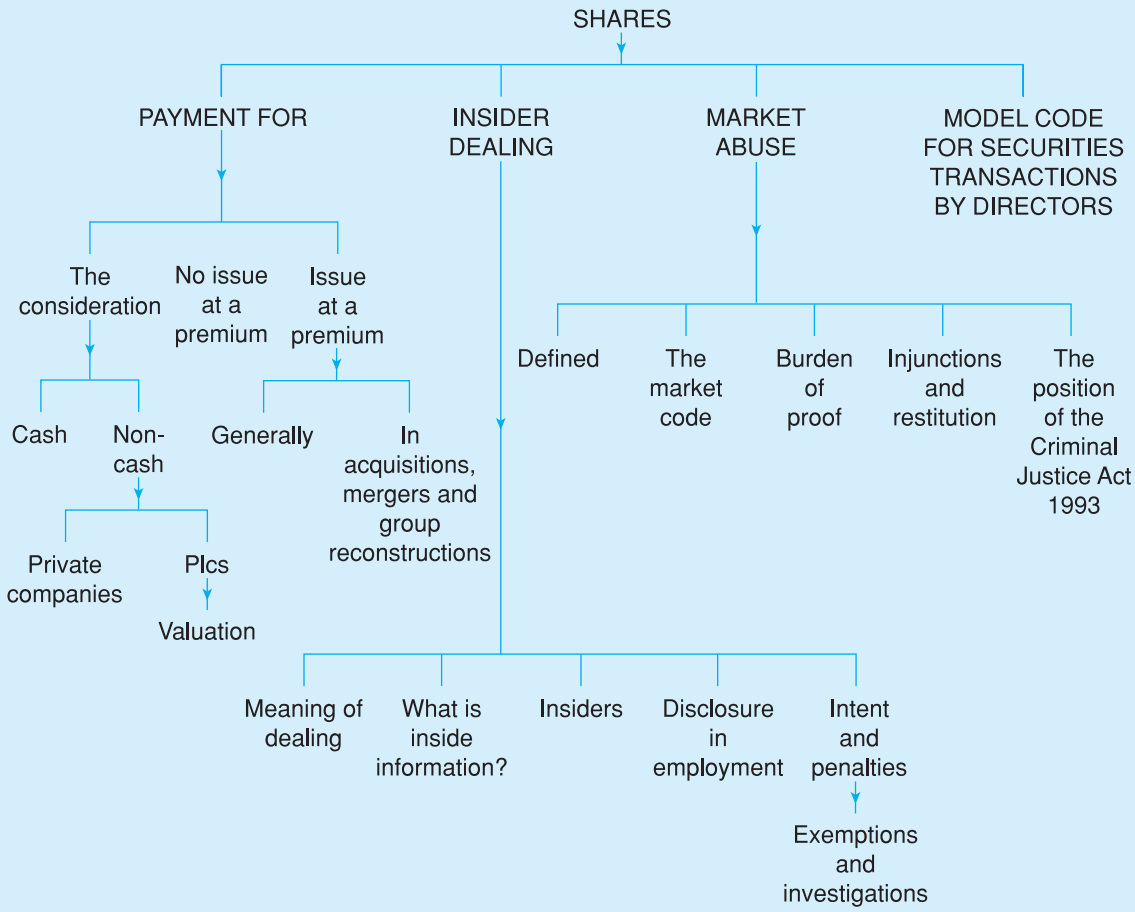
6 In which of the following circumstances is Fred not a member of a company?

- **A** Fred subscribed the memorandum but his name is not as yet on the register of members.
- **B** Fred has been allotted shares and entered on the register but has not received a letter of allotment.
- **C** Fred has lodged a transfer with the company as transferee but has not yet been entered on the register of members.
- **D** Fred has sold all his shares in the company to Bill but Fred's name has not yet been removed from the register of members.

The answers to test your knowledge questions appear on p. 616.

Visit **www.mylawchamber.co.uk/keenancompany** to access study support resources including practice exam questions with guidance, weblinks, legal newsfeed, answers to questions in this chapter, legal updates and further reading.

13 Shares – payment for and insider dealing



In this chapter we shall deal with the methods of payment for shares and the rules which apply according to the consideration offered, together with the rules relating to insider dealing. Companies Acts 2006, Chapter 5 to Part 17 is the applicable provisions that deal with payment for shares.

The consideration – generally

A member of a company must pay for his shares in full, and no arrangement between the company and the members can affect this rule (***Ooregum Gold Mining Co of India*** v ***Roper*** [1892] AC 125). However, payment need not be in cash but may be for some other consideration. Where this is so issues at a discount may still in effect be made in private companies. CA 2006, s 580 requires that shares must not be allotted at a discount. CA 2006, s 581 considers provision for different amounts to be paid on shares.

Payment in cash

This is generally affected by handing cash or a cheque to the company, but if the company pays an existing debt by an issue of shares to the creditor, this set-off arrangement is deemed to be a payment in cash. CA 2006, s 582 provides that shares allotted by a company and any premium on them may be paid up in money or money's worth (including goodwill and know-how). CA 2006, s 583 provides the definition for payment in cash: a share in a company is deemed paid up in cash, or allotted for cash, if the consideration received for the allotment or payment up is a cash consideration.

Re Harmony and Montague Tin and Copper Mining Co, Spargo's Case
(1873) LR 8 Ch App 407

A company purchased a mine from Spargo and he made an agreement to buy shares in the company. The moneys owed by Spargo to the company for his shares and by the company to Spargo for the mine were payable immediately. Under a further agreement between Spargo and the company, he was debited with the amount payable on the shares and credited with the purchase price of the property making up the difference in cash. It was *held* by the Court of Appeal in Chancery that Spargo must be deemed to have paid for his shares in cash.

Comment

The provisions of the Companies Act relating to an issue of shares for a non-cash consideration seem not to apply to set-offs of this kind which are regarded as cash transactions. Section 739 provides, in effect, that the issue of shares to satisfy a liquidated sum, i.e. an existing quantified debt, as in this case, is not an issue for a consideration other than cash.

Considerations other than cash

(a) In private companies

Such considerations are legal, and the consideration very often consists in the sale of property to the company or the rendering of services. The consideration offered must be sufficient to

support the contract in law and must not, for example, be past, though in private companies, at least, it need not be adequate.

Re Eddystone Marine Insurance Co [1893] 3 Ch 9

The company proposed to raise capital from the public, but passed a resolution before going to the public to allot £6,000 worth of fully paid shares to the existing directors and shareholders for a consideration other than cash. A copy of the agreement was filed in which the consideration was said to be services rendered by the allottees to the company during its formation. There was in fact no such rendering of services. Eighteen months later the company was wound up, and the liquidator proposed to regard the shares as unpaid on the grounds that there was no consideration given for them.

Held – by the Court of Appeal – the allottees must contribute the nominal value of the shares. There was in fact no consideration because the services had not been rendered, but even if they had, they would not have supported the contract to take the shares because the consideration would have been past.

Comment

CA 2006, s 585 provides that a public company shall not accept at any time in payment up of its shares or any premium on them, an undertaking given by any person that he or another should do work or perform services for the company or any other person. If shares are issued for services by a public company the holder is liable to pay the nominal value and any premium to the company plus interest set by the authorities pursuant to CA 2006, s 592. This applies whether the services are rendered or not. If services are rendered the person who renders them must pay for his shares and submit an account for the services.

Re Wragg Ltd [1897] 1 Ch 796

Messrs Wragg and Martin were the proprietors of a livery stable business and they agreed to sell it to a company, Wragg Ltd, which they formed. The business was sold to the company for £46,300, among the assets being horses and carriages valued for the purposes of the sale at £27,000. The company paid for the business by issuing shares and debentures to Wragg and Martin, and later, when the company was being wound up, the liquidator asked the court to declare that the shares were not fully paid up because it appeared that the horses and carriages had been overvalued and were really worth only £15,000 at the date of sale.

Held – by the Court of Appeal – that:

(a) Where fully paid shares are allotted to vendors under a contract registered in accordance with the Companies Acts, it is not illegal for the said vendors or promoters to make a profit, though disclosure is required. In this case disclosure did not arise, since Wragg and Martin and certain nominees of theirs became the only shareholders in Wragg Ltd, and they were aware of the details of the transaction.
(b) The court will not go behind a contract of this sort and enquire into the adequacy of the consideration unless the consideration appears on the face of the contract to be insufficient or illusory. This was not the case here for if the company had received advice on the purchase of the business, some advisers might have thought that, looking at the business as a whole, it was a good bargain at £46,300.

(c) Where persons, as vendors, make an agreement with themselves and their nominees in the character of a limited company it is, following ***Salomon* v *Salomon & Co***, 1897, an agreement between independent legal entities and is valid.

Comment

The CA 2006, s 585 places restrictions on public companies in regard to the allotment of shares for a non-cash consideration by requiring, among other things, a valuation of that consideration. However, in private companies the company's valuation of the consideration will still be accepted as conclusive in the absence of, for example, fraud.

It should be noted, however, that the court will enquire into the agreement where the consideration does not really exist.

Hong Kong & China Gas Co Ltd* v *Glen [1914] 1 Ch 527

The company agreed that in return for a concession to supply gas to the city of Victoria, Hong Kong, it would allot the vendor of the concession 400 shares of £10 each, fully paid; and it further agreed that if and when it increased its capital in the future, the vendor or his executors, administrators or assigns should have as fully paid, one-fifth of the increased capital. In this action the company asked the court to decide whether the part of the agreement relating to the one-fifth share of any increase in the capital of the company was binding.

Held – by the High Court – it was not. The insufficiency of the consideration appeared on the face of the contract, for the company had agreed to give at any future time or times a wholly indefinite and possibly unlimited value for the purchase of the concession.

An agreement to allot shares for future services, even in a private company, may mean that the allottee will become liable to pay for the shares in full, since if he does not render the services, the company would otherwise be reduced to a mere action for damages, and would not have an action for the actual price of the shares, and it is doubtful whether a company can replace the liability of a member to pay for his shares in full with a mere action for damages (***Gardner* v *Iredale*** [1912] 1 Ch 700).

Where shares are issued for a consideration other than cash, the contract, or if the contract is not in writing written particulars of it, must be sent to the Registrar for registration within one month of the allotment of the shares. If there is no such registration within the time prescribed, the officers of the company are liable to a fine under the CA 2006, s 590, but the allotment is not affected. It should be noted that *mere registration* of a contract will not make it binding on the company if there is no consideration for it (***Re Eddystone Marine Insurance Co***, 1893, see above).

(b) In public companies

Under s 587 of the CA 2006 a public company is only allowed to allot shares as fully or partly paid by an undertaking to transfer a non-cash asset to the company if the transfer is to take place within five years of the date of the allotment.

In addition, under CA 2006, s 593 an allotment for a non-cash consideration is not to be made unless the non-cash asset has been valued by an independent accountant who would be qualified to be the auditor of the company (or by someone else approved by that independent accountant). In addition, the independent accountant must have reported to