

Trap for Directors Dealing in Shares

A recent dispute over the purchase of shares has highlighted to us an opportunity for disaffected parties who buy shares from or sell shares to directors, and a pitfall for directors selling or purchasing shares in the same company. Section 149 of the Companies Act 1993 ("Section 149") can have an extraordinary effect on the price of shares sold or purchased by a director of the same company to which the shares belong.

Section 149 states that where a director of a company holds information which they would not otherwise have access to but for being a director of the company, and it is material to the assessment of the value of the shares, that director may only acquire or dispose of shares if:

- the acquisition is not made for less than the fair value of the shares; or
- the sale is not made for more than the fair value of the shares.

This has opened up a line of litigation where the courts have changed the price of a transaction in cases where a director held information that affected the price of the shares so that the other party received less than "fair value" from the transaction.

It does not matter that the other party was also in possession of the same information so long as it was not public knowledge. It also does not matter whether the transfer price was agreed to by the other party if the other party had the same information so long as the transfer was not made for "fair value". There is a very high expectation that a director dealing in shares must abstain from dealing in their shares if they would receive more than fair value.

"Fair value" may also have a different meaning from "Fair market value" which has had consequences where the price under a contract for the sale of shares at "Fair Market Value" was found to not be a sale at "fair value" under Section 149.

Section 149 can have very drastic consequences for both directors and any party who sells or purchases shares from a director.

Directors must be very careful with the price at which they sell or purchase shares in the company in which they are a director. Where a director might perceive they are getting a good deal a court may overturn the transaction or change the price of the share transaction against the director's interests.

For parties dealing with directors in a share sale or purchase this may also mean that even if the price of a share transfer is agreed to with the full knowledge that the director is getting more than fair value from



the transaction, the other party may be able to insist on receiving “fair value” for the shares. This could happen even once the transaction has been completed.

From public companies to the smallest SME, directors need to be aware of their duties in relation to dealing in shares. Be aware also that directors who are trustees of a trust that owns shares could be caught out too.

If you have any questions or queries in relation to sale or purchase of shares where an interested director is involved please contact us at Brookfields Lawyers. We would be pleased to assist you.

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