



SHIELDING THE VULNERABLE: ASSESSING THE ADEQUACY OF MINORITY SHAREHOLDER PROTECTION UNDER SRI LANKA'S COMPANIES ACT

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The protection of minority shareholders has become an increasingly critical concern in corporate governance, particularly in jurisdictions with high ownership concentration, such as Sri Lanka. In the contemporary corporate world, activists often strive to ensure that all shareholders of a company, regardless of their stake size, receive fair treatment in decision-making processes and equitable treatment within corporations, as disparities among the shareholders can lead to dissent and potential conflicts which can be injurious for the success of a company. This article critically examines the adequacy of legal safeguards available to minority shareholders under the Companies Act No. 7 of 2007 of Sri Lanka. When drawing upon the foundational common law principle of 'Majority Rule' laid down in the *Foss v. Harbottle case*, it states any wrong done to the company must be remedied by the company not individual shareholders. In other words, the company is a separate legal entity, and only the company (usually through a majority vote of shareholders) can sue to enforce its rights. This paper reconnoiters how statutory interventions have evolved to mitigate the potential for majority shareholder abuse. It also explores how the Companies Act No. 7 of 2007 and common law principles aid the protection of minority shareholders. The study analyzes key remedial provisions such as derivative actions, oppression remedies, minority-buy-out and the just and equitable winding-up mechanism. This research is based on primary texts such as legislation written on shareholder rights and case law and secondary sources such as journal articles, textbooks, research reports, past case studies concerning subject matter and comparative analysis with foreign jurisdiction UK. The essay gauges whether these statutory protections offer sufficient recourse to minority shareholders facing marginalization, unfair prejudice, or expropriation. The findings suggest that while the Sri Lankan legal framework offers several formal protections, practical enforcement challenges and judicial dogmatism may hinder their efficacy. To ensure a fair balance between majority control and minority rights it is recommended to continually develop the judicial interpretation and minority activism to the effective practice of the intent of the Companies Act of Sri Lanka which gives significant protection to the minority shareholders.

Keywords: majority shareholders, minority shareholders, companies act (Sri Lanka), Foss v. Harbottle, Corporate Governance

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INTRODUCTION

In the intricate world of corporate governance, power is rarely distributed equally among the shareholders of a company. Thus, corporate dynamics create a distinction among shareholders as majority and minority of a company. Majority shareholders hold a significant position in the ownership structure of a company, frequently possessing the power to influence key decisions through their voting rights. Their control subtleties can shape corporate governance and undoubtedly affect the strategic direction of the organization while the minority shareholders are lacking control over corporate decisions and have less than 50% of a company's shares. Minority shareholders often face challenges in protecting their interests. This research aims to seek whether all shareholders of a company, regardless of their stake size, receive fair treatment in decision-making processes and equitable treatment within corporations as per the Companies Act No. 7 of 2007. Disparities among the shareholders can lead to dissent and potential conflicts which can be injurious for the success of a company. To strive for success all investors can engage effectively in the governance of their companies with objective of balancing the conflict between majority and minority shareholder rights in Sri Lanka and guarantee protection to the minority shareholders under the legal framework of Sri Lanka.

METHODOLOGY

This doctrinal approach draws on legislation, case laws, journal articles, textbooks, research papers, assessments, past case studies, reports with respect to the subject matter and related electronic data bases to reach its conclusion. Furthermore, best practices from foreign jurisdictions, particularly the UK, were examined to assess remedies for protecting minority shareholders.

RESULTS AND DISCUSSION

When tracing the history of Minority Shareholder Rights, the legal principles laid down in the *Foss v. Harbottle* case are significantly important. The majority rule laid down in *Foss v. Harbottle* case limits the rights of minority shareholders by demarking the idea that emphasizing that they cannot bring any legal action simply because they disagree with a decision approved by the majority shareholders of the company. The majority rule endorsed in *Foss v Harbottle*



extends to cases in which the corporations are competent to ratify managerial misdeeds. The freedom given to the majority in decision making might be abusive or incorrect, and it can be harmful for the growth and success of the company, as the majority shareholders are also capable of being wrong in decision making. Majority shareholders have a fiduciary duty to act in the best interests of the corporation and proactively protect the rights of minority shareholders. Thus, it can be established that the callousness and absolute nature of principle of majority rule needs to be mitigated to establish corporate democracy and minority protection in a company. There are certain acts and incidents which no majority of shareholders can approve of or affirm such as in oppressive conduct, reduction of stated capital etc. In such cases, shareholder may sue to enforce obligations owed to the company. Likewise, due to the exceptions to the general principle established under *Foss v. Harbottle* case such as, a shareholder may bring action against a company in those instances where an act is ultra vires, for the acts requiring special majority, violation of individual rights of the shareholders, where the majority of a company's members use their power to defraud or oppress the minority.

Consequently, law needs to neither give more power to majority shareholders nor minority shareholders. Under the Companies Act No. 07 of 2007 of Sri Lanka protection is rendered on minority shareholders expressly stating remedies for them. Firstly, Section 234 to Section 237, which establishes, Derivative. Derivative action is a claim brought by a shareholder on behalf of and for the benefit of the company, in respect to a wrong done to the company. Simply, a derivative action is a complaint brought by a shareholder against directors, management and/or other shareholders of the corporation, for a failure by management. This type of action often arises when there is fraud, mismanagement and/or dishonesty which are being disregarded by officers and the Board of Directors. Secondly, as per Section 224, any shareholder or shareholder of a company who has a complaint against the company that the affairs of such company are being conducted in a manner oppressive to any shareholder or shareholders (including the shareholder or shareholders with such complaint) may make an application to court. Thirdly, Section 225, shareholder or shareholders of a company, having a complaint that the affairs of the company are being conducted in a manner prejudicial to the interests of the company or that a material change (not being a change brought about by or in the interest of any creditors, including debenture holders or any class of shareholders of the company) has taken place in the management or control of the company can bring actions. Fourthly, on an application made under Section 233, the Court may, make an order restraining a company that, or a director of a company, proposes engage in a conduct that would contravene the articles of the company or any provision of the Companies Act, from engaging in that conduct. Additionally, for the protection of the minority shareholders, the Companies Act of Sri Lanka establishes an exist option for dissenting minority shareholders



which is known as Minority-Buy-Out under the Section 93. Additionally, minority shareholder rights are protected under the Companies Act of Sri Lanka by giving right to inspect company records, including the register of shareholders, the register of directors, the financial statements. This right is given under the Section 119 of the Companies Act of Sri Lanka. This ensures transparency within the company and can detect any misconduct or unfair conduct of the majority shareholders.

When comparing the Sri Lanka jurisdiction with United Kingdom's jurisdiction regarding the protection of minority shareholder rights, Sri Lankan Companies Act was largely exhibited on British corporate law, particularly with respect to minority shareholder remedies. However, UK has evolved significantly, introducing more advanced mechanisms for shareholder protection. For an instance, Sri Lanka and UK recognize Derivative action under their Companies Acts. However, in Sri Lanka the practical enforcement is limited due to high legal costs, lack of awareness, and judicial delays, whereas in UK, Strong judicial guidelines and court oversight enable derivative actions to be a realistic remedy for minority shareholders. With regards to 'Just and Equitable Winding Up', courts in Sri Lanka are reluctant to grant winding-up orders and prefer alternative remedies. Nevertheless, spotting the commercial realities of close corporations, the UK courts are more prepared to intervene. Additionally, courts are accessible, and costs are mitigated through case management, ADR, and active judicial oversight in UK, whereas court delays and litigation costs discourage minority shareholder activism and lack of specialized commercial courts hampers effective enforcement. Moreover, in UK shareholders can easily access due to broader interpretation, more case law, and streamlined commercial courts. However, in Sri Lanka, by adopting these best practices in UK, Sri Lanka can move to a system where minority shareholder rights are truly protected and enforced, thereby enhancing investor confidence and corporate accountability.



CONCLUSIONS/RECOMMENDATIONS

The Companies Act no. 07 of 2007 effectively balances the principle of majority rule with protection for minority shareholders by entrenching several statutory exceptions and judicial remedies, while the majority shareholders maintain significant power in a company, the companies act of Sri Lanka introduces mechanisms to curtail abuse and protect minority interests, aligning with modern corporate governance principles and judicial precedents. Despite the robust legal framework, practical challenges such as cost and complexity of derivative and oppressive actions deter minority shareholders, and judicial delays, informal control (e.g.- family-run companies) can defy formal protections granted under the legal framework. However, the effectiveness in practice depends on enforcement, access to remedies, and awareness among shareholders. Moreover, it is recommended to continually develop the judicial interpretation by strengthen Judicial Interpretation through a Purposive Approach for an instance, courts in Sri Lanka should interpret minority protection provisions in a commercially realistic and equitable manner, similar to the UK's approach under *O'Neill v Phillips [1999] 1 WLR 1092*(Sri Lankan courts could more explicitly adopt the *legitimate expectations* doctrine). Thus, it is recommended to expand the scope of 'unfair prejudice' under section 224 of the Companies Act of Sri Lanka. This development can be done through: regular judicial training programmes in corporate governance law, publication of detailed written judgments to guide lower courts and practitioners, establishing a specialised commercial bench to handle complex shareholder disputes. Moreover, to develop minority activism to the effective practice of the intent of the Companies Act of Sri Lanka which gives proper and significant protection to the minority shareholders.

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