Corporate democracy in theory and practice : the role of shareholders in modern corporations

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CORPORATE DEMOCRACY IN THEORY AND PRACTICE

THE ROLE OF SHAREHOLDERS IN MODERN CORPORATIONS, THE EFFECTIVENESS OF THE EXISTING MEANS FOR PROTECTING THEIR INTERESTS AND THE POSSIBILITY AND DESIRABILITY OF IMPROVEMENT

by

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ABSTRACT

This thesis examines the theory of shareholder democracy and the law of corporate democracy governing the role and procedures of the general meeting. The discussion is illuminated by a comparison of Australian, British, Canadian and American law which features references to the Canada Business Corporations Act, 1974, the Business Corporations Act, 1970 (Ontario), the Model Business Corporations Act and the regime established under the Securities Exchange Act, 1934 (USA). The contribution which shareholder democracy can make to solving the problems of the modern corporation is assessed in the context of the other major theories of corporate reform.

The allocation of powers to the general meeting is examined and it is suggested that the power of the general meeting be clarified by adopting provisions comparable to the North American provisions defining proper subject. The influence of the majority rule principle on voting rights and devices influencing "control" is considered and the adoption of provisions governing use of shareholder agreements and voting trusts is recommended.

The law relating to convocation and notice of the general meeting and to the proxy system is scrutinized. Various recommendations are made as to the principles which should be recognized and the procedural requirements which should be laid down in these areas.

NOTE AS TO METHODOLOGY OF FOOTNOTES

1. Four Acts are repeatedly cited throughout the thesis and accordingly the following abbreviations have been adopted for ease of reference:

U.C.A. - The Uniform Companies Act, Australia, as adopted in New South Wales, Victoria, Queensland and Western Australia in 1961 and in South Australia, Tasmania, the Australian Capital Territory and the Northern Territory in 1962. Where appropriate amendments adopted in the several States are noted.

Bus. Corp. Act (Ont.) - The Business Corporations Act of Ontario, R.S.O. 1970 c. 53.

Can. Bus. Corp. Act - The Canada Business Corporations Act, 1974-1976 c. 33.

Mod. Bus. Corp. Act Ann. 2d. - The Model Business Corporations Act, Annotated, second edition, produced by the American Bar Association - Section on Corporation, Banking and Business Law, Committee on Corporate Law, 1971 supp. 1973.

2. In citing decisions of courts in the United States of America, the Anglo-Australian style is followed in that the year of the decision is given in parenthesis immediately after the name of the case while jurisdiction and court are given after the citation unless they appear from the name of the report. The manner of indicating court and jurisdiction is that stipulated in M.O. Price & H. Bitner, Effective Legal Research, Third edition (Boston, Little Brown, 1969).

3. Two changes in the style of the footnotes were made by the typist in the final version. These are the printing of the names of articles in italics instead of plain face and the placement of author's initials after instead of before the surname. The writer apologizes for the annoyance this departure from usual legal style may cause and asks the reader's indulgence.

PART I INTRODUCTION

This thesis sets out to examine the contribution which shareholder democracy as a reform strategy can make to the problem of the growth within our society of the power of the corporate manager, particularly of the power of the manager of the large corporation. There are two factors contributing to the growth of managerial power. These are, first, the growth in power of the large corporation and, secondly, the growth of the manager's power within the corporate structure.

It is possible to seek a solution to the problem by directing attention either to restraining the power of the corporation within the society or by seeking to limit the power of the manager within the corporation. Corporate social responsibility is the catch-phrase of those who seek to restrain the power of the corporation, but there is no general agreement as to its specific meaning[1]. It is clear, however, that those who advocate recognition of corporate social responsibility are motivated by their recognition of the direct and decisive impact of the large corporations on the economic and political life of society to call on the corporation to have regard to the interests of society at large instead of solely the interests of the shareholder. For some this implies that the corporation should abandon the profit motive[2], for others it merely means that the corporation should recognize duties and obligations arising from its relationships with society at large and

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1. Blumberg, P., *Corporate Responsibility in a Changing Society, Essays on Corporate Social Responsibility,* (Boston, Boston University School of Law, 1972) 2-10.
2. Dodd, E.M., *"For Whom are Corporate Managers Trustees?"* (1932) 45 Harv L Rev 1145.

should refrain from the single-minded pursuit of short-range profit[3]. Blumberg, writing in 1973, pointed out that although the recognition by corporate managers of a responsibility to interests other than those of shareholders has been the subject of considerable academic discussion, significant legal recognition of corporate responsibilities has not been achieved[4], and nothing has happened in the intervening years to change this situation.

Shareholder democracy as a reform strategy, unlike the movement for corporate social responsibility, concentrates on proposals for altering the distribution of power within the corporation so as to limit the power of the manager by giving more power to the general meeting. Inasmuch as it is considered that the shareholders voting in general meeting may be influenced by motives other than the desire to see profits increased, shareholder democracy may allow individuals to bring various social imperatives into play in forming corporate objectives, but this is not the formal objective of the movement.

As an introduction to the study of the reform proposals put forward by those who advocate shareholder democracy, it has been deemed appropriate to survey the philosophies of corporate reform in an attempt to come to an understanding of the role and importance of shareholder democracy. This part of the thesis is intended merely as an introduction. This is stressed because it is necessary to acknowledge that discussion of the matters briefly touched upon in its course could be greatly expanded. The objectives of this introduction are to define the problem addressed,

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3. See Confederation of British Industry, *The Responsibilities of the British Public Company*, Final Report of the Company Affairs Committee (London, 1973).
4. Blumberg, *op cit*, 49; see also Landowne, R. and Segal, J.,*"The Social Responsibility of Modern Corporations"* (1978) 2 UNSWLJ 336.

to outline a number of responses that the problem has elicited, and to show how these responses are related.

A. THE PROBLEMS PERCEIVED

In the early 1930's, Berle and Means were moved to unite their talents to study the increasing power that was being concentrated through the means of the corporate system in the hands of corporate managers. The result was the production of the classic study, *The Modern Corporation and Private Property*[5]. That work contained the first factual study of ownership patterns undertaken[6], as well as the beginnings of a prescriptive analysis of the problems of corporate control[7]. Since that time, a number of comparable studies has been produced. In Australia particular notice should be taken of the work of Wheelwright, Rolfe and most recently Lawriwsky[8]. No attempt has been made to duplicate or update that work in this thesis. This section concentrates instead on an

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5. Berle, A.A. and Means, G.C., *The Modern Corporation and Private Property*, (New York, MacMillan & Co, 1932).
6. Berle's comment on the importance of the work is of interest: "I thought we were merely describing a phenomenon with which everyone was familiar and still think so. But the phenomenon had not apparently received economic attention." Berle, A.A., *Power without Property*, (New York, Harcourt, Bruce & World Inc, 1959) 19-20, but see Flynn, J.J., "Corporate Democracy: Nice Work If You Can Get It" in Nader, R. and Green, M., *Corporate Power in America*, (New York, Grossman Publishers, 1973) 95.
7. Nichols, T., *Ownership, Control and Ideology*, (London, George Allen & Unwin Ltd, 1969) 29.
8. Wheelwright, E.L., *Ownership and Control of Australian Companies: A Study of 102 of the Largest Public Companies Incorporated in Australia*, (Sydney, Law Book Co, 1957); Wheelwright, E.L. and Miskelly, J., *Anatomy of Australian Manufacturing Industry: The Ownership and Control of 300 of the Largest Manufacturing Companies in Australia*, (Sydney, Law Book Co, 1967); Rolfe, H., *The Controllers: Interlocking Directorates in Large Australian Companies*, (Melbourne, F.W. Cheshire, 1967); Lawriwsky, M., *Ownership and Control of Australian Corporations*, (Transnational Corporations Research Project, University of Sydney, 1978).

attempt to show how the significance of the facts has been assessed by those who have cared to comment on them.

It was Berle and Means' conclusion that:

> "[A] society in which production is governed by blind economic forces is being replaced by one in which production is carried on under the ultimate control of a handful of individuals. The economic power in the hands of the few persons who control a giant corporation is a tremendous force which can harm or benefit a multitude of individuals."*9*

Writing in 1959, Berle found renewed cause for concern in the continuation of the trend towards concentration of power in the hands of the large corporations and the growth of institutional investment with the consequent accumulation of voting rights in the hands of institutional managers. The result as he saw it was that:

> "Past rights are collectivized, present capacity is concentrated, future development of economic government will be by relatively few men. These men are detached from the conventional workings of the profit system; they become in fact an unrecognized group of professional administrators distributing the fruits of the...industrial system, directing its present activities and selecting the path of its future growth."*10*

One of the most recent reports on the area is that of the 1978 Canadian Royal Commission on Corporate Concentrations. The Commissioners found that although the aggregate concentration, that is, the percentage of economic activity accounted for by the largest firms, had decreased in Canada from 1923 to 1975, and despite the fact that Canada's largest corporations were very much smaller than their counterparts in the

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9. Berle and Means, *op cit*, 46 ; for an assessment of this conclusion see Hazen, T.L. and Buckley, B.L.,*"Models of Corporate Conduct: From the Government Dominated Corporation to the Corporate Dominated Government"* (1979) 58 Nebraska L Rev 100, 106.

10. Berle, *op cit*, 18.

United States of America, large firms were more dominant in Canada than in the United States[11]. On the basis of the Australian studies, it may be suggested that here too the dominance of big companies may be more pronounced[12].

The facts revealed by these studies furnish two separate though interrelated causes of concern. The problem of curbing the power of the corporation or company itself would be less urgent if there was no cause for concern with the manner of selection and the method of calling corporate management to account for their use of that power. However, there is evidence to suggest that these methods are not totally satisfactory. The Canadian Royal Commission report, cited above, referred to the results of a 1976 American study which revealed the fact that from 1956 through 1973, the elections of directors that went unopposed in the companies studied went from 98.10% in 1958 and 1961 to 99.79% in 1975, while in the same years the elections in which management retained control of the board ranged from 99.70% to 99.90%. No comparable statistics were available for Canada but it was suggested that a Canadian survey would

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11. Canada, Royal Commission on Corporate Concentration, *Report of the Royal Commission on Corporate Concentration*, (Ottawa, Minister of Supply and Services, 1978) 11-12. Compare these results with those reported for Great Britain: Hannah, L. and Kay, J.A., *Concentration in Modern Industry*, (London, MacMillan Press Ltd, 1977) 85 *et seq* where it was reported that during the period 1957 to 1976, industrial concentration in Britain increased significantly.

12. Wheelwright, E.L., "Introduction" in Rolfe, *op cit*, ix: "The dominance of companies is a well known fact of modern capitalist economies. Australia is no exception. In fact, because the Australian economy is relatively so small, their dominance...is probably more pronounced than in larger economies." For Australian statistics see Dunlop, W.C., "The Small Firm" in Lindgren, K.E. and Aislabie, C.J., *The Australian Firm*, (Sydney, McGraw-Hill, 1976) 146 where it is shown, for example, that small manufacturing firms consisting 94.1% of all manufacturing firms employed 32% of the employees engaged in manufacturing and were responsible for 25.8% of total value added.

reveal similar results[13], and there seems no reason to doubt that the pattern would be carried through in Australia.

One response that has been elicited by these perceived facts has been a call for the recovery of constituent power over the corporation[14]. It has been suggested that fundamental changes in the structure of the corporation may be necessary to achieve legitimacy and accountability[15]. By way of definition it may be pointed out that power is legitimate when its holder's entitlement to it depends on meeting the requirements of some test or standard so that he will be deprived of it if it is demonstrated that he has no title or right to possess it[16]. For those concerned with legitimacy and accountability,

> "the essential elements in a healthy system of corporate government...are, first, a mechanism by which the shareholders or other constituents of the corporation can make an informed decision on the choice of their managers and on other important questions of corporate policy and second a method by which corporate managers may be required to account for their stewardship."[17]

To some extent, legitimacy and accountability are provided by the current framework and accordingly for many commentators the crux of the problem is the fact that the power wielded by company managers is now seen as being significant in a much wider context. "Today there is only a tenuous

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13. Canada, Royal Commission on Corporate Concentration, *op cit*, 284 citing Nader, R., Green, M. and Seligman, J., *Constitutionalizing the Corporation, the Case for the Federal Chartering of Corporations*, (Corporate Accountability Responsibility Group, 1976).
14. Eells, R., *The Government of Corporations*, (New York, The Free Press, 1962) 43.
15. Blumberg, *op cit*, 59; see also Flynn, *op cit*, 100-103.
16. Berle, *op cit*, 98.
17. Cohen, M.T., "Introduction" in Aranow, E.R. and Einhorn, H.H., *Proxy Contests for Corporate Control*, 2nd ed (New York, Columbia University Press, 1968) as at XIII.

connection between the givers of the mandate and the power granted and exercised...the power has outgrown the mandate; the ritual process of selection has only historical connection with the real function and concurrent power entrusted to the individual."[18]

The economist and the political scientist tend to face the problem armed with preconceptions derived from their study of the mechanisms of the government of the state and think in terms of political analogies[19]. The lawyer, on the other hand, approaches the problem with preconceptions of another sort and frequently sees the problem as consisting of a discrepancy between the legal model and the reality of corporate governance and control[20]. This approach carries with it the danger that it will lead to an attempt to change reality to correspond with the thoery in order to avoid the necessity of working out a new theory rather than because of a considered decision that this is the way to achieve a desired result. This criticism is dealt with at greater length below; at this stage attention is directed to a description of the discrepancy.

The traditional legal model of the corporate structure was that the board of directors as the managing body of the company had to execute the shareholders' wishes, "the shareholders being the real masters of the corporation"[21]. This model never fully squared with reality[22]. As early as 1776, Adam Smith commented that the general disinterest of the

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18. Berle and Means, *op cit*, 105-107.
19. Eells, *op cit*, 47-48.
20. *Idem*.
21. Grossfield, B., "Management and Control of Marketable Share Companies" in *International Encyclopedia of Comparative Law*, vol XIII c 4.4.
22. *Idem*.

proprietors of joint stock companies in the affairs of the company led to enhanced powers for management[23]. During the nineteenth century similar observations were made by Marx[24].

The generally accepted modern view is that:

> "The balance of power within the firm has been very different from that envisaged by company law, according to which power over the firm is supposed to be wielded by the shareholders. In fact the latter's general meetings have become mere formalities... . The average shareholder has no interest in the general meeting since the important decisions have already been made by the managing committee with the permission of the board of directors which has itself been nominated by the same pressure group. The real policymakers do not own the company, they act as if they had been given a mandate by the shareholders which is not in reality the case."[25]

One commentator, D.E. Schwartz, has taken the position that the problem lies not in a gap between the legal model and reality but in a failure of the legal model to comprehend the process of corporate decision-making. But the distinction is unlikely to make a difference, as: "The fact remains...that management...is the main policy maker and little recognition of their power is found in corporate statutes"[26]. It would therefore seem pointless to insist on the distinction especially as the question of whether the law does make or has ever made specific provision for corporate decision-making in fact is not conclusive of the question of whether there is a gap between the legal model and reality.

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23. Adam Smith, *Wealth of Nations*, (1776) Book V ch 1 part III art 1.
24. Karl Marx, *Das Kapital III*, (Hamburg) ch 23.
25. De Hogton, C. (ed), *The Company: Law, Structure and Reform in Eleven Countries*, (London, Allen & Unwin for PEP, 1970) 177; see also Schwartz, R.N., *"A Proposal for the Designation of Shareholder Nominees in the Corporate Proxy Statement"* (1974) 74 Col L Rev 1139, 1140.
26. Schwartz, D.E., *"Towards New Corporate Goals: Co-existence with Society"* (1971) 60 Geo LJ 57, 76, 77.

Despite the fact that the failure of the law to make provision adequately controlling the process of decision-making in the modern company has been perceived and discussed in academic circles for almost fifty years, the general public, the business world and the legislative process have virtually ignored the problem[27]. The question therefore arises whether the perceived lack or discrepancy is a legitimate matter for concern. Hetherington, having raised the question, points out that not all the anomalies produced by the discrepancy are harmful and that the facade of share ownership may have some useful latent functions with respect to managerial practices and attitudes but concludes that the discrepancy is, in fact, costly. Its dysfunctional consequences include, in his estimation, preventing the law from regulating conduct in realistic terms, producing a preoccupation with the restoration of control to the owners, and obscuring and diverting attention away from the real relationship between management and the shareholders[28].

In the traditional legal model of the company, the board of directors is conceived of as discharging the management function. However, in the large twentieth century corporation this is no longer true; management is instead delegated to executive officers who may or may not occupy a position on the board of directors. The new theoretical function of the board of directors is that of supervising management[29]. Nevertheless, for the purposes of this thesis this distinction is not considered relevant. This is, first, because the degree to which the board has

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27. Hetherington, J.A.C., *"Fact and Legal Theory: Shareholders, Managers and Corporate Social Responsibility"* (1969) 21 Stan L Rev 248, 272.
28. *Ibid*, 273.
29. See Grossfield, B. and Ebke, W., *"Controlling the Modern Corporation: A Comparative View of Corporate Power in the United States and Europe"* (1978) 26 Am J Comp Law 397, 400.

assumed the strictly supervisory position will vary from company to company and, secondly, because management in most companies in which the board does occupy a strictly supervisory position will usually be able to control the membership of the board. This will mean that, instead of being accountable to a board of directors selected by and responsive to the shareholders, management will be in a position to control the board through its selection of directors. Shareholders will be denied any real influence over corporate policy, and an unfortunate by-product of this situation is that it will tend to prevent critical assessment of managerial policies at an early stage[30].

The general meeting cannot hope either to discharge the managerial function or to exercise direct supervision of management. It is clear that the board's intermediation is necessary and that it is neither realistically nor theoretically possible to deprive corporate managements of all powers. However, a recognition of the discrepancy between the legal model and reality does raise the question of whether additional methods of supervision or control should be developed to limit the powers of company executives and what form, if any, such measures might take[31]. Managerialists, as will be seen, would answer the threshold question in the negative, maintaining that there is no need for additional limits. Of those who do concede that there is a problem, some are concerned simply to protect the members of the company from the abuse or improper exercise of powers by management. Others have not accepted the virtual elimination of the general meeting as an effective controlling agent as either necessary or desirable, and accordingly seek to revitalize or restructure the corporate model.

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30. Schwartz, R.N., *op cit*, 1142.
31. Hadden, T., *Company Law and Capitalism*, 2nd ed (London, Weidenfeld & Nicholson, 1977) 327.

B. THE RELEVANCE OF COMPANY SIZE

The problem of the inflation of management power is particularly noticeable in the larger company[32], but the problem of the discrepancy between the legal model and reality or the problem of formulating decision-making rules is not unique to the larger company.

Hetherington has stated that:

> "There is no clear line between corporations in which shareholders are plainly not owners and smaller corporations where, because of concentration of shareholdings, some degree of ownership exists. Changes in social and economic structures are never clear cut, both the ascendant and the declining models co-exist."[33]

But, with respect, the observation about ascendant and declining models is based on an assumption that the smaller corporation will eventually disappear. There is no evidence to indicate that this will happen.

In this regard the result of a study of American corporations by Conard may be noted. It was his conclusion that:

> "The typical corporation is not a multi-billion dollar, multi-million shareholder enterprise...the median corporation may be one with assets of approximately $100,000 and...three shareholders but there is not, in a meaningful sense, any 'typical corporation'. Corporations are spread out along an unbroken spectrum, from no assets to billions of dollars worth and from one shareholder to millions. The greatest number of corporations have assets valued between $10,000 and $1,000,000 and have shareholders numbering less than ten."[34]

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32. Hadden, *op cit*, 327-328; De Hogton, *op cit*, 150.
33. Hetherington, *op cit*, 273.
34. Conard, A.F., *"The Corporate Census: A Preliminary Exploration"* (1975) 63 Calif L Rev 440, 462.

The Australian statistics available tend to suggest the same conclusion: the greatest number of companies appear to fall within the category of exempt proprietary company[35].

Eisenberg criticized the traditional legal model of the corporation for a number of faults including its attempt to embrace all corporations regardless of size. It was his view that the two types of business association, to wit, those owned by a large number of people and those owned by a relatively small number of people, had little in common. Accordingly, he set out to develop two normative models of the corporation[36].

Others have suggested that it is possible to distinguish three types of company. They would recognize, in addition to the very large and the very small corporation, a third intermediate type which closely resembles the legal model described above[37]. This is the classification that is adopted here and an attempt is made below to describe the management problems which may be experienced in the small domestic or quasi-partnership company, the middle range majority controlled company, and the large endocratic corporation.

1. THE DOMESTIC COMPANY

The defining characteristic of this type of company is the substantial

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35. See *Report of the Corporate Affairs Commission, 31 December 1978*, NSW Parliamentary Paper no 111 of 1979, 39 from which it appears that the percentage of public companies fell marginally between 1977 and 1978 from 1.23% to 1.12% while exempt proprietary companies continued in 1978 to make up 78.91% of registered companies.
36. Eisenberg, M.A., *"The Legal Role of Shareholders and Management in Modern Corporate Decision-making"* (1969) 57 Calif L. Rev.1
37. Vagts, D.F., *"Reforming the Modern Corporation: Prospectives from the German"* (1966) 80 Harv L Rev 23, 32.

identification between management and ownership[38]. Membership in these companies is relatively small, even though it may not strictly be limited to members of one family. The assumption may be made that agreements between the owners in such a company are likely to be bargained out, to be real agreements and not merely contracts of adhesion[39].

A number of legal systems, but not the Anglo-Australian system, provide a considerable degree of protection for shareholders in such small companies by means of specific legislative provision[40]. In the United States of America the so-called "close corporation" had to struggle for recognition, but it is now clearly accorded special status[41]. The close corporation and the proprietary company cannot be equated because the category of proprietary company is large enough to embrace many companies where membership numbers exceed the point where it is possible to maintain personal relationships among the members.

Recently there have been certain indications that the courts are willing to recognize that in certain circumstances special considerations must apply to such companies. In *Ebrahimi* v *Westbourne Galleries Ltd*[42], the House of Lords decided that the exercise of legal rights should be subjected to equitable considerations because the association was formed or continued on the basis of a personal relationship involving mutual confidence between the members and that an agreement or understanding to the effect that all of the shareholders would participate in the conduct of the business was proven. More recently in *Clemens* v *Clemens*[43],

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38. See Rider, B.A.K., *"Partnership Law and its Impact on 'Domestic Companies'"* (1979) 38 Camb LJ 148, 149.
39. Eisenberg, *op cit*, 7.
40. Rider, *op cit*, 133.
41. *Ibid*, 158. See O'Neal, F.H., *Close Corporations: Law and Practice*, 2nd ed (Illinois, Callaghan Mundelein, 1971).
42. [1973] AC 360.
43. [1976] 2 All ER 268.

Foster J subjected the exercise of shareholder voting rights in the context of a small domestic company to equitable considerations and supported his decision with dicta from *Ebrahimi* v *Westbourne Galleries Ltd*[44].

In Australia it was recognized in *Re Medefield*[45] that special considerations may apply to "incorporated partnerships". Elsewhere the common law appears to be moving in the same direction[46], and it is submitted that such a development may be supported both in law and in commonsense. A distinction should be drawn between the position of a shareholder in such a company and that of a shareholder in a much larger enterprise both in regard to his relationship with the company and to his relationship with his fellow shareholders[47].

If such a distinction is recognized, it will have certain implications for the constitutional law of the company. In domestic companies the role of the general meeting is preserved by the demands of the companies legislation that certain functions be performed by the company in general meeting. However, it is only where voting rights in general meeting are distributed differently from those in the board of directors that the distinction attains anything other than a formal significance.

In the context of this type of company it is beside the point to talk of the necessity for controlling management power. Problems can and do arise where irreconcilable disputes arise between the members but the

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44. See Rider, *op cit*, 166.
45. (1977) 2 ACLR 406.
46. *Ebrahimi* v *Westbourne Galleries Ltd* [1973] AC 360. See *Wong Kim Fat* v *Leong & Co Sdn Bhd* [1973] MLJ 20 as cited by Rider, *op cit*, 168.
47. Rider, *op cit*, 179.

solution to such problems lies not in a restructuring of the corporate form but in the provision of statutory remedies such as are found in the oppression provisions[48] or in allowing the provisions of a shareholders' agreement to prevail[49].

There is a divergence between the traditional legal model and the reality of the domestic company, and it may be that consideration should be given in Australia to the adoption of provisions akin to those adopted in the United States to govern close corporations[50], but on this question this thesis will have very little more to say.

2. MAJORITY CONTROLLED COMPANIES

Majority controlled companies will for the most part be larger proprietary companies or unlisted public companies, but nevertheless, in his study of two hundred and twenty-six listed companies, Lawriwsky classified twelve of the companies he studied as falling within this category[51]. The defining characteristic of this type of company is that an individual or a coherent group of shareholders owns a majority of the voting shares and is thus assured of carrying an ordinary resolution in general meeting barring the dissolution of the group. Alternatively, there may be a possibility of a re-alignment of votes on each issue so long as the individual shareholdings are large enough for the individual shareholder to expect to be influential in determining the outcome of an issue submitted to the general meeting.

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48. See UCA ss 186 and 222(1)(h).
49. See Part III.
50. See Part III.
51. Lawriwsky, *op cit*, 19.

The reality of the majority controlled company corresponds more closely to the theoretical model than do the realities of either the domestic company or the large endocratic company. Nevertheless, the power of management in such companies is far from negligible. In Australia, where cumulative voting[52] is not in force, there will be shareholders in the majority controlled company who are unrepresented on the board. At the same time, the principle of majority rule may be applied in such companies to augment management power. An instance of this is the fact that in cases concerning such companies there has been a tendency to play down the role of the general meeting. Influenced by the fact that, were things done properly, the will of the majority would prevail, the courts have applied the "internal management" rule[53] against the minority shareholder, at least in situations where the will of the majority is clear.

It is submitted that the fact that the outcome of a poll might be predictable should not prejudice its proper conduct. Putting aside the fact that the alignment of votes might change, the fact remains that the forum should be useful for other things besides merely winning one's point. The importance of the general meeting as a means by which information can be obtained and disseminated and by which dissent can be registered is reason enough to look critically at the role of management in convening and running such meetings and to prompt efforts to ensure that this may be done even where management is unco-operative.

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52. See Part III.

53. See Ford, H.A.J., *Principles of Company Law*, 2nd ed (Sydney, Butterworths, 1978) [305] *et seq.*

3. THE ENDOCRATIC COMPANY

The term "endocratic", meaning governed from within, was coined from two Greek roots by Rostow[54] for application to the large listed company of the sort that is governed by a self-perpetuating body of professional administrators. Endocratic companies fall within this category because their shares are widely dispersed through the agency of the stock market and accordingly only listed companies fall within this category. It is proposed to apply the term "endocratic" generally to all listed corporations that are not majority controlled, but within this grouping it is necessary to distinguish between companies according to control-type in so far as this can be determined.

In determining control-type, regard is had to the ownership of stock, but a classification derived from this information solely will not be totally accurate. Zeitlin has indicated that in assessing the existence of potential for control it is also necessary to have reference to the history of the development of the corporation, to the position within the corporation of institutions or personalities which played important roles in this development, to the resources of any potential rivals for control, and to the inter-relationships between individuals linked by family or professional ties[55]. It is also necessary to take into account the fact that the potential may never be realized because the ownership group lacks the incentive to use it or because the ownership group lacks the energy or the technical competence to utilize its

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54. See Eells, *op cit*, 69.
55. Zeitlin, M., "*Corporate Ownership and Control: The Large Corporation and the Capitalist Class*" 79 Am J Sociology 1073-1119 as cited by Lawriwsky, *op cit*, 3.

potential[56].

The control-types distinguished by Lawriwsky were: majority ownership; minority ownership, where the directors owns between ten per cent and fifty per cent of the ordinary shares, or another private group owns between fifteen per cent and fifty per cent of these shares; domestic, where another Australian company holds more than fifteen per cent of the ordinary shares, which is the dominant holding; or overseas, where a foreign company is dominant and holds more than fifteen per cent of the shares; joint domestic-overseas control; and management control, where shareholdings are so dispersed that none of the above conditions is satisfied[57]. Lawriwsky's conclusion was that ownership of strategic blocks of shares in most listed Australian corporations is highly concentrated, with only thirty-five per cent of companies falling into the management-controlled category. Although this figure was significantly higher than that reported by Wheelwright and Miskelly[58], Lawriwsky considered that it was an overestimate and that although the managerial revolution may have begun in Australia, it was nowhere near completion[59].

The attention of the economist and political scientist has been focussed on the endocratic corporation to the exclusion of any other type of corporation. The endocratic corporation departs from the traditional legal model in a direction which is the exact opposite of that taken by the domestic company. The general meeting in the endocratic company has

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56. Reeder, J.A.,*"Corporate Ownership and Control: A Synthesis of Recent Findings"* (1975) 3 Industrial Organization Rev 18-27 cited by Lawriwsky, *op cit*, 3.
57. Lawriwsky, *op cit*, 9-10.
58. Wheelwright and Miskelly, *op cit*, 6.
59. Lawriwsky, *op cit*, 30-31.

tended, in the face of practical difficulties created by size and shareholder disinterest, to become an empty ritual leaving the shareholders powerless. This tendency has been encouraged by the development of proxy machinery and the resulting shift of emphasis from discussion in the meeting itself to presentation of the proxy materials. However, until it is clearly demonstrated that there is a suitable alternative, the time will not have come to abolish the general meeting. This brings us to a consideration of the alternatives that have been offered for controlling excessive management power.

For the most part, these alternatives have been designed with the endocratic corporation in mind and should accordingly be assessed first from that point of view, but before the present law is changed it will be necessary to consider whether or not any changes made should also apply to domestic companies or majority controlled companies. It will be suggested that many of the proposals put forward by the proponents of shareholder democracy could also be applied for the benefit of the shareholders in majority controlled companies.

C. A PROPOSAL FOR REFORM: SHAREHOLDER DEMOCRACY

Many attempts have been made to prescribe and implement a strategy of legal reform which will provide a satisfactory solution to the perceived problems of the corporate form. In attempting to classify these endeavours, two distinctions are relevant. The first of these is the distinction between reform strategies which may be pursued within the framework of the received corporate model and more radical strategies which call for a wholesale review and restructuring of the corporate

framework[60]. A second distinction overlapping, but not coterminous with, the first is that between constitutionalist reform, which proposes modifying intra-corporate bodies and procedures, and non-constitutionalist reform, which looks to the extension or amplification of extra-corporate review procedures.

The proposals of those who advocate shareholder democracy call for the modification of intra-corporate bodies and procedures within the framework of the received corporate model with the object of bringing the ideal embodied by the model into actuality. Managerialists oppose suggestions for the modification of the role of the manager, and when and inasmuch as its advocates do more than merely attempting to justify the *status quo* they are concerned to make the remedies currently provided by the law more effective. Advocates of non-capital representation suggest that intra-corporate bodies and procedures should be modified to allow workers, consumers and others to be represented and accordingly reject the traditional view of the corporation's structure and role. Advocates of government interventionism also reject the traditional view, but their solution is to depend on the application by the government of external pressures to control the corporation and its managers. There are other factors which may perhaps be relied upon to control the corporation from the outside, but those who rely upon them tend to take the point of view that these are already satisfactorily in control. An attempt will be made to describe the general tenor of the proposals for reform under the headings: shareholder democracy; managerialism; non-capital representation; and governmental interventionism.

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60. Redmond, P.M., *Some Aspects of the Company Director's Fiduciary Obligation*, (unpublished) 169.

1. SHAREHOLDER DEMOCRACY IN THEORY

The term "shareholder democracy" is used interchangeably with the term "corporate democracy" and appears to be an American contribution to the literature of corporate reform. Livingston states that the term, "which was unknown in the twenties", had become accepted terminology by the "mid fifties despite the fact that it constitutes a legal solecism"[61]. The solecism referred to lies in the fact that a corporation is not a democracy inasmuch as a democracy is a government in which each person has an equal vote regardless of the amount of his wealth, while voting rights in a corporation are usually proportional to the member's shareholding[62].

Despite the fact that the term is American, and despite Manning's statement to the effect that corporate democracy is "a shimmering conception fusing good old American free enterprise with good old American Jacksonianism"[63], the concept to which the label is applied is far from being exclusively American. In Britain, as also in Australia and all other countries where the companies legislation is based on the British model, shareholders have always, at least theoretically, played an important role in the corporate structure; indeed, at one stage the company was identified with the shareholders[64]. Moreover, the concept of shareholder democracy, although perhaps not so labelled, extends beyond the common law nations, so that Grossfield, speaking of all Western countries, could state that "all jurisdictions are very much

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61. Livingston, J.A., *The American Stockholder*, (Philadelphia, J.B. Lippincott Company, 1958) 68.
62. Further, see Part III C.
63. Manning, B., *"Review of 'The American Stockholder'"* (1957-58) 67 Yale LJ 1475, 1483.
64. See Part II.

aware of the concept of shareholder's democracy and try to make the shareholders' meeting a real decision-making organ of the corporation"[65].

The ideal of shareholder democracy is that the government of the affairs of a company should be subject to control by the shareholders as the affairs of a democratic government are subject to control by the citizens. All exponents of this reform strategy agree that the power to elect corporate officers and to determine broad issues of policy should be the prerogative of the general meeting, the body of shareholders[66], but differences may appear when it comes to a question of deciding which policy issues should be left to the shareholders. Holding the ideal stated, proponents of shareholder democracy refuse to accept the virtual elimination of the general meeting as an effective controlling agency and the resulting domination of the affairs of large companies by a self-perpetuating body of managers. Accordingly, they urge the adoption of measures which would allow ordinary shareholders acting through the general meeting to exercise general control over the management of the company[67].

Various means of revising the electoral processes so as to replace the present "make-believe democracy" by one in which the "owner-constituency" would be an effective force for self-government have been proposed[68]. These include adoption of the practice of cumulative voting, recognition of the shareholder's right to put forward proposals on proper subjects and various changes to the system of proxy voting designed to make it a

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65. Grossfield, *op cit*, 85.
66. Hadden, *op cit*, 402.
67. *Ibid*, 404-405.
68. Eells, *op cit*, 45.

tool for communication between shareholders and from the shareholders to management instead of merely a tool by which management addresses the shareholders. All of these suggestions are examined in succeeding parts of the thesis.

2. SHAREHOLDER DEMOCRACY IN PRACTICE

(a) In Australia and Britain

Although the Australian Companies Acts give a central role in the company to the shareholders in general meeting, the possibilities of shareholder democracy as a reform strategy have not been explored in the Australian context. In large part this fact can be explained by reference to the history of Australian companies legislation. Until the appointment of the Eggleston Committee in 1967, revision of the Australian Companies Act was not preceded by public inquiry and discussion[69]. Instead, Australian legislation was the result of a series of local adoptions of the legislation passed in England on the recommendation of the various committees set up in that country[70].

At the practical level manifestations or invocations[71] of the spirit of shareholder democracy in Australia are not lacking. It is not considered possible to rehearse here the history of shareholder activist groups established within the framework of individual companies, although the fact that such groups have not been lacking is attested to elsewhere in in this thesis[72]. The existence of the Australian Shareholders

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69. See "*Current Topics*" (1966) 44 ALJ 386; (1961) 34 ALJ 246.
70. Ford, *op cit*, [111].
71. See for example, Editorial, *Australian Financial Review*, Friday 12 April 1977, 2.
72. See Part II A.

Association should, however, be noted. This body considers that its function is to represent shareholder interests and an instance of its activities is its involvement in the affairs of the Nugan group of companies in 1977[73].

In the context of British company law, it has frequently been acknowledged[74] that the principles of shareholder democracy have been the guiding force behind the British Companies Acts since 1855. The said legislation has been framed on the basis that ultimate control over the directors should be exercised by the shareholders[75] and that the most satisfactory way of promoting the objective of shareholder control is by increasing disclosure requirements[76].

The Cohen Committee is noticeable among the successive British company law reform committees that have made it their major concern to find means of making it easier for shareholders to exercise a more effective general control over the management of their companies[77]. It noted the perceived problems of corporate control described above in these terms:

> "The illusory nature of the control theoretically exercised by shareholders over directors has been accentuated by the dispersion of capital among an increasing number of share holders who pay little attention to their

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73. See *Australian Financial Review*, Thursday 29 September 1977, 21; Friday 28 October 1977, 43; Saturday 10 November 1977, 31.
74. See Brown, L., Erskine, G. and Gower, L.C.B., "A Note of Assent" in Great Britain, Board of Trade, *Report of the Company Law Committee*, Cmd 1973 (1962) para 3, hereinafter referred to as the *Jenkins Report*; see also Labour Party, Great Britain, *The Community and the Company: Report of a Working Group of the Labour Party Industrial Sub-Committee*, (London, 1974) 7.
75. Brown, Erskine and Gower, *op cit*, para 3.
76. Labour Party, Great Britain, *op cit*, 2.
77. Brown, Erskine and Gower, *op cit*, para 4.

> investments so long as satisfactory dividends are forthcoming[78], who lack sufficient time, money and experience to make full use of their rights as occasion arises and who are, in many cases, too numerous and too widely dispersed to be able to organize themselves."[79]

Nevertheless, the Committee considered that the fullest practicable disclosure of information should be required so as to lessen opportunities for abuse of power of company management and sought means to make it easier for shareholders to exercise more effective general control over the management of their companies[80]. Among the recommendations they put forward were provisions designed "to make it more difficult for directors to secure the hurried passage of controversial matters and as far as possible to encourage shareholders carefully to consider any proposals required by law to be put before them by the directors"[81]. In consonance with the recommendations of the Cohen Committee, various amendments, some of which will be discussed in the body of the thesis, were introduced into the British Companies Act in 1947 and 1948 and were subsequently incorporated in the Australian Uniform Companies Act adopted in 1961.

The Jenkins Committee adopted an approach at once less pessimistic as to the realities of shareholder control and less committed to its desirability. Commenting on the observations of the Cohen Committee and on the efficacy of the amendments introduced as a consequence of that report, the Jenkins Report states that:

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78. It is suggested that this statement no longer applies with the same force and most especially is this so in the case of the institutional investor in Australia and overseas. See below,
79. Great Britain, Board of Trade, *Report of the Committee on Company Law Amendment*, Cmd 6659 (1943) para 7(a), hereinafter referred to as the *Cohen Report*.
80. *Ibid*, para 5.
81. *Ibid*, para 121.

> "Basically...the passages just quoted from the Cohen Report are as true today as they were in 1945, though we venture to think that the description of 'the control theoretically exercised by shareholders' as 'illusory' is perhaps now something of an overstatement. The Act provides shareholders with powerful weapons provided they choose to use them, and even if practical considerations make them difficult for the small investor to wield, the same cannot be said of the institutional investor."*82*

On the other hand, the Jenkins Committee was alive to the conflicting considerations involved in imposing disclosure requirements and in implementing proposals to give the shareholders closer control over the directors*83*. Nevertheless, they came to the conclusion that a case was made out for legislation, (a) designed to provide shareholders with full information about the company's activities; (b) excluding from the general delegation of powers to directors any sale of the whole or substantially the whole of the company's undertaking and assets; and (c) placing the power of issuing shares under a special form of control exercisable by the company in general meeting*84*. The last two recommendations have not yet been implemented.

The Jenkins Committee considered the suggestion that the sale of voteless shares should be prohibited and, by a majority, rejected it. A minority consisting of Brown, Erskine and Gower, dissented from the majority in this respect, and appended a "Note of Dissent" to the Report. This "Note of Dissent" contains one of the strongest statements in British company law literature of the case for shareholder democracy. The note states that opposition to voteless non-equity shares was based on the fact that the issue of such shares undermined the basic principle

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82. *Jenkins Report, op cit,* para 106.
83. *Ibid,* paras 13 and 14.
84. *Ibid,* para 113.

of shareholder control. In the course of the note the arguments that shareholder control is ineffective and inefficient were discussed. In answer to the argument that shareholder control is ineffective because of shareholder apathy it was said that shareholder intervention is required only when things go wrong and that in such a case shareholders will be collectively powerful so long as they have votes. It was suggested further that the possibility of an outsider acquiring control will cause the directors to pay greater heed to the interests of the shareholders than they otherwise would[85]. In answer to the argument that shareholder control is inefficient because of the directors' greater business skills it was objected that it cannot be said that business efficiency is ensured by allowing the directors to function free from outside control, except that which the courts exert in the event of fraud or misfeasance or to make themselves irremovable without their own consent, however inefficient they prove to be[86].

The descriptive statements in the British reports stated above are out of date, and in particular, no mention is made in them of the significance of the growing power of the institutional investor and the decreasing reluctance of these shareholders to use their power. This is a factor which will in the future have to be taken into account. While those who seek to implement shareholder democracy as a means of redressing the swing away from individual to institutional power will find no consolation in the growing activity of institutional investors, those who advocate it on the basis that it contributes to corporate efficiency by exposing management policies to internal review must welcome such growth.

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85. Brown, Erskine and Gower, *op cit*, para 7.
86. *Ibid*, para 8.

Despite the fact that the Jenkins and Cohen Committee Reports are thus in one respect outdated, they have been quoted at length because outside the context of the reports of committees set up for the specific purpose of advising on changes in the companies legislation, there has been little discussion of the principles of shareholder democracy in either Australia or Britain. In this area there has been none of the impassioned advocacy of a principle which can be found in American periodical literature[87]. However, it is suggested that this difference is not peculiar to this area of legal discussion.

(b) In the United States of America before 1967

Among the American advocates of shareholder democracy it is possible to distinguish two separate groups. These groups are defined by reference to their objectives. The original adherents of the concept were concerned to monitor the performance of company managements to ensure that mismanagement did not occur and that managerial interests were not allowed to supplant the interests of the shareholders[88]. This group, who might be called "corporate gadflies" after the soubriquet applied to their most famous member, Lewis D. Gilbert[89], commenced activity in the 1930's and were alone in the field until 1967. The second group, which calls itself "Ethical Investors", consists of people who base their investment or proxy voting decisions partially or wholly on information characterized as non-financial. Their objective is to promote corporate social responsibility. This second group emerged as a

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87. See for example Bayne, *"Basic Rationale of Proper Subject"* (1937) U Det LJ
88. Gilbert, L.D., *Dividends and Democracy*, (Larchmont, New York, American Research Council, 1956) 6.

phenomenon in the stock market in the late 'sixties[90]. The significance of the ethical investor movement will be discussed in the next succeeding subsection of this thesis.

Basic American corporation law is laid down by state statutes which, like their Anglo-Australian counterparts, give shareholders a right to vote in general meeting and demand that certain of the corporation's powers must be exercised in general meeting[91]. However, the right to vote is only one of the three elements that are necessary to allow shareholders to perform a substantial role in enforcing managerial responsibility. As well as the power to vote, shareholders need information about the corporation's affairs and the power of initiative to prevent the inertia or contrary intention of the managers from prevailing[92].

Hurst states that the standard pattern of corporate law in the states of the United States of America by the 1880's made sufficient provision for shareholders' right to vote, to receive information and to take the initiative to give some substance to their supervisory role. However, he continues,

> "the prevailing trend of state law did not improve and in some respects weakened the stockholder's capacity for effective oversight. The span from the 1930's through the 1960's included more active concern in law for the shareholder's power position than any previous era had witnessed but there were strong enough cross currents to deny a clear net gain in stockholder impact."*93*

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90. Thorson, J.,*"The Ethical Investor and the SEC Conflict over the Proper Scope of the Shareholders Role in the Corporation"* (1978) 2 J Corp L 115. See also Purcell, T.V.,*"Management and 'Ethical Investors'"* (Sept-Oct 1979) Harv Bus Rev 24.

91. Mod Bus Corp Act Ann 2d s 33 para 1 and see, for example, ss 39, 59, 73 and 79.

92. Hurst, J.W., *The Legitimacy of the Business Corporation in the Law of the United States, 1780-1970,* (Charlottesville, University Press of Virginia, 1970) 88.

93. Hurst, *op cit,* 89.

Emerson and Latcham appear to disagree with Hurst inasmuch as they assert that the state corporation statutes failed to give the stockholder the right to receive information and accordingly had the result of making the general meeting into a mere formality[94]. Whatever the attributed cause, it is generally agreed that in the early twentieth century, general meetings of shareholders in American business companies had become empty formalities.

The unregulated development of the proxy system in the first quarter of the twentieth century had the effect of exaggerating the stockholder's helplessness. Management was not obliged to divulge any information to the stockholders from whom it solicited proxies, to give these stockholders any option other than to give management a blank endorsement, to solicit proxies from all stockholders or to exercise the proxies which were received. Further, when management entered a general meeting armed with sufficient proxies to decide any motion put before the meeting, it could treat the stockholders who did attend the meeting with contempt. The result was that the stockholder's ability to ask questions in general meeting and to propose motions from the floor of the meeting became meaningless.

One of the objects of the "New Deal" securities legislation enacted by the federal government of the United States was to restore some power to the general meeting. The Securities Exchange Act of 1934 enabled the Securities and Exchange Commission to make rules regulating the solicitation and use of proxies[95]. These rules provided for effective

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94. Emerson, F.D. and Latcham, F.C., *Shareholder Democracy: A Broader Outlook for Corporations*, (Cleveland, Press of Western Reserve University, 1954) 7.
95. Securities Exchange Act, 1934 (US) s 14, Code of Federal Regulations.

disclosure of all material information pertinent to proposals for corporate action put forward by management. They specifically prohibited resort to the use of fraud or fraudulent practices in the solicitation of proxies. Finally, they gave to the independent stockholder the right to solicit proxies himself or to put forward proposals for action to be included in the proxy materials sent out by management[96].

The statement that Congress intended by its enactment of section 14 of the Securities Exchange Act to give true vitality to the concept of corporate democracy is so well supported and has been repeated so often that it is now described as a banality[97]. It is supported by reference to the express statement to this effect made in Congress in the course of its enactment[98], by the language of the section, by the history and record of its administration[99], and by judicial interpretation[100].

Taking advantage of this legislation, an informed and active group of shareholders led by Lewis D. Gilbert emerged to lead the fight to put corporate democracy into practice[101]. The "corporate gadflies", whose members included the Gilbert brothers and Wilma Soss, made a practice of appearing and speaking at company meetings, of writing and of using litigation to enforce shareholder rights and advance corporate democracy. As a result of their efforts, more and more managements became conscious

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96. Emerson and Latcham, *op cit*, 8.
97. *Medical Committee for Human Rights* v *SEC* (1970) 432 F 2d 659 (DC Cir).
98. "Fair corporate suffrage is an important right that should attach to every equity security bought on a public exchange. Managements of properties owned by the investing public should not be permitted to perpetuate themselves by the misuse of corporate proxies." HR Rep No 1383, 23d Cong 2d Sess 63 (1934).
99. *Medical Committee for Human Rights* v *SEC* (1970) 432 F 2d 659, 680 (DC Cir).
100. See *Medical Committee for Human Rights* v *SEC* (1970) 432 F 2d 659 (DC Cir); *SEC* v *Transamerica Corp* (1946) 67 F Supp 326 (D Del), (1947) 163 F 2d 511 (3rd Cir).
101. Livingston, *op cit*, 68-76.

of their relations with their shareholders. Better corporate reports were produced and attendances at general meetings increased[102]. The increased awareness of and concern for the principles of corporate or shareholder democracy was attested by the attention given to the 1954 amendments to the proxy rules. Not only did a number of academics give testimony at the hearings[103], but a remarkable number of articles appeared in legal periodicals[104].

Nevertheless, Manning, writing in 1958, compared the findings of Berle and Means in 1932 with the recent report from Livingston and concluded that shareholders as a group did not seem to have gained in power[105].

One of the main factors to which Gilbert attributed the failure of the efforts of shareholder democracy to have a larger effect on the corporate world was the so-called "Wall Street Rule"[106]. This rule of practice which was adhered to most noticeably by institutional investors prompted its adherents to use their voting power to support management and, if unable to do so, to sell out rather than to vote against management[107]. The prevalence of this practice threatened to become increasingly significant as statistics showed that the holdings of stock by institutional investors increased from eighteen per cent of

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102. Livingston, *op cit*, 71-72.
103. Bayne, D.C., Caplin, M.M., Emerson, F.D. and Latcham, F.C., *"Proxy Regulation and the Rule Making Process: The 1954 Amendments"* (1954) 40 Va L Rev 387.
104. See Bayne, D.C., *"Law, the Proxy and Social Responsibility"* (1955) 34 Mich State L Rev 36; Bayne, D.C., *"Basic Rationale of Proper Subject"* (1957) 34 U Det LJ 575; Caplin, M.M., *"Shareholder Nominations of Directors"* (1953) 39 Va L Rev 141.
105. Manning, *op cit*, 148.
106. Gilbert, *op cit*, 50.
107. Schwartz, D.E., *"The Public Interest Proxy Contest - Reflections on Campaign GM"* (1971) 69 Mich L Rev 419, 495.

corporate stock outstanding in 1951 to twenty-four per cent in 1968[108] and have continued to grow since that time. However, it must be noted that the practice has changed in the last ten or fifteen years. In the United States the ethical investor movement is at least partially responsible for the change.

(c) In the United States since 1967

The first attempt by a public interest group to use the proxy machinery to force management to consider matters of public interest was the 1967 Eastman Kodak campaign mounted by a group known as FIGHT[109]. The year 1967 is therefore significant because it marked the first emergence of an organized group intent on using shareholder or corporate democracy as a method of promoting corporate social responsibility. The activity of such groups has been a significant factor in the history of corporate government in the United States of America since that date. It is not proposed to rehearse here the detailed history of the activities of these groups, but in order to assess the significance of such groups some reference must be made to their major achievements.

An early theoretical victory was won by the Medical Committee for Human Rights when it challenged the Securities and Exchange Commission's decision to allow management to exclude the proposal to prohibit the sale of napalm from the proxy material to be circulated by Dow Chemical Company. The Securities and Exchange Commission contended that their decision was not reviewable, but this contention was rejected by the court[110]. Furthermore, the court evinced a willingness to measure the Commission's

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108. Goldsmith, R.W. (ed), *Institutional Investors and Corporate Stock*, (New York, National Bureau of Economic Research, 1973) 148.
109. Thorson, *op cit*, 131.
110. *Medical Committee for Human Rights* v *SEC* (1970) 432 F 2d 659 (DC Cir).

determinations against the intention to promote corporate democracy which it found underlying the relevant section of the Securities Exchange Act[111].

Campaign GM succeeded in attracting wide public attention to the issues of corporate responsibility and corporate democracy and focussed more specifically on the issues of the scope of resolutions that may properly be presented for inclusion in the proxy statement, the methods of proxy solicitation, and the role of financial institutions as shareholders[112]. Campaign GM succeeded in having two of its nine proposals included in the General Motors proxy statement in 1970. Its efforts to win the votes of institutional investors also met with some success when the New York City Pension Funds voted for and vocally supported its proposals. Furthermore, the debate generated within the community of financial institutions signified that the "Wall Street rule" no longer commanded undivided loyalty and led one observer to predict that "next time around, it may be different"[113].

The interest aroused in the issues of corporate social responsibility and corporate democracy by these activities led to a revision of the Securities and Exchange Commission's shareholder proposal rules in 1972[114]. It also led to a much deeper inquiry into the possibility of using the proxy rules to promote communications between the shareholders and the company and among the shareholders. In 1977 the Commission initiated a

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111. See Allen, P.H., *"The Proxy System and the Promotion of Social Goals"* (1970-71) 26 Bus Law 481 and Thorson, *op cit,* 131-134.
112. Schwartz, D.E., *The Public Interest Proxy Contest, op cit,* 430; see also Schwartz, D.E., *"Corporate Responsibility in the Age of Aquarius"* (1970-71) 26 Bus Law 513; Schwartz, D.E., *"Towards New Corporate Goals: Co-existence with Society"* (1971) 60 Geo LJ 57.
113. Schwartz, D.E., *"The Public Interest Proxy Contest - Reflections on Campaign GM"* (1971) 69 Mich L Rev 419, 506 and 495.

re-examination of Regulation 14A governing proxy solicitations by requesting submission of written statements on the topics of shareholder communications, shareholder participation in the corporate electoral process and corporate governance[115]. Hearings were subsequently held in four cities. In June 1978, the Commission deferred action on some of the issues which included the ability of shareholders to nominate board candidates and whether legislation is needed to protect shareholder rights. Action continued on other issues and in July 1978 a release detailed several proposed changes in the proxy rules designed to provide shareholders with increased information concerning the quality and effectiveness of the corporate board of directors[116]. The comments received on these proposals were overwhelmingly negative and accordingly the proposals were revised before being incorporated in rules which became effective as of 25 December 1978[117]. In August 1979[118] the Commission agreed to propose a rule that would limit corporate management's discretionary authority to vote the proxies of shareholders who did not specify a choice on non-election matters along the lines suggested in the body of this thesis[119]: that is, shareholders could expressly give management discretionary voting authority, but without such approval shares could not be voted, although they could be counted for quorum purposes. A second proposal put forward at this time would allow shareholders to vote for or against individual directors and require that information on such voting be provided if

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115. 401 Securities Regulation and Law Report (5.4.77) G1-4, hereafter cited as SRLR.
116. 461 SRLR (7.12.78) A9-11; 462 SRLR (7.19,78)A18, F1-11.
117. 482 SRLR (12.13.78) E1.
118. 515 SRLR (8.8.79) A1; 516 SRLR (8.15.1979) H1-6.
119. See Part VI.

one director received a five per cent negative vote. As of September 1979, no further action had been taken, although publication of a comprehensive report on issues of corporate governance in early 1980 was forecast.

As of 1979, the significance of the ethical investor movement in the United States of America is seen to lie mainly in the fact that the attitudes of many of the actors in the corporate drama appear to have changed inasmuch as there is now a heightened sensitivity to corporate governance and corporate accountability issues. This increased sensitivity obviously owes something to the revelations of corporate corruption in the mid-seventies, and the role of business initiative in fostering it cannot be discounted, but the ethical investor movement has also been instrumental in furthering it. The change of attitude by the courts has been described above. The change of attitude on the part of the Securities and Exchange Commission has led to the amendments to the shareholder proposal rules which have already been detailed.

A change of attitude on the part of institutional investors is demonstrated by the establishment and growth of bodies such as the Inter-Faith Centre on Corporate Responsibilities and the Investor Responsibility Research Centre, whose function is to analyse the issues involved in corporate social responsibility shareholder proposals and to advise institutional investors on them[120].

Shareholder proposals, which continue to be advanced in increasing numbers, are almost invariably rejected in general meeting if management decides to oppose them, but some concrete results have been achieved.

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120. Purcell, *op cit*, 26.

In some cases the proposal has received management support and has been adopted, in others the proposal has been rejected but corporate behaviour has later been changed to conform to it[121]. In a number of cases proposals have been withdrawn after discussions between the proponents and management have led to agreement on the issues involved[122]. On first sight the withdrawal of proposals which has the effect of preventing the issues from being decided by the general meeting may not seem to advance the interests of corporate democracy, but on reflection it is seen that the decision of non-contentious issues is not submitted to the *demos* in any type of representative democracy.

Although many managements probably continue to see the movement as a harassment, this attitude is no longer universal. Among those who have commented favourably on the impact of the shareholder movement are certain corporate directors. One such man, the secretary of Connecticut General Life Insurance Company, stated that:

> "I believe the effectiveness of the shareholder movement has been demonstrated in several different ways through the higher levels of management involvement, the significant number of companies dialoguing with shareholders... and the impact the resolutions are having on companies."*123*

D.H. Ruttenberg, chairman of Studebaker-Worthington, has been quoted as saying that:

> "The ethical investor movement gives managers a chance, I think, better to share with activists, large institutional investors and the general public their problems and limitations on their ability to change things."*124*

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121. Purcell, *op cit*, 24-25.
122. *Ibid*, 30.
123. As quoted by Purcell, *op cit*, 44.
124. As quoted by Purcell, *op cit*, 43-44.

It would thus appear that the last decade in the United States has seen an expansion of the potentialities of shareholder democracy through the injection of new interests.

3. ASSESSMENT OF SHAREHOLDER DEMOCRACY

What follows is an attempt to assess the worth of shareholder democracy as a reform strategy. For the purposes of evaluation, the strategy will first be assessed without reference to the efforts and achievements of the ethical investor movement. This is done because it is considered that the interests represented by the movement are wider than those of the shareholder *qua* shareholder. Once this basic evaluation has been made, an attempt will be made to assess the significance of the ethical investor movement to the strategy.

Hetherington, writing in 1969, before the existence of the ethical investor movement was widely recognized, described the efforts of the corporate democracy movement as an attempt to remodel reality to conform with theory. He stated that the movement had produced a considerable amount of publicity and much smoother corporate public relations but little else[125]. It may be observed that to attempt to remodel reality to conform with theory is regarded as a heinous offence compounded of an ostrich-like burying of the head in sand and an indulgence in futile efforts. On the other hand, an attempt to use the law to improve the current situation is generally regarded as laudable. It is suggested that the fact that a reformer's attempts to improve a current situation are informed by reference to a familiar theory need not make them less praiseworthy or less capable of achieving their objective given that

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125. Hetherington, *op cit*, 252.

the merits of the theory have been reassessed. As regards the criticism that the movement has produced nothing but smoother corporate public relations, it is suggested that, so long as disclosure is regarded as a specific against abuse, the production of smoother corporate public relations even in and by itself should not be decried. Further, it is suggested that these changes signify at the very least an alteration for the better in managerial attitudes.

Manning's criticism of shareholder democracy is that it is based on unwarranted assumptions. Shareholder democracy is, in his view, relevant if, but only if, it is assumed that shareholders when in power will keep managers in line to the benefit of all society[126]. The unwarranted assumptions on which he considers shareholder democracy to be based are the assumptions that the rest of society need not worry about corporate power so long as the "owners" are running the companies and that the same corporate policies are more satisfactory when set by shareholders than when set by managers[127]. Given the premise that shareholder democracy is designed to be a method of making corporate power socially responsible, the criticism is well founded. However, the premise must be challenged. It has been suggested that the question of how to make corporate managers accountable and responsible is separate from the question of how to make the corporation itself socially responsible. It is now suggested that shareholder democracy is addressed primarily to the first of these issues and only secondarily, if at all, to the second. Under these circumstances, to criticize the strategy for failing to be a complete answer to the problem of corporate social responsibility

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126. Manning, *op cit.*
127. Manning, B., *"Corporate Power and Individual Freedom"* (1960) 55 NW U L Rev 38, 42.

is not a damning argument. Further, Eisenberg, commenting on Manning's criticism, points out that if power to determine vital aspects of national economic life has become concentrated in the hands of a few enterprises, it might seem better to disperse decision-making powers within those enterprises rather than to limit the number of voices to be heard within the enterprise[128].

At this stage the school of thought which discounts shareholder democracy on the basis of the assertion that shareholders are not as well equipped to make corporate decisions as the directors must be considered. It is argued by those who advance this criticism that shareholders must frequently exercise their powers "on the basis of an imperfect understanding of the situation, in a forum which is not suited to arriving at the most reasonable solution because a simple answer of 'yes' or 'no' is required rather than a consideration of alternative policies"[129]. In response to this criticism the defence offered is confession and avoidance. It is acknowledged that the general meeting is not the place to work out the details of a business decision. Such details are the responsibility of the corporate executive, but broad questions of policy can and should be determined by the general meeting. The question of whether an issue should be submitted to the general meeting should be determined not by asking whether the shareholders' ability to understand an issue is equivalent to management's but by asking whether a proposal can be so framed as to be decided by a yes or no answer and whether shareholders have enough interest and understanding to want to make that decision[130].

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128. Eisenberg, M.A., *The Structure of the Corporation*, (Boston, Little, Brown & Co, 1976) 19.
129. De Hogton, *op cit*, 182.
130. Schulman, S.,*"Shareholder Cause Proposals: A Technique to Catch the Conscience of the Corporation"* (1971-72) 40 Geo Wash L Rev 1, 65.

It is submitted that shareholder democracy as a reform strategy has a contribution to make to all but the smallest companies. The reasons why shareholder democracy is inapplicable in the very small company were explored above[131]. In the middle range majority controlled company, however, shareholder democracy is highly relevant. There, the number of shareholders is small enough to allow for effective organization of sizable minority groups and rights of communication and initiative become significant. In the very large endocratic company, it might well be that no change in the actual control and management of the company would result if all efforts to maintain shareholder democracy were abandoned[132]. However, Eisenberg's argument that the fact that shareholder democracy successfully prevents a *de facto* self-perpetuating oligarchy from becoming a *de jure* self-perpetuating oligarchy is sufficient reason for maintaining it[133] is respectfully adopted. It is suggested that in Australia, as in the United States of America, few people would be found ready to dismantle the machinery of corporate democracy even in the largest companies[134]. Further, the developments of the last decade in the United States of America[135], which appear to suggest that institutional investors are prepared to abandon their neutrality, gives reason to hope that new validity will be lent to the concept of shareholder democracy in Australia too.

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131. See above, 12-15.
132. Conard, A.F., *Corporations in Perspective*, (Mineola, New York, Foundation Press Inc, 1976) 359.
133. Eisenberg, *The Structure of the Corporation*, *op cit*, 19.
134. Conard, *Corporations in Perspective*, *op cit*, 339.
135. See generally, Longstreth, B. and Rosenbloom, H.D., *Corporate Social Responsibility and the Institutional Investor: A Report to the Ford Foundation*, (New York, Praeger Publishers, 1973) and see above 33-38; see also Blumberg, P.I., *The Megacorporation in American Society: The Scope of Corporate Power*, (Englewood Cliffs, New Jersy, Prentice-Hall, 1975).

The ethical investor movement is designed to use the methods of shareholder democracy to serve the purpose of promoting corporate social responsibility. Inasmuch as the shareholder is also a citizen of the society in which the corporation exists, he has a legitimate interest in ensuring or attempting to ensure that all the implications of corporate decisions are considered. As a responsible citizen, the shareholder would presumably consider it his duty to evaluate all the implications of any decision made in the course of his personal business and it is argued that it is his right and duty[136] to attempt to ensure that the same is true of corporate decisions. Further, it is submitted that the fact that a person whose interest in the corporation is occasioned primarily by some other relationship with the corporation, such as an employee of the corporate enterprise or a consumer of the company's products, may by purchasing shares in the company secure a voice in the company's general meeting, is not a disadvantage[137]. It may not be strictly consistent with the theory that the property interest should dominate in questions of corporate policy, but it is an appropriate means of focussing the social consensus on particular questions of corporate policy.

It is further submitted that the use of the general meeting as a forum in which corporate issues can be presented for discussion makes it easier to accept the thesis advanced by Berle in *Power without Property*[138] that corporate power may properly be controlled by the public consensus. Without the existence of a forum in which specific corporate issues can

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136. Bayne, *Basic Rational of Proper Subject, op cit.*
137. Schulman, *op cit*, 42-43.
138. Berle, *op cit*; see below, 48-51.

be discussed it would be impossible to form the requisite consensus.

D. MANAGERIALISM

Managerialism is primarily a socio-economic theory which perceives the development of managerial power as one of the most important aspects of the evolution of twentieth century society. Managerialist writers are so called because they adopt a tone of descriptive approbation sometimes bordering on the lyrical when writing about the growth of managerial power in the major institutions of the twentieth century including the modern corporation. In so far as these commentators have devoted any attention to suggestions for reform, their efforts have been directed to discrediting proposals made by others.

1. MANAGERIALISM AS A SOCIO-ECONOMIC THEORY

The proposition that a separation of ownership and control occurs in the context of the modern corporation is the first premise of the socio-economic theory labelled managerialism. All managerialists accept as factually correct the statement that, due to the increased financial and technological complexity of modern business, the shareholders have lost the ability to intervene. Some managerialists argue that shareholders today have no desire to intervene. Managerialists further assume that because managers have a different relationship to private property to that of the controlling owner-manager, they also have different interests and objectives and pursue significantly different policies[139].

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139. See Nichols, *op cit*, 52.

When managerialists set out to formulate problems for inquiry, they make the fundamental assumption that the two functions of ownership and management, which were originally performed by one actor, the owner-manager, are now performed by two actors, the shareholder and the manager. This formulation rests on the assumption that the shareholder and the manager are two discrete entities and has tended to neglect the possibility that their expectations of each other may have an important formative influence[140].

The proposition that industrialism would lead to a separation of ownership and control had been mooted before the advent of the twentieth century, but the first scholars to muster factual data to show that such a change had in fact occurred were, as already stated, Berle and Means, leading managerialists. Later studies have tended to confirm their findings with some reservations[141], and this premise has for many years been almost universally accepted in Western non-communist nations[142].

The implications of this premise are not so clear-cut, and managerialist writers themselves have advanced many different points of view. An early controversy inside the managerialist ranks was that between Berle, who stated that managers should thenceforth be seen as holding their powers in trust for the shareholders[143], and Dodd, who argued that corporate managers should be seen as holding their powers in trust for the community as a whole rather than for the shareholders alone[144]. In

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140. Nichols, *op cit*, 144.
141. Dahrendorf, *Class and Class Conflict in Industrial Society* as cited by Nichols, *op cit*, 42.
142. Nichols, *op cit*, 40 citing Dahrendorf, *op cit*, 42.
143. Berle and Means, *op cit*, 242.
144. Hazen and Buckley, *op cit*, 111-115; see also Rostow, E.W., "The Responsibility of Corporate Managements" in Mason, E.S. (ed), *The Corporation in Modern Society*, (Harvard University Press, 1960).

later years Berle came to hold the view that corporate management had been forced into a role of social statesmanship by public demand and now held their powers in trust for the community[145]. If Berle's original approach is adopted, the degree to which the corporation's decisions are socially responsible will depend on the shareholders; abandoning this position leaves it open to place the responsibility squarely on management.

If the managerial premise is accepted, the question of the motivation of company managers becomes important. There is a theory, labelled "non-sectional managerialism" by Nichols, which maintains that managers, far from being self-interested, are "neutral" men who strive to fulfil a variety of social responsibilities. There is a conflicting theory, adopted by Burnham and Dahrendorf and others[146], which maintains that managers do in fact act in their own self-interest. Commenting on the relative merits of these two theories, Nichols said:

> "Sectional theories appear to have a higher face validity ... . It is more realistic to assume that business men will be more interested in the pursuit of self-rewarding objectives than they will be in policies of the social service variety."[147]

This assessment, however, ignores the fact that self-rewarding objectives can include such intangibles as prestige and security of position as well as financial gain.

In *The Twentieth Century Capitalist Revolution*, Berle invoked the Augustinian hypothesis of the City of God, which stipulated that

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145. Hazen and Buckley, *op cit*, 112.
146. Nichols, *op cit*, 43.
147. *Ibid*, 154.

> "underlying, entering, complementing and ultimately controlling every tangible institutional organization of affairs there was inevitably a moral and philosophical organization which continued from age to age and which ultimately directed power."*148*

Applying this hypothesis, Berle maintained that

> "corporate managements...are constrained to work within a frame of surrounding conceptions which in time impose themselves. The price of failure to understand and observe them is decay of the corporation itself."*149*

In *Power without Property*, Berle further developed this notion by introducing the two new terms of "corporate conscience", which restrains management from acting in its own self-interest, and "public consensus", or public opinion, to which he suggests management is ultimately accountable[150]. It was Berle's view that management was now directly accountable to society due to the development of the corporate conscience and the recognition of the importance of public consensus, and that this development had been made possible by a decline in shareholder control[151].

The concept of the corporate conscience, the influence of the principles held by individual members of management, is reinforced by the observations of Galbraith on motivation[152]. In particular Galbraith points out that although pecuniary compensation is an extremely important stimulus to individual members up to a point, inasmuch as they will demand an acceptable salary, once this requirement is met other goals

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148. Berle, A.A., *The Twentieth Century Revolution*, (London, MacMillan & Co, 1955) 145.
149. *Ibid*, 153.
150. Berle, A.A., *Power without Property*, (New York, Harcourt, Bruce and World Inc, 1959) 96-99, 110.
151. See Nichols, *op cit*, 23.
152. Galbraith, J.K., *The New Industrial State*, 2nd ed (London, Penguin Books, 1974) 139-173.

become more important[153], that inasmuch as the decisions taken by management are group decisions, the technostructure bans personal profit making[154].

Even if it is accepted that the motivation of a modern member of management differs from that of an old-style entrepreneur, it does not necessarily follow that the separation of ownership and control has resulted in a change of business behaviour. The assumption that such a change has occurred cannot be substantiated inasmuch as it rests, first, on an unproven assumption that as long as industry was controlled by owner-managers, all company decisions were dictated by the self-interest of the owner and, secondly, on the assumption that a change in personal motivation must necessarily lead to a change in corporate objectives. Both Wheelwright and Nichols point out that the suggestion that business behaviour has changed is unwarranted, and Wheelwright, considering the Australian evidence, concludes that it is more compatible with the theory that the managers now in power continue to pursue the interests of property than it is with the theory that a revolution in business behaviour has occurred[155]. It is highly possible that because management success will be judged in terms of whether or not traditional corporate profit and growth objectives are met, these objectives will continue to be pursued.

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153. Galbraith, *op cit*, 170.
154. Galbraith, *op cit*, as cited by Grossfield, *op cit*, 81.
155. Wheelwright, *"Introduction"*, *op cit*, xii-xiv.

2. MANAGERIALISM AS A LEGAL REFORM STRATEGY

Those managerialists who have given some thought to the implications of the theory for legal reform seem to belong almost exclusively to the non-sectarian school of managerial thought. They argue that, rather than seeking to curb managerial power, the reformist should seek to increase it. The theory is advanced that, while shareholders are interested only in profits and groups such as employees and consumers only in their own welfare, management is in a position to balance the claims of all groups dependent on the corporation[156]. A rejection of the arguments of non-sectarian managerialism will necessarily lead to a rejection of these arguments, while if it is accepted that, although managerial motivation is different, business behaviour has not changed, the strength of these arguments is diminished. Attempts to persuade management to change corporate behaviour are in the latter case an alternative to seeking to obtain non-capital representation.

Even if the premises of non-sectarian managerialism were granted, they would not necessarily require a redistribution of corporate decision-making power. Most managerialists would seek to insulate management decisions putting other interests ahead of shareholder demands from shareholder attack. Galbraith points out that the technostructure requires a high measure of autonomy:

> "It is vulnerable to any intervention by external authority, for, given the nature of the group decision-making and the problems being solved, such external authority will always be incompletely informed and hence arbitrary."[157]

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156. Manning, *Corporate Power and Individual Freedom, op cit,* 42; see also Eisenberg, *The Structure of the Corporation, op cit,* 25.
157. Galbraith, *op cit,* 91.

It is Galbraith's view that the corporation needs protection against intervention by the state and also against intervention by the stockholder[158]. However, he is of the opinion that to a large extent the present corporate structure provides the necessary protection against intervention by the shareholders[159].

In general, it has been said[160], managerialists tend to shy away from details at the level of execution. Such suggestions as have been offered were primarily palliative measures expressly designed to prevent dissatisfaction from forcing a change at a later stage[161]. For the most part these proposals were merely cosmetic and need not be noted.

Manning's proposal of a voteless model of the corporation is worth consideration, however, because he associated with it certain suggestions as to the direction which reformers could fruitfully pursue. As to the model itself, he was quick to point out that:

> "The model is not to be taken literally of course. Legally votable stock is in fact votable and the vote can, in some circumstances, make a difference."*162*

He favoured de-emphasis of the role of shareholder voting but not the scrapping of existing electoral machinery:

> "Although the proxy system of electing directors is largely an engine of, rather than for, management control, someone has to elect directors and there would be no advantage in permitting them overtly to choose their own successors."*163*

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158. Galbraith, *op cit*, 92. See also at 101: "The one thing worse than the loss of power by the small or passive stockholder would be its uninformed exercise."

159. Galbraith, *op cit*, 29, 98-99 and 101.

160. Eisenberg, *The Structure of the Corporation*, *op cit*, 21.

161. See for example Ruml, B., *"Corporate Management as a Locus of Power"* (1950-51) 29 Chi Kent L Rev 228. The policy behind his proposals is expressly stated at 245-246; see also Rostow, *op cit*, 59.

162. Manning, *Review*, *op cit*, 1493.

163. *Ibid*, 1494.

Manning's purpose in proposing the voteless model was to put the emphasis on a four-fold scheme to ensure managerial responsibility which omitted any mention of restructuring corporate meeting and electoral machinery. His programme called for, first, full and periodic disclosure to be made to the shareholders and perhaps to a judicial or other public agency; secondly, supervision of management in corporate matters affecting its own personal interest by some governmental or other machinery; thirdly, maintenance of avenues which will allow the individual shareholder to pull out of participation in the corporate venture; and fourthly, continuation or extension of the business judgment rule[164]. The utility of each of these four suggestions and also of efforts to restructure corporate meeting and electoral machinery are considered in Section F below. For the moment, it is sufficient to put forward the suggestion that a comprehensive approach to reform of company law will not neglect any reform that might possibly be useful.

The unsatisfactory nature of managerialism as a legal reform strategy may perhaps be explained by the fact that no one has yet satisfactorily explained why managements always or generally act in the public interest. In his article, *"Apologetics of Managerialism"*, Mason suggests that institutional stability and the opportunity for growth of an economic system are heavily dependent on the existence of a philosophy or ideology justifying the system in a manner generally acceptable to the leaders of thought in the community. This point is similar to the "City of God" notion discussed by Berle. Mason further contends that, whereas nineteenth century capitalism was such a philosophy, to date managerial

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164. Manning, *Review, op cit*, 1490; see also Eisenberg, *The Structure of the Corporation, op cit*, 28.

literature has not produced an equally satisfying ideology to explain twentieth century society despite the fact that enough has changed both in the social system and the techniques of thinking about it to make the classical apologetic quite unacceptable to twentieth century opinion. He advances three possible explanations for this failure of managerial economics. It may be, he states, that the economy is not as managerial as is supposed; or that the system is not sufficiently understood to explain why managements always or generally act in the public interest; or it may be that corporate managements do not always or generally behave in this manner[165].

Whatever the reasons, it is suggested that whereas managerialism as a socio-economic theory has convincingly pointed to certain differences between nineteenth and twentieth century society, managerialism as a legal reform strategy has failed to provide satisfactory solutions to the problems these changes present.

E. REPLACE THE GENERAL MEETING: TWO RADICAL SUGGESTIONS

Neither shareholder democracy nor managerialism is premised on the abolition of the general meeting or even on its partial replacement. The proponents of shareholder democracy, on the contrary, call for legal reform to strengthen the powers of the shareholders in general meeting. The managerialists argue that there is no need for any greater supervision of management than is currently provided. Both theories accept the basic corporate structure now in existence. To a greater or lesser

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165. Mason, E.S.,"*Apologetics of Managerialism*" (1958) 31 J Bus L 5-10.

extent the reverse is true of all proponents of non-capital representation and governmental interventionism. Because proponents of these theories call for a partial replacement of the general meeting, if not for its abolition, the theories can be classed together as radical strategies. These radical strategies are considered here because more and more attention is being paid to them. It appears that adoption of one or other of these strategies in some form may in the long run be the only satisfactory way to answer the problems posed by the evolution of the endocratic corporation.

1. NON-CAPITAL REPRESENTATION

The various suggestions that can be grouped together under this heading may also be categorized under the term "client-group participation" used by Eisenberg[166]. The common feature of all these proposals is the suggestion that some group dependent on the corporation for "fear or favour" but not currently represented in corporate councils be given a voice in the internal decision-making processes of the company. This category of proposals comprehends, but is not limited to, proposals for "industrial democracy", the suggestion that workers in the company's enterprise be given a formalized voice in the decision-making processes of the corporation through participatory or representative means[167]. It also includes proposals for giving consumers, franchise dealers or other groups affected by corporate conduct such a voice. In recent years, much work

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166. Eisenberg, *The Structure of the Corporation, op cit*, 19.
167. See Wood, R. (ed), *Proceedings of the International Conference on Industrial Democracy, Adelaide, South Australia*, (Sydney, CCH Australia Ltd, 1978); see also *Australian Financial Review*, Wednesday 1 August 1977, 25 where the ACTU Draft Policy on Industrial Democracy is printed.

has been done towards developing practical programmes for bringing industrial democracy into effect. The same is not true of suggestions which focus on other interest groups. However, as the purpose of this section is to consider the effect that such suggestions would have on the role of the general meeting in the corporate structure, it was deemed appropriate that all such proposals be considered together. This is not the place to discuss the details of any particular suggestion.

Suggestions for non-capital representation appear to have been prompted in the first place by a dissatisfaction with shareholder democracy. This dissatisfaction was coupled with an acceptance of the "democratic imperative", the concept that the solution for all problems of political (using that word in its widest sense) power is to make the governors responsible to the governed. Thus Chayes, an American academic who was an early proponent of non-capital representation in theoretical terms, presented the suggestion in the context of a criticism of shareholder democracy. He stated that it was unrealistic to rely on the shareholder constituency to keep corporate power responsible by the exercise of the franchise. Of all those standing in relation to the large corporation, the shareholder is, he states, the least subject to its power and consequently the shareholders are not the governed of the corporation whose consent must be sought[168]. He criticizes the concept of membership in the corporation which makes the word "member" analogous with the word "shareholder"[169]. In his view, "a more spacious conception of 'membership' and one closer to the facts of corporate life would include all

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168. Chayes, A., "The Modern Corporation and the Rule of Law" in Mason, E.S. (ed), *The Corporation in Modern Society*, (Cambridge, Harvard University Press, 1960) 25.

169. *Ibid*, 41.

those who have a relationship of sufficient intimacy with the corporation or subject to its power in a sufficiently specialized way"[170]. With respect, it is submitted that this statement raises more problems than it solves. What is a relationship of sufficient intimacy? Chayes admits the difficulty. Although it is not anticipated that great use will be made of the provision, it is of interest to note that British Columbia recently defined a member of the company for the purpose of an application for relief from oppression as including "any other person who in the discretion of the court is a proper person"[171]. This may constitute a step towards widening the concept of corporate membership as advocated by Chayes.

A necessary premise of the argument that provision should be made for non-capital representation is the proposition that corporations should be managed with a view not only to the interests of shareholders but also to the interests of such groups as company employees, customers, consumers, creditors, and co-habitants. This proposition, which is increasingly well-accepted[172], will be taken as established for the purposes of this discussion.

Given that non-capital interests deserve consideration, this consideration may be secured in a number of ways. It may be obtained by the exertion of economic power through the market mechanism, by the exercise of political power to gain governmental intervention, or by the provision of representative channels internal to the corporation itself. As

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170. Chayes, *op cit*, 41.
171. British Columbia Companies Act (1973) c 18 s 221 as amended by British Columbia Companies Act (Amendment) Act 1976 c 12 ss 44 and 45.
172. Conard, *Corporations in Perspective*, *op cit*, 365.

Conard points out,

> "if warring interests can be adjusted within the corporation's own governance structure, there are immense advantages for everyone. The lost income, the violence and the bitterness of strikes, the expense of litigation and the necrosis of government regulation, may all be minimized."*173*

But, he admits, these happy consequences will not necessarily flow from representation. Such representation may mean that the organization will be paralyzed by deadlock, or ruined by profligate decisions that make short-term accommodations at the cost of long-term insolvency. Conard recommends that experiments with non-capital representation should be made now so that these doubts may be resolved. In order to avoid deadlock, he further suggests that the experiments be launched with two non-capital groups rather than one*174*.

Not all commentators have displayed Conard's liberal attitude towards experimentation. R.N. Schwartz is of the view that:

> "Unless and until it is evident that management's accountability for the social consequences of corporate conduct is impossible without radical changes in the corporate electorate, the practical difficulties of bestowing the corporate franchise on these interest groups as well as the American disposition towards the resolution of interest group conflicts through adversarial procedures and negotiation, changes in market behaviour and litigation are compelling reasons for denying corporate affected constituencies access to the corporate franchise."*175*

It is submitted that Schwartz's attitude towards experimentation is to be preferred, at least where substantial changes in the statutes now in force would be necessary to permit such experimentation. Further, it

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173. Conard, *Corporations in Perspective, op cit*, 366.
174. *Idem*.
175. Schwartz, R.N., *op cit*, 1172.

must be noted that even some of those who are willing to move towards non-capital representation in the form of employee participation would find great difficulty with the suggestion that the said experiments should comprehend two non-capital groups[176]. Eisenberg's observation that the idea of direct participation by non-capital groups in corporate decision-making is susceptible of meaningful discussion only at the level of execution[177] is applicable to Conard's comments, and too much importance should not be attached to them.

Eisenberg takes the view that the American pre-occupation with democratic models of organization is responsible for suggestions that non-capital groups be granted a right to participate in corporate decision-making. He intimates that efforts to put such ideas into practice by force may well lead to conflict and frustrations[178], and supports this intimation by devoting some attention to the difficulties that are likely to be presented by any attempt to put the idea into execution. Among the difficulties which he suggests may arise are: (1) those given decision-making power are likely to lack necessary skills; (2) as giant corporations are also suppliers and consumers, the measure might work to increase their power; (3) there is no apparent way other than dollar-volume to allocate votes among the members of such groups; and (4) the interests of the client-group frequently conflict with those of the corporation. Eisenberg admits that when it comes to a question of the participation of labour, the problems are less severe, but he would nevertheless oppose this as well[179].

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176. Flynn, *op cit*, 107.
177. Eisenberg, *Structure, op cit*, 21.
178. *Ibid*, 24
179. *Ibid*, 21-23.

The Canadian Royal Commission on Corporate Concentration devoted some attention to the suggestion put forward by Chayes. It concluded that, in so far as any group but labour was concerned, non-capital representation was not feasible. Its reasons for this conclusion were that:

> "It is *never* easy to identify the appropriate constituencies and the appropriate institutional forms are *never* clearly definable. Even if it were possible to select special interest groups, balancing the extent of their participation relative to one another and to shareholders would inevitably be completely arbitrary."*180*

The Royal Commission equally rejected for the present the suggestion that the workers should be given the right to elect directors, although it acknowledged that this question was much more complex. The basis for this rejection was the fact that "neither Canadian labour nor Canadian management generally advocates or appears to support the idea"*181*.

Without venturing to make a submission as to whether or not non-capital representation should be adopted in Australia, it is relevant to note for the purposes of this thesis that the type of scheme put forward by the Bullock Report*182* does not encompass the abolition of the general meeting.

2. GOVERNMENTAL INTERVENTION

Proposals which call for governmental intervention in company affairs are numerous and wide-ranging, and it must be quickly made clear that it is not suggested that all of these proposals are radical. Proposals for

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180. Canada, *Report of the Royal Commission on Corporate Concentration, op cit*, 299

181. *Ibid*, 301.

182. Great Britain, Department of Trade, *Report of the Committee of Inquiry on Industrial Democracy*, (1977), hereinafter referred to as the *Bullock Report*.

governmental intervention which envisage that a governmental agency should take over some or all of the control functions of the general meeting are, however, properly categorized as radical. This sort of proposal is to be distinguished from the proposal that the state should take over the ownership function of the shareholders, which constitutes socialism. It is not intended in this discussion to canvass the merits or otherwise of socialism.

Governmental agencies have long been one of the most important of the external checks on management activity, and proposals that this role should be extended or strengthened are not radical. Nevertheless, it is considered appropriate to examine here certain of these proposals and the criticisms that may be levelled at them, because the same sort of criticism may also be brought against proposals that a governmental agency be given the power to intervene in company affairs at the internal level.

The power of the Australian Corporate Affairs Commissions to intervene in the internal affairs of companies is limited. The Commissions will police compliance with the formal requirements of the companies legislation and will investigate and prosecute charges that may be brought against companies, but they have no powers to go beyond the law and, for example, form and act upon an opinion that a proposal being put forward by management is unfair. The powers of the American Securities and Exchange Commission appear to be broader than those outlined. In the work on company law edited by De Hogton, the British reaction to the suggestion that a Securities and Exchange Commission be established in Britain is surveyed. It is admitted that there are advantages in using an existing body, but the present British system, in which the Board of Trade, the Stock Exchange, and the Registrar of Companies all have roles,

is described as "haphazard rather than flexible"[183]. The conclusion drawn is that

> "if Britain is not to have a Securities and Exchange Commission, there is certainly an argument in favour of combining or co-ordinating the work of these various bodies to prevent confusion and hardship through unnecessary duplication."[184]

This question of whether a body more nearly equivalent to the Securities and Exchange Commission should or must be established in Australia is discussed in the body of this thesis[185].

A proposal that was put forward in 1973 for a shareholder's tribunal in New South Wales deserves brief attention here. The proposal in question was put forward by F.J. Ryan, Commissioner for Corporate Affairs as he was then, in a Minute to the Attorney-General concerning the Alexander Barton group of companies[186]. It was submitted that:

> "the corporate system would be enhanced and the confidence of investors promoted if provision existed whereby directors could be called upon to justify their conduct before an independent authority."[187]

The system as envisaged would allow the authority, where it had grounds for believing that the directors were about to embark upon action which appeared to be contrary to the interests of shareholders, to apply for a temporary injunction, to receive the representations of the directors, and where appropriate to refer the matter to a court which would have wide powers to issue a perpetual injunction to restrain action on the

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183. De Hogton, *op cit*, 185.
184. *Ibid*, 185–186.
185. See Part VI.
186. New South Wales, Parliamentary Paper No 38 at 1973.
187. *Ibid*, 10.

proposal or to take steps to ensure that the shareholders were consulted[188]. The fact that an alternative for disposition of the matter would be to require the shareholders to be consulted makes it clear that it was not intended that the general meeting be displaced in authority.

Eisenberg considers that governmental review of structural proposals might be one method of ensuring that management is kept under control, but contends that this proposal has limitations inasmuch as governmental action is perceived as an inefficient tool which tends to be confined to a reviewing rather than an initiating function[189]. R.N. Schwartz expands the criticisms of government intervention:

> "Although government regulation has had a salutary impact in some instances, regulatory agencies have often fallen far short of fulfilling their congressional mandate. Government agencies have often become the pawns of those they were intended to regulate... . Moreover government regulation with its bureaucratic overlays frequently has the effect of reducing the efficiency of private industry by ensnaring it in costly, protracted administrative proceedings. Finally, government intervention is often contingent upon the occurrence of crises and rarely takes the form of ongoing supervision necessary to spot and resolve problems before they cause economic disasters. The government agency's response tends to come long after the time when effective standards of corporate conduct should have been put into practice... . Perhaps the best that can be said for government regulation as a vehicle for encouraging corporate accountability is that it certainly has a role to play, but exclusive reliance upon it would surely be misplaced."*190*

In France and Italy proposals have been put forward which would give a public or governmental agency the power to provide the control which shareholders no longer exercise[191]. Similarly, in the United States of

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188. New South Wales Parliament, Parliamentary Paper No 38 at 10.
189. Eisenberg, *Legal Roles*, *op cit*, 32.
190. Schwartz, R.N., *op cit*, 1144.
191. De Hogton, *op cit*, 188-189 and 195.

America, Stone proposes the establishment of two categories of public directorships[192]. General public directors would be appointed to the boards of large public corporations in numbers to be fixed according to a formula which calls for ten per cent of the directors to be so appointed for every billion dollars of assets or sales. Stone notes that if this formula, without any limitations, had been applied to American corporations in 1975, the boards of thirteen American corporations would have been entirely public directors[193]. He proposes that candidates for public directorships be nominated by a Federal Corporations Commission if and when such a body is established, and otherwise by the Securities and Exchange Commission. Each nominee would have to be approved by a majority of the board of the company involved and public directors would be removable by the company by a unanimous vote of the board without the necessity to show cause[194]. He insists that the functions of these public directors would have to be clearly spelled out and outlines eight possible functions. It is his position that:

> "If the *only* virtue of the general public directorship system was the symbolic one - a more obstrusive nagging reminder of these companies' obligations to society than the American flag over the plants - the system would, to my mind, have justified itself."[195]

In addition to general public directors, Stone proposes the appointment of special public directors in cases in which the forces of the market and ordinary legal mechanisms seem inadequate on their own to keep the

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192. Stone, C.D., *Where the Law Ends, the Social Control of Corporate Behaviour*, (New York, Harper & Row, 1975) chapters 15 and 16; see Hazen and Buckley, *op cit*, 117 *et seq*.
193. Stone, *op cit*, 138.
194. *Ibid*, 159.
195. *Ibid*, 174.

corporation within socially desirable bounds. The institution of special public directorships may be expected to be of assistance, he feels, in two situations, that is, in the "demonstrated delinquency situation and where there is a generic industry problem", such as pollution in the case of the paper-making industry[196].

The reaction to Stone's public directorship and similar proposals has to date been largely negative[197]. There are a number of reasons for this. First, it is felt that the public bureaucracy is an unreliable overseer of private bureaucracy. This feeling, and additional reasons for it inherent in the nature of bureaucracy as outlined by Weber, were stated by Levitt in his book, *The Third Sector: New Tactics for a Responsive Society*[198]. It is Levitt's contention that public criticism and threats to economic security thereby occasioned will best motivate both corporate and governmental bureaucracies to respond to social needs.

Another reason for the rejection of the alternative of governmental intervention is the feeling, which is prevalent in the United States of America and present to a lesser degree in other English-speaking countries, that individual responsibility and individual initiative ought to be utilized for the enforcement of the law rather than the courts and government agencies[199].

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196. Stone, *op cit*, 175.

197. De Mott, D., *"Management Structure and the Control of Corporate Information"* (Summer 1977) 41 Law and Contemp Probs 182; Nader, R., Green, M. and Seligman, J., *Taming the Giant Corporation*, (New York, W.W. Norton & Co Inc, 1976) 123-124.

198. Levitt, T., *The Third Sector: New Tactics for a Responsive Society*, (New York, AMACOM, 1973) 13, 14, 31-32.

199. Grossfield, *op cit*, 107; see for example Caplin, *op cit*, 686.

Grossfield and Ebke point out that:

> "The history of modern corporation law, particularly during the nineteenth century, shows very clearly how limited the possibilities of such general state control are."*200*

Further, it is submitted that the history of the Mercantile Bank affair in Victoria in the closing years of the nineteenth century*201*, and more recently in Britain, the history of Mr Moir's attempts to get governmental assistance in taking action against Dr Wallersteiner*202*, demonstrate that governments are not always quick to take action even when attention is called to a particular transgression.

In conclusion, it may be said that it does not appear likely that the general meeting will be denuded of its powers of controlling corporate management in the near future. Further, it is submitted that it is not desirable that this should be done. It is therefore necessary that all possible steps be taken to ensure that those powers are equal to the task set them.

F. TACTICS OF REFORM

The role of a strategy is to assist the leadership to decide what objectives to pursue and in what order of priority. When the objectives have been decided, the question of method or tactics arises. Choice of tactics may be influenced, but is not necessarily decided, by the overall strategy that is being pursued.

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200. Grossfield and Ebke, *op cit*, 427.
201. Gordon, M., *Sir Isaac Isaacs: A Life of Service*, (Melbourne, Heinemann, 1963) 60-71.
202. See *Wallersteiner* v *Moir (No 2)* [1975] 2 WLR 389, [1975] 1 All ER 849.

In the foregoing sections of this part, four possible reform strategies for dealing with the problem of keeping the powers of corporate management under control have been described. Proponents of each of these strategies have their own views of the correct and proper way to achieve the desired end, but it does not necessarily follow that they will disagree with the proponents of all other strategies when it comes to a choice of tactics. A proponent of shareholder democracy need not oppose the establishment of governmental agencies and can be expected to advocate both a widening of disclosure requirements and a restructuring of corporate meeting and electoral machinery. An advocate of non-capital representation would not be opposed to improving access to the courts in respect of company matters or to maintaining the stock market as a means of exit for the shareholder. In this section, a brief outline of five types of reform measure is offered for the purpose of attempting to indicate how proponents of each of the strategies outlined would regard them.

1. IMPROVING ACCESS TO THE COURTS

Attempts to remedy abuses of corporate and managerial power by resort to the courts have, in the past, been thwarted both by rules of procedure and by the courts' unwillingness to interfere with the exercise of the managerial function of assessing probabilities in the light of the facts known at the time and making decisions on this basis, that is, the exercise of "business judgment". Among the reform measures which have been advocated in the field of company law are revision of the procedural rules, scrapping of the business judgment rule and adoption of new laws to widen the scope of judicial review.

The rule in *Foss* v *Harbottle*[203] requires a shareholder to establish either that he has been personally injured by the action complained of or that exceptional circumstances exist which entitle the shareholder to bring an action in the name of the company[204]. This rule has thrown unnecessary difficulties in the way of a shareholder attempting to prevent or remedy an abuse of managerial power.

The Australian Law Reform Commission is now considering whether the introduction of class action rules on the American model is feasible or desirable in Australia[205], and similar proposals have been considered in South Australia[206]. If these rules are adopted, they will be of some relevance to controlling the abuse of power by corporate managements inasmuch as where a personal right exists in one shareholder it will usually exist in other shareholders as well and a class action will be available in which damages may be obtained. However, the adoption of class action rules will not change the substantive law or, without more, enable shareholders to sue where the wrong has been done to the company.

The innovations made by the English Court of Appeal in *Wallersteiner* v *Moir (No 2)*[207] in respect of the costs of a derivative action can be expected to assist where it can be established that standing exists to bring a derivative action. In that case it was held that a shareholder who sues in a derivative capacity could recover his costs from the company on a common fund basis and observations were made on the procedures

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203. (1843) 2 Hare 461, 67 ER 189.
204. See Ford, *op cit* [1411], see below 143-144
205. Australian Law Reform Commission, *Discussion Paper 16: Class Actions*.
206. Bentley, P., *South Australian Industrial Democracy, Past, Present and Future*, (Premier's Department, Unit for Industrial Democracy, Adelaide, 1977).
207. [1975] 2 WLR 389, [1975] 1 All ER 849.

to be followed where a shareholder wished to do so. In Canada, new statutory provisions have been adopted to govern derivative actions[208]. It seems to have been intended to make the rule in *Foss* v *Harbottle* obsolete[209], but in effect the provisions seem to do little more than allow for the recovery of costs of a derivative action. However, it may be noted that a rash of new decisions in the area has resulted from the new Canadian provisions[210], and the effect of these decisions is hard to assess in a few words.

In the nineteenth century, the courts proclaimed that they would not interfere with the business judgment of corporate management. This attitude has continued to play a role in making abuses of managerial power difficult to attack through the courts. Writing in 1958, Manning, speaking for the managerialists, advocated the retention and extension of the business judgment rule[211]. However, in the intervening twenty years, Commonwealth courts, at least, appear to have moved in the opposite direction. Cases in which the courts have examined the merits of what is arguably a business judgment include *Harlowe's Nominees Pty Ltd* v *Woodside (Lakes Entrance) Oil Co NL*[212], *Ampol Petroleum Ltd* v *R.W. Miller (Holdings) Ltd*[213] and *Clemens* v *Clemens*[214]. However, a

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208. Can Bus Corp Act ss 232 and 233; Bus Corp Act (Ont) s 99.

209. Dickerson, R.W.V., Howard, J.L. and Getz, L., *Proposals for a New Business Corporations Law for Canada*, (Ottawa, 1971) paras 487-489; Ontario Legislative Assembly, *1967 Interim Report of the Select Committee on Company Law*, c 7.3, 55-61, hereinafter referred to as the *Lawrence Report*.

210. Ahmad, S.U., *"Disentanglement of Shareholder's Personal Action from Derivative Action - Recent Canadian Experience"* (1975-76) 1 UNSW LJ 264.

211. See above, 48.

212. (1968) 121 CLR 483.

213. [1972] 2 NSWLR 860 per Street J, but see *Howard Smith* v *Ampol Petroleum Ltd* [1974] AC 821.

214. [1976] 2 All ER 268.

recent conference in the United States saw a discussion of the business judgment rule which reversed the tendency towards discrediting the rule[215].

While Manning, speaking for the managerialists, would deprecate the disappearance of the business judgment rule, he placed some importance on assuring that shareholders had access to the courts and would therefore, it appears, welcome the changes in the procedural rules. Those who advocate shareholder democracy would welcome both reforms even though in some isolated instances they may feel that a particular question should have been decided by the general meeting rather than the court[216]. On the whole, those who believe that the individual shareholder can and should play a role in the life of the company would agree that access to the courts is an important and necessary protection for the shareholder who has been unjustly deprived of such a role by management. Those radicals who advocate replacing the general meeting argue that the shareholder's remedy lies either in the courts or in the stock market and would therefore support reforms that improve shareholder access to the courts.

2. ESTABLISHING SUPERVISORY AGENCIES

Although certain objections to placing too much reliance on governmental regulation and the supervisory agency have been canvassed above, it must not be forgotten that the Securities and Exchange Commission has played

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215. SRLR 530 (11.28.79) A1 reporting on the PLI Eleventh Annual Institute on Securities Regulation Conference.

216. Gilbert, *op cit*, 174.

an important role in promoting shareholder democracy in the United States. It may thus be seen that rejecting government intervention as the final and complete answer to problems of corporate and managerial power is not inconsistent with advocating the establishment of a governmental agency to supervise various aspects of corporate life. Neither managerialists nor proponents of shareholder democracy would find any insuperable objection to the idea that such an agency should be established, while proponents of both radical suggestions might be expected to be even readier to adopt such an idea.

3. MAINTAINING AN OUT: THE STOCK MARKET

> "One of the most effective external means of keeping corporate power within socially tolerable limits is an active, dynamic market that is free from restraints."[217]

Managerialists, together with proponents of both radical strategies, will naturally attach a greater importance to the stock market *vis a vis* the general meeting as a device for protecting the interests of the shareholder-investor than will the proponent of shareholder democracy. It is submitted, however, that this is because the others downgrade the importance of the general meeting rather than because the proponents of shareholder democracy under-estimate the value of the stock market. Although proponents of shareholder democracy do maintain that the stock market is not a complete answer to problems of corporate control, they would not advise its abolition. The converse suggestion has, however, been made[218]. Before the practicability of the suggestion is evaluated, some attempt must be made to understand the complex inter-relationship of the two institutions.

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217. Grossfield and Ebke, *op cit*, 425.
218. Manning, *Review*, *op cit*.

In Hetherington's analysis[219] as summarized and discussed by Grossfield[220], the impact of the stock market on corporate control is twofold. In the first place, the existence of the stock market can cause a diminution of shareholder control because it encourages the shareholder to leave the company rather than to utilize intra-corporate mechanisms to change the company. But on the other hand, the stock market can serve as a means of effecting control over management. If a large number of shareholders becomes dissatisfied and attempts to sell their shares, the market price will tend to drop. This will enhance the difficulty of attracting new capital and will adversely affect management morale. At the same time it exposes the corporation's management to the dangers associated with a takeover[221].

Both the mechanisms of the stock market and of the general meeting must be successfully employed before a takeover can be accomplished. The contemplation of the process shows that the institutions are complementary and enhance the value of each other.

Manne has stated that "the corporate system of allowing the sale of votes guarantees an electorate that is both relatively well informed and more intensely interested in the outcome of the election than would be the case if votes were not transferable"[222], while Hetherington takes the position that the fact that the corporate electoral procedures make it possible to challenge management, even if this happens infrequently, is a "principal if not a sufficient justification" for their preservation[223].

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219. Hetherington, *op cit*, 269–270.
220. Grossfield, *op cit*, 83–85.
221. Hetherington, *op cit*, 269–270.
222. Manne, *op cit*, 1144.
223. Hetherington, *op cit*, 270.

Emerson and Latcham marshalled other arguments to support the conclusion that the existence of the stock market was not in itself a complete answer to problems of corporate control. They pointed to the fact that, in selling shares, a shareholder will often have to sell at a loss which he has had little or no opportunity to prevent, that the corporation and society itself may suffer great loss which might have been prevented had it been possible to take action immediately, and that it has not yet been demonstrated that market prices bear a sufficiently close relationship to the effectiveness of the corporation as an economic unit[224]. Grossfield and Ebke endorse the proposition that the stock market alone does not provide sufficient protection fot the investor on the basis that it acts solely as a loose, indirect control and is at best only a means of protection against very grave abuses and managerial incompetence[225].

Before leaving this area, attention may be directed briefly to Hirschman's study of the function of "exit" and "voice" as reactions to decline in organizational performance[226]. Hirschman analyses in general terms the factors which tend to cause the dissatisfied member to leave the organization or to attempt to reform it from within by use of such democratic machinery as may have been provided, and the factors which will tend to make organizations more sensitive to one or other of the reaction mechanisms. He points out that there are certain perverse cases in which those who are dissatisfied will tend to vent their feelings in a way to which management is relatively indifferent. Hirschman categorizes corporation-shareholder relations in large corporations as one of these

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224. Emerson and Latcham, *op cit*, 151.
225. Grossfield and Ebke, *op cit*, 426.
226. Hirschman, A.O., *Exit, Voice and Loyalty*, (Cambridge, Harvard University Press, 1970).

perverse cases but does not further discuss the large corporation even in general terms[227]. He states that where one mode of reaction is favoured over another, management efforts will be directed to minimizing its effects while simultaneously members, by relying increasingly on it, will let the mechanisms appropriate to the other mode of reaction atrophy to the point where the effectiveness of the less familiar mode becomes not only more uncertain but tends to be increasingly under-estimated[228]. It appears that this may be what was happening in the case of the corporation until the emergence of the ethical investor movement.

It is Hirschman's conclusion that "in order to retain their ability to fight deterioration those organizations that rely primarily on one of the two reaction mechanisms need an occasional injection of the other. Other organizations may have to go through regular cycles in which exit and voice alternate as principal actors, while in those organizations in which both exit and voice must be maintained in good health an awareness of the instability of the optimal mix is necessary"[229]. It is suggested that these remarks are instructive regardless of which category one considers that the company falls into.

The stock market, inasmuch as it provides an "out" for the shareholder, and the general meeting, which provides a "voice" or speaking platform for the shareholder, are complementary alternatives. There is another sense in which the stock market complements the controls imposed on management by the articles and company law. The Stock Exchange Listing Requirements have an appreciable influence on the behaviour of corporate

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227. Hirschman, *op cit*, 122.
228. *Ibid*, 124–125.
229. *Ibid*, 126.

management, but this influence is discussed elsewhere in this thesis.

4. WIDENING DISCLOSURE REQUIREMENTS

> "In this century there has been a continuous development of legislation designed to perfect the machinery of administration and control of the company. In particular there has been an extension of the information that is to be made available to shareholders and creditors and to the public generally, especially by way of prospectuses and accounts."[230]

So said the Victorian Attorney-General when introducing the Bill that was to become the precursor of the Uniform Companies Act. In the New South Wales Legislative Assembly three years later, the comment was made of the Act that it

> "recognizes more fully than has ever been done in the history of company legislation in this state the fact that shareholders own their companies and that, as owners, they are entitled to have full information concerning the management of these companies"

subject only to the qualification that disclosure which would only benefit competitors should not be required[231].

A great deal has been written about disclosure of corporate information and it is not possible to cover the issues fully here, but reference should be made to the work done in the area by the recent Canadian Royal Commission on Corporate Concentration[232]. The report summarizes the various disclosure and reporting requirements to which Canadian corporations were then subject before turning to examine the arguments

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230. Victoria, Parliamentary Debates V 255 318 (9 September 1958), Mr Rylah, Attorney-General.
231. New South Wales Parliamentary Debates Session 1961-1962, Legislative Assembly 2869-2870.
232. Canada, *Report of the Royal Commission on Corporate Concentration*, *op cit*, 311-336.

for and against more disclosure. The Commission concluded that "the public does have a right to know more than it does now", but as well that "many of the present disclosure requirements should be clarified and simplified"[233]. Remarking that most of the corporate information currently available is linked to the processes of the capital markets, it recommended that large enterprises should focus their disclosure policy on making information available to the public in general[234].

The recommendations of the Canadian Royal Commission would be welcomed by the proponents of non-capital representation in particular. But proponents of all the schools of thought outlined above would agree that greater and better disclosure would tend to prevent corporate abuses although they might then disagree as to what should be disclosed to whom and in what format.

Governmental interventionists would naturally tend to argue that information should be disclosed to the government or its agencies and might tend to rely on regulation to lay down the content and format of required disclosure.

Proponents of non-capital representation would argue for disclosure to all interest groups, including labour, consumer and similar groups but not excluding shareholders, of a wide range of information both financial and otherwise.

Managerialism as represented by Manning advocates disclosure but with the reservation that it should not be action-orientated. He admits that

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233. Canada, *Report of the Royal Commission on Corporate Concentration, op cit*, 322.
234. *Idem*.

disclosure requirements have historically been linked to shareholder voting[235], but expresses the view that this is no more than a convenience[236]. Eisenberg, however, expresses the contrary view that disclosure, without more, has a disembodied quality. He states that

> "if disclosure is to be relied upon as a primary tool it should be action-oriented disclosure, disclosure required in connection with an approval to be sought ...even if the approval will be granted more or less *pro forma* simply because men have a different attitude when they must seek approval."[237]

Eisenberg's views are here respectfully adopted.

Proponents of shareholder democracy maintain that the shareholder has a right to information about his company and support the requirement that the company issue an annual report as well as arguing that the shareholder has a right to ask questions and to have his questions answered[238]. It is suggested that inasmuch as it is sometimes difficult to foresee when laying down general requirements what specific information will be wanted in a particular situation, the right to ask questions is a valuable addition to the battery of disclosure requirements which may be made by shareholder democracy.

5. RESTRUCTURING THE CORPORATE GENERAL MEETING AND PROXY SYSTEM

This particular tactic in the field of company law reform has little or no appeal to anyone who does not adhere to the ideals of shareholder

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235. Manning, *Review*, *op cit*, 1494.
236. *Ibid*, 1487
237. Eisenberg, *Structure*, *op cit*, 33.
238. Gilbert, *op cit*, 37,206.

democracy. Proponents of shareholder democracy in the United States of America have, however, put forward a variety of suggestions as to how the general meeting and particularly the proxy system could be remodelled so as to enable minority shareholders to participate more meaningfully in the corporate decision-making process. It is suggested that so long as the general meeting retains its role in the company structure, it is desirable to ensure at the very least that the law does not enhance management control of the company by the provisions that are made for convocation, notice and electoral procedures.

G. CONCLUSION AND PREVIEW

This introduction has attempted to outline the two major problems portrayed by modern company law commentators, that is, the problem of the company's enlarged power in society and of management's enlarged power within the company. These problems, although linked, are not identical and the focus in this thesis will be primarily on the problem of how to make company management accountable. Four strategies of corporate reform were described. These were shareholder democracy, managerialism, non-capital representation, and government interventionism. The feature which distinguishes these strategies is the place assigned by each to the general meeting in the corporate structure. Finally, an attempt was made to state how proponents of each strategy would utilize five types of reform tactic.

It is suggested that regardless of any views that might be taken as to the relative merits of the four reform strategies described, it would be unrealistic to look for the abolition of the general meeting in even the largest companies, at any rate within the foreseeable future. Further,

it is suggested that the role of the general meeting in the middle-range company is and will continue to be influential and that despite any opinion to the contrary, shareholder democracy has a contribution to make to the reform of the law as it affects these companies. This is the basis on which this thesis will proceed.

Part II of the thesis explores the division of powers between the board of directors and the general meeting and is for the most part declaratory of the law as it currently stands in Australia and Britain. The American concept of proper subject, which was developed under the aegis of the Securities and Exchange Commission's proxy rules is, however, introduced and considered in this part on the basis that its adoption broadened the range of matters that could be considered by the general meeting and thus affected its powers. It is suggested that a similar development would be appropriate in Australia.

Part III examines the distribution of voting rights in the general meeting and focuses in particular on the one share one vote model, a suggestion which may perhaps be regarded as quixotic is made to the effect that limited proportional voting still has features which would recommend it. This part concludes with a brief survey of devices for separating ownership and control and the recommendation that the adoption of provisions regulating shareholder agreements should be considered.

Parts IV and V of the thesis are devoted respectively to a consideration of the law as regards convocation of meetings and notice requirements. In these parts a close comparison of the Australian and British provisions with the provisions contained in the American Model Business Corporations Act, the Canada Business Corporations Act and the Business Corporations Act of Ontario is made. Because the Canadian statutes were so recently adopted and because there are several significant points of

difference between the American and the Anglo-Australian practice, it was considered that such a comparison would be valuable.

The sixth and final section is devoted to a consideration of the law as it affects proxy voting. Again this part features a comparison of the North American provisions with the Anglo-Australian, but an attempt has also been made to place the right to vote by proxy in historical context and to examine in detail the proxy voting machinery currently in force in Australia.

This thesis constitutes an attempt to canvass and assess the contribution which shareholder democracy has to make to that part of company law which deals with the role and machinery of the general meeting. No attempt is made to assess the contribution of shareholder democracy to the theory and development of other corporate reform tactics. Nor are all the aspects of the procedures of the general meeting explored. To sum up the argument of this thesis in one sentence: It is suggested that the proponents of shareholder democracy in North America have effected some changes in the law as it affects general meetings of company shareholders and have suggested other changes which could and should be considered in Australia.

PART II DIVISION OF POWERS BETWEEN THE BOARD OF DIRECTORS AND THE GENERAL MEETING

A. THE SIGNIFICANCE OF THE DIVISION

The division of powers between the board of directors and the general meeting of the company is effected by the companies legislation and the company's memorandum and articles, but interpretation of their provisions is subject to the influence of a large body of case law. On a broader level, the allocation of specific powers reflects the basic theory of the corporate structure. This part of the thesis explores the division of powers between the board and the general meeting in an attempt to demonstrate the role of the general meeting in the corporation.

In the course of this exploration it will become evident that while "control" of a company or corporation is, by definition, vested in the shareholder who holds a majority of voting rights in the general meeting[1], this does not mean that he controls the activities of the corporation. It is necessary to distinguish between control of the company by which is meant the possession of the ultimate power to hire and fire the directors and to alter the company's constitution and control of the day to day affairs of the company. The board of directors, under the articles in force in most companies today, is charged with management of the business of the company[2]. In construing this provision the distinction between matters of management and matters

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1. *Mendes* v *Commissioner of Probate Duties (Vic)* (1967) 122 CLR 152; see also *Barclay's Bank Ltd* v *Inland Revenue Commissioners* [1961] AC 509; *Inland Revenue Commissioners* v *J. Bibby & Sons Ltd* [1945] 1 All ER 667. For further discussion see Part III.
2. UCA Fourth schedule Table A reg 73.

of policy has not been clearly drawn. It is suggested that the general meeting's powers should be redefined in order to establish clearly that it has jurisdiction to consider matters of policy. Such a redefinition seems to have been achieved under the rules defining proper subject promulgated by the American Securities and Exchange Commission in connection with its proxy solicitation regime. The final section of this part of the thesis will therefore be devoted to an examination of those rules.

1. THE EXPECTATIONS OF THE SHAREHOLDERS

Which powers do shareholders expect to exercise? This query is relevant because if shareholders generally are given more and greater powers than the average shareholder expects to exercise, many of these powers will atrophy. Unfortunately there is little factual evidence relevant to answering this question.

Eisenberg[3], a leading American commentator, offers an analysis of four factors which he claims are relevant to a hypothesis as to the matters share owners might expect to decide. First, he suggests that the extent to which the matter requires skills of a specifically business nature as opposed to financial orientated enterprise evaluation or investment skills will be relevant. The greater the need for the latter the more likely it would be that the share owners would expect to make the decision. The second factor which he considers relevant is the economic significance of the matter. The greater the economic significance the

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3. Eisenberg, M.A., *The Structure of the Corporation*, (Boston, Little Brown and Company, 1976), hereinafter referred to as *Structure;* see also Eisenberg, M.A.,*"Legal Roles of Shareholders and Management in Modern Corporate Decisionmaking"* (1969) 57 Calif L Rev 1, hereinafter referred to as *Legal Roles;* and Iaccobucci, F., Pilkington, M.L. and Pritchard, J.R.S., *Canadian Business Corporations*, (Agincourt, Ontario, Canada Law Books Ltd, 1977) 135, 145.

more likely it is that the owners will seek to decide the matter. The third factor he lists is the frequency with which the decision arises to be made. Decisions needing to be made frequently are more likely to be left to the management. Finally, he considers that the speed with which the matter must be decided is relevant. Where the need for speed is great, there will be another argument for leaving the matter to management[4].

Taking these factors into account, Eisenberg constructs a normative model of decision-making power in the close corporation by placing the kinds of decisions which arise in a business enterprise into four general categories: business decisions in and out of the ordinary course; decisions involving a substantial change in the structure of the enterprise; and decisions relating to the control structure of the corporation[5]. He concludes that decisions in the first category should be left to management because of the primary relevance of business skills and the frequency with which they arise. Decisions in the second category he would leave to management but subject to shareholder intervention because these decisions may have a large significance economically and, arising infrequently, may have a continuing impact. Decisions in the last two categories should, he insists, be for the shareholders themselves[6]. However, he does not address the question of the degree of shareholder agreement which should be necessary in each case. Another commentator suggests, using the partnership analogy, that majority decisions should prevail in the second category while an extraordinary majority should be required for structural changes[7].

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4. Eisenberg, *Structure, op cit,* 13; Iaccobucci *et al, op cit,* 136-137.
5. Eisenberg, *Structure, op cit,* 13.
6. *Ibid,* 16.
7. Iaccobucci *et al, op cit,* 138.

More controversial are Eisenberg's conclusions as to the expectations of shareholders in publicly held corporations. Most commentators, he points out, when discussing shareholder expectations from this perspective, have assumed that shareholdings in such companies will be atomistically dispersed and on that basis have argued that shareholders today have no interest in participating in structural decisions[8]. Eisenberg assumes that the extent to which a shareholder in such a corporation is interested in, and expects to participate in, structural decisions is intimately related to the size of his shareholding[9], and proceeds to analyse in detail the data as to the average number of shareholders in public corporations and the concentration of stockholdings in the United States. He concludes that most of the stock in any given publicly held corporation is in the hands of a relatively small number of sophisticated holders who know how to interpret financial data and can be expected to have a strong interest in structural changes[10], and notes parenthetically that the fact that shareholders with very small holdings lack this interest is yet to be proved[11]. On this basis and in the light of the need for a check on managerial self-interest and inefficiency, he concludes that the rules governing the allocation of decision-making power in public corporations should differ from those governing closely held corporations only in two respects. First, in publicly held corporations all business decisions should be solely for management; secondly, in the public corporation

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8. Eisenberg, *Structure, op cit* citing Chayes, "The Modern Corporation and the Rule of Law" in Mason, E.S. (ed), *The Corporation in Modern Society*, (1959) and Hornstein, G., *"Corporate Control and Private Property Rules"* (1943) 92 U Pa L Rev 1, 3.
9. Eisenberg, *Structure, op cit*, 37.
10. *Ibid*, 65.
11. *Ibid*, 65, n 1.

the decision-making rules should be mandatory while in the close corporation such rules should apply only where there is no contrary shareholder agreement[12].

Although studies[13] have been done of patterns of share ownership in Australia, the findings are not reported in forms directly comparable with the statistics Eisenberg quotes[14]. The conclusion, drawn by all the studies, that ownership of shares in Australian companies is highly concentrated[15], is sufficient to make Eisenberg's arguments applicable.

If additional evidence is sought to rebut the suggestion that shareholders neither expect nor desire to exercise, through the general meeting, powers any broader than those they now have, the writer can point to a number of instances reported in the Sydney newspapers in 1978 where shareholders as such manifested an interest in the concerns of their company broader than that they are sometimes supposed to feel. A shareholder in James Hardie Asbestos Ltd is reported to have raised the question of a lump sum payment to the widow of an employee who died from asbestosis contracted in the course of his employment[16]; shareholders of Queensland Mines Ltd demonstrated concern about the development of uranium mining from an environmentalist viewpoint[17]; and a shareholder in Tooth's brewery was concerned with management policy on retail outlets[18]. As to the results of these demonstrations

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12. Eisenberg, *Structure, op cit*, 68.
13. Wheelwright, E.L., *Ownership and Control of Australian Companies*, (Sydney, Law Book Co, 1957); Wheelwright, E.L. and Miskelly, J. *Anatomy of Australian Manufacturing Industry*, (Sydney, Law Book Co, 1967); Lawriwsky, M., *Ownership and Control of Australian Corporations*, (Transnational Corporations Research Project, University of Sydney, 1978).
14. For example, Lawriwsky, *op cit*, 11-18 discusses the twenty largest cohesive groups of shareholders while Eisenberg, *Structure, op cit*, 45-53 discusses the thirty largest shareholders.
15. Lawriwsky, *op cit*, 30.
16. *Sydney Morning Herald*, Friday 28 July 1978, 13.
17. *Sydney Morning Herald*, Thursday 25 May 1978, 17
18. *Sydney Morning Herald*, Friday 7 July 1978, 11.

of concern, the shareholder in James Hardie Asbestos Ltd failed to have his resolution accepted for consideration, the Queensland Mines Ltd meeting was disrupted but the environmentalists secured a hearing, while the shareholder who had nominated for a directorship in Tooth's withdrew because the board had proved receptive to his views. The fact that in certain cases individual shareholders display an interest in matters of policy is not, however, conclusive.

The potential significance of a high concentration of ownership for the distribution of power inside the corporate complex is twofold. While it may mean that the "average shareholder" who owns only a microscopic amount of stock will be so heavily outvoted as to make his voting rights virtually meaningless, it will also mean that in each company there will be shareholders with sizable blocks of shares who may be expected to have an interest in corporate decisions[19]. Although such shareholders may be able to exert pressure on management through informal channels, this is not an argument for abolishing a formal channel for allowing them a voice in corporate decisions. Following Eisenberg's reasoning, which is respectfully adopted here, shareholders in public as in proprietary companies should be empowered to make all structural decisions affecting the company[20].

19. Eisenberg, *Structure, op cit*, 65-66.
20. See also Iaccobucci *et al, op cit*, 144 n 3.

2. THE CORPORATE STRUCTURE

(a) Under the Companies Legislation

Under Anglo-Australian law, the corporate structure consists of two major component parts, the general meeting and the board of directors. On registration the subscribers to the memorandum of the company together with such other persons as may become members of the company shall, the Act states, be a body corporate able to carry on business as such[21]. This provision which provides for one "body" cannot, however, be read alone. The Act also requires that each company shall have a number of directors[22] and requires every company to hold periodic general meetings[23]. A general meeting of the company is a meeting of the members or shareholders of a company which is called to transact company business. Every member of the company who enjoys voting rights has a right to attend the general meeting. Although statute and the Table A articles make no reference as such to the board of directors it is clear that when a duty is imposed on "the directors" as a body they are required to act collectively as a "board" at meetings which must be attended by a quorum of directors. Two corporate organs are thus called into existence by the companies legislation. The Act stipulates that certain powers be reserved to the company in general meeting[24] but otherwise leaves the question of the division of powers between the general meeting and the board of directors of the company to be settled by the company's constitution.

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21. UCA s 16(4).
22. UCA s 114(1).
23. UCA s 136(1).
24. See for example UCA ss 28, 31, 92, 120, 166(3) and 166B.

If the companies legislation did not specifically call into being the two corporate organs referred to above it would be necessary to make provision in the company's constitution for some allocation of powers to committees of the company's members or of appointees of the members. It would be impracticable to try to consult each individual member about every company decision.

It has been held by the courts that a company is an abstraction having no mind or body of its own. It follows, therefore, that its powers must be exercised through some person or persons who, though they may be called agents, in fact represent the company directly. This doctrine, the "organic theory" first laid down in *Lennard's Carrying Co Ltd* v *Asiatic Petroleum Co Ltd*[25] , has subsequently been developed in cases considering the criminal liability of corporations[26]. However, inasmuch as this body of law governing the external relations of companies has apparently developed entirely independently of the law as to internal relationships[27] with which this thesis is concerned, this line of authority is not pursued.

It may be noted at this point that while Anglo-Australian legal writers talk of dyarchies[28] and focus on but two centres of corporate powers, American writers are discussing a tripartite division of powers between the general meeting, the board of directors and the corporate executive[29]. While it would seem that further attention should be paid

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25. [1915] AC 705, 713.
26. See *Tesco Supermarkets Ltd* v *Nattrass* [1972] AC 153; *H.L. Bolton (Engineering) Co Ltd* v *T.J. Graham & Sons Ltd* [1957] 1 QB 159.
27. Gower, L.C.B., *Principles of Modern Company Law*, 3rd ed (London, Stevens & Sons, 1969).
28. Ford, H.A.J., *Principles of Company Law*, (Sydney, Butterworths, 1974) [1408].
29. Cary, W.L., *Cases and Materials on Corporations*, 4th ed (Mineola, New York, The Foundation Press Inc, 1969)150; Ratner, D.L., *Book Review: The Structure of the Corporation* (1976) 64 Cal L Rev 1484.

to the division of powers between the corporate executive and the board of directors in the Anglo-Australian context, it is submitted that this question is of little or no relevance to the powers of the general meeting as the powers enjoyed by corporate executives under the Australian legislation are derived from the board of directors by delegation. Indeed, the Uniform Companies Act largely ignores the existence of the corporate executive. The exceptions to the rule are the mention in the penal provisions of "corporate officers"[30] and the inclusion in the Table A regulations of provisions allowing the board to delegate its powers[31] and to appoint a managing director[32]. This thesis, following the practice of the Australian legislation, will not give separate consideration to the power of the corporate executive.

(b) The Relevance of the Table A Articles

In contrast to the position in the United States of America where the statutes stipulate that "the business of the company shall be managed by the directors"[33], Anglo-Australian companies acts give the company promoters complete flexibility to divide company powers between the two corporate organs as they see fit. The statutes require that there be directors, but so long as these directors have the minimal powers necessary for the performance of their statutory duties the requirements of the legislation will be met.

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30. See for example UCA ss 44(7), 50(2), 54(7) and 58(5).
31. UCA Fourth sched Table A reg 86.
32. UCA Fourth sched Table A reg 91.
33. Mod Bus Corp Act Ann 2d s 35.

Although there is no statistical basis for the statement, corporators rarely appear to avail themselves of the ability to distribute company powers as they will. The provisions of the Table A articles on this subject are usually adopted unchanged in drafting the individual company's constitutive documents[34]. When discussing the details of the division of power in Section D below, this paper will be confined to a discussion of the statutory provisions and the provisions of the Table A articles and no specific mention will be made of other possible provisions. However, the fact that the company is completely free to adopt any articles it chooses must not be forgotten.

The company is free to adopt articles conferring wide powers on the board of directors and in construing these articles the modern court will not be guided by any *a priori* assumption that the board's powers are subordinate to those of the general meeting[35]. This was not always the case as, at one stage, the courts required very clear words to displace such an assumption[36]. Today, even the exponents of the widest view of the powers of the general meeting do not attempt to maintain this proposition[37]. If anything, the current view is moving to the opposite extreme of assuming that there is no intention to limit the powers of the board of directors. The point is further developed below.

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34. Sullivan, G.R., *"The Relationship between the Board of Directors and the General Meeting in Limited Companies"* (1977) 93 LQR 569; Gower, *op cit*, 132 n 27; Goldberg, G.B., *"Article 80 of Table A of the Companies Act, 1948"* (1970) 33 Mod L Rev 177; Hornsey, G., *"Aspects of Law Relating to Company Control"* (1950) 13 Mod L Rev 470.
35. *Scott* v *Scott* [1943] 1 All ER 582.
36. See for example *Wilkins* v *Roebuck* (1858) 4 Drew 281, 62 ER 109; *City Bank* v *Australian Paper Co* (1871) 10 NSWSCR 235.
37. Sullivan, *op cit;* Goldberg, *op cit;* These authors may be categorized as exponents of the widest view of the powers of the general meeting because they argue that the proviso to article 73, UCA is effective to allow the general meeting to give directions to the board of directors, a view not commonly held.

B. THE HISTORICAL AND THEORETICAL BACKGROUND

1. OUTLINE OF GROUP THEORY

A group, as defined by Stoljar, is differentiated from a mere aggregate by the fact that interactions within it take place in a certain manner. That is, interaction is confined to specified or specifiable persons and assumes that certain purposes or tasks are to be performed or pursued by regular methods according to common standards[38]. Where a group or association such as a partnership or company is formed for the purpose of trading in search of a profit, the persons who so combine may contribute materially to form a joint fund or estate. When such a joint fund or estate is formed, the individual contributor necessarily forfeits some measure of control over the property that he so contributes. The joint fund is to be used only for the purposes of the group; certain members of the group are given authority to bind the group[39]. In an ordinary partnership each individual partner will have such authority but by agreement among the parties the number of members so authorized may be restricted. In return for forfeiting sole control over the property he contributes to the joint fund, each contributer is recognized to have an interest over the whole stock, thus when decisions concerning the joint fund are to be made each contributor will have a right to some voice in shaping that decision[40]. Where the number of individuals is small, it may be practicable to require unanimity on all major decisions and this, subject to contrary agreement, is the rule governing partnerships.

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38. Stoljar, S.J., *Groups and Entities*, (Canberra, ANU Press, 1973) 6.
39. *Ibid*, 78.
40. *Ibid*, 79; Ford, *op cit*, [1403].

However, when the number of individuals concerned expands, it becomes less practical to require unanimity. Where unanimity is required and the group is unable to reach agreement, no action may be taken by the group. Where a deadlock arises which proves incapable of resolution, it may be necessary to dissolve the group. Alternatively, where the members feel that this is undesirable and that the common purpose outweighs the problem in dispute, they may agree to substitute for the rule requiring unanimity an agreement to abide by the joint decision of some number of members that is less than the total number[41]. This may be done voluntarily when actual disagreements eventuate or may be the subject of a stipulation embodied in the agreement setting up the association.

In the larger group or corporation, it will be necessary to adopt the principle of majority rule as a compulsory feature of the group organization in order to ensure a reasonable life expectancy for the group. This may be done contractually when each member joining the group expressly binds himself by a promise to abide by majority decisions or, independently of individual agreement, by imposition from without under the operation of the general law or statute. Majority rule has long been a feature of corporation law. The courts, to ensure that public corporations would endure longer than a night and a day, held that by the act of joining such an organization a member agrees to majority rule, and implied this term into the corporate constitution[42].

As an alternative to adopting a majority rule principle, power may be withdrawn from the body of individual members and transferred to an agency that will thenceforth make decisions for the group. Weber states

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41. Stoljar, *op cit*, 39.
42. *Chamberlain of London* (1391) 5 Co Rep at f 639; see also *Mayor of Norwich* (1481) YB 21, Edw 4 Fol 67-70 cited by Stoljar, *op cit*, 132-133.

that the centralization of power in such an agency is a definitive characteristic of a corporate body[43]. Authority may be transferred to such an agency voluntarily or the arrangement can be set up from outside the organization. When the disposition of power is dependent upon a voluntary agreement among the members it is properly styled a "delegation" and may be reversible. When centralization is imposed from without the use of the term "delegation" is inappropriate and no quest question of reversing the process can arise within the group. Both the majority rule principle and the principle of central authority have an indisputable role to play in the structure of the modern registered company. However, the question of which powers are governed by which principle is not so easily settled. Further, a question arises as to whether the board's powers are derived from delegation by the general meeting or are conferred on it at the same time as other powers are conferred on the general meeting so that the bodies are co-ordinate in authority.

2. HISTORY OF JOINT STOCK COMPANIES

(a) 1720 - 1844

At the beginning of the nineteenth century three forms of business organization were in existence. Only two of these, the corporation and the partnership, were fully recognized by law. The third type of business organization was the deed of settlement association whose position under the law was anomalous in the light of the Bubble Act, 1720.

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43. Weber, M., *Theory of Social and Economic Organisation*, translated by Henderson and Parsons, (New York, The Free Press), 145-154.

To avoid the prohibition contained in that Act the business world had recourse to the equitable device of the trust. The effect was that, in law, the deed of settlement association was regarded as a partnership[44].

Corporations as a form of group organization were dependent upon a grant of special authority under Royal Charter, or under a private act of Parliament. At this stage of history the incidents of this form of group organization had long been defined. They included the principle of majority rule[45]. It was not uncommon, however, for the corporate body to set up an executive committee. The relationships between the corporator or stockholder, the committeeman or director and the corporation were as yet unclear and this question has been described as constituting "the sole field of conflict in this body of law"[46].

The partnership, in which each member had an equal share in management decisions, while suitable for the smaller organization was proving unsatisfactory for the larger concern where size and numbers made it impossible for each man to personally supervise his investment[47]. The need for a form of group organization which did not depend on legislative authority but which otherwise closely approximated the corporate form was responsible for the formation of deed of settlement companies. Using this form of organization, the advantages of continuous existence and transmissable and transferable stock were available without the drawbacks of an individual right in every member to bind the other

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44. Cooke, C.A., *Corporation, Trust and Company*, (Manchester, Manchester University Press, 1950) 85, 86.
45. *R* v *Varlo* (1775) 1 Cowp 248, 98 ER 1068; *Attorney-General* v *Davy* (1741) 2 Atk 212, 26 ER 53.
46. Cooke, *op cit*, 79.
47. Hunt, B.C., *Development of the Business Corporation in England 1800-1867*, (New York, Russell & Russell, 1936) 29, quoting Ffooks, W., *The Law of Partnership*, (London, 1852): "no prudent man can, with the present law of partnership, like the sword of Damocles suspended above his head, invest his surplus in any business that he cannot himself practically superintend".

associates or to deal with the assets of the association single-handedly[48].

The deed of settlement companies are so called after their chief constitutive documents which were in effect deeds of partnership consisting of a mutual covenant between a few of the shareholders who agreed to act as trustees and the other shareholders to carry out the provisions contained in the deed[49]. Although it has been stated that there was no pattern of internal management common to these associations before 1844, Dubois[50] does outline a pattern that was often followed. He asserts that, as a rule, the general court or body of proprietors had the exclusive consideration of any policy or change of major importance. The conduct of the day by day business was in the control of a small group of members elected by the general court and usually called directors. But the division of authority between these bodies was, he states, attended by a considerable degree of flexibility[51], and most importantly, the directors were subject to interference and domination by the general court[52].

In many cases[53] concerning these deed of settlement companies the judges were moved to comment on the difficulty of applying rules suitable to the "ordinary" small partnership to large unincorporated

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48. *Baird's Case* (1869) LR 5 Ch App 234 per James LJ; and see Hunt, *op cit*, 12.
49. Cooke, *op cit*, 138.
50. Dubois, A.B., *The English Company after the Bubble Act, 1720-1800*, (New York, Octagon Books, 1971).
51. *Ibid*, 291.
52. *Ibid*, 292, citing proposed charter of the Lake Superior Mining Company of 1772, Privy Council Papers 2,116 which would have made the officials of the company answerable to the General Assembly, *inter alia*, for disobedience of orders.
53. *Van Sandau* v *Moore* (1825) 1 Russ 472, 38 ER 171; *Hallett* v *Dowdall* (1852) 21 LJ QB 98.

associations. The chief difference between these two forms of group organization, as has been pointed out, is that members of the larger association formed the habit of exercising many of their functions solely through the means of directors[54]. Nevertheless, the range of business transacted at general meetings appears to have been commonly wider than would be usual today. In one case it was reported that the business of the general meeting included confirming the sale of one mine and empowering the directors to sell another, sending out a new agent for the company and providing for the payment of certain bills[55].

Dissatisfaction was, however, expressed with the breadth of the powers sometimes left to the directors. The reason for this was that some directors of some companies were mere figureheads. They were appointed to obtain the prestige of their names for the company and did not attempt to fulfil their supposed functions[56]. Thus the Gladstone Committee in 1844 recommended that meetings of shareholders be required periodically, that accounts be audited and published and that directors and officers be made more immediately responsible to the shareholders[57].

(b) 1844 - 1856

The Joint Stock Companies Act, 1844, was the first to afford sanction to the new form of business organization. Joint stock companies were required to apply for registration which would be granted upon fairly stringent conditions including the presentation to the Registrar of a Deed of Settlement. Upon incorporation the company was, *inter alia*,

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54. *Greenwood's Case* (1854) 3 De GM & G 459, 43 ER 180.
55. *Harrison* v *Heathorn* (1843) 6 Man & Gr 81, 134 ER 817.
56. Hunt, *op cit*, 36.
57. British Parliamentary Papers - Report of Select Committee on Joint Stock Companies, VII (1844) No. 413, as cited by Hunt, *op cit*, 93.

empowered to hold general meetings periodically and extraordinary meetings upon due summons, to make by-laws in general meeting for the regulation of the shareholders, members, directors and officers of the company, and to perform all other acts necessary for carrying into effect the purpose of the company and in all respects "as other partnerships are entitled to do"[58]. Further, the company was empowered and required to appoint "from time to time, for the conduct and superintendence of the execution of the affairs of the company, a number of directors"[59]. The term "company" used in this section signifies the fictional entity or business organization but, when it is asked how the powers enumerated above are to be exercised, the answer is that these powers are to be exercised through the general meeting. The power to appoint directors would normally be exercised after an election but there is no requirement that an election be held. More noteworthy is the fact that the company in general meeting is given the power to make by-laws. Such a power may be equivalent to the power to alter or adopt articles reserved to the shareholders in general meeting under modern companies legislation. However, a comparison of the requirements of Schedule A of the Joint Stock Companies Act, 1844, with the modern Table A articles seems to show that most of the provisions currently found in the articles would then have been expected to be included in the Deed of Settlement. It is possible that a power to make by-laws allowed scope for a more detailed regulation of company affairs.

The clause relating to reserve powers does not make express mention of the general meeting. However, in the light of the reference to "other partnerships", it would appear that this clause was intended as a grant

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58. Joint Stock Companies Act (1844) 7 & 8 Vic c 110 s XXV(10), (11), and (12).
59. Joint Stock Companies Act (1844) 7 & 8 Vic c 110 s XXVII.

of powers to "owners" or shareholders. This supposition is reinforced by the context in which the clause occurs, sandwiched between provisions for the general meeting's power over by-laws and for appointment of directors.

The powers of directors are specifically defined in section 27 of the Act which stipulates that it shall be lawful for the directors to conduct and manage the affairs of the company subject to the restrictions of the Act, the Deed of Settlement and the by-laws. The directors are empowered to enter into contracts for the company and specifically to appoint and remove company servants including the company secretary. The unique feature of this provision is found in the rider to the proviso. Directors' powers are stated to be subject to the Deed of Settlement or other special authority "but not so as to enable the shareholders to act in their own behalf in the ordinary management of the concerns of the company otherwise than by means of directors"[60].

In the absence of authority it may be suggested that this provision would not prevent the shareholders in general meeting from giving binding directions to the board of directors. Actions performed under such directions would be accomplished "by means of the directors".

The Companies Clauses Consolidation Act[61] was brought into force in 1845. The provisions there laid down were to govern the internal affairs of companies created by Act of Parliament for public purposes. Sections 90 and 91 made provision for the division of powers between the directors and the general meeting. The directors were empowered to

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60. Joint Stock Companies Act (1844) 7 & 8 Vic c 110 s XXVII
61. Companies Clauses Consolidation Act (1845) 8 & 9 Vic c 16.

manage the affairs of the company and to exercise all the powers of the company not reserved to the general meeting, but the exercise of these powers was stated to be subject to control and regulation by any general meeting specially convened for the purpose. The only limitation on the general meeting's power to exercise such control was found in a proviso that they could not render invalid any act completed prior to the passage of the resolution [62]. In addition, certain powers were expressly required to be exercised by the company in general meeting. These included choice and removal of directors and auditors, control of remuneration of company officers and control of major decisions as to finance including the amounts of money to be borrowed on mortgage, increases of capital and declaration of dividends[63].

The big question in the area of company law development in this period was whether limited liability should be conceded to joint stock companies. This paper will not explore the debate that preceded this concession in any detail, but in its course certain opinions as to management power were expressed which are worth noting. The link between the two questions of limited liability and division of power lay in the argument that limited liability motivated the shareholders to supervise the management of the business closely. The counter argument was that in a large association it was impossible for each member to superintend the business personally and that in the circumstances it was unjust to hold the individual member personally liable[64]. One observer stated that:

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62. Companies Clauses Consolidation Act (1845) 8 & 9 Vic c 15 s XV.
63. Companies Clauses Consolidation Act (1845) 8 & 9 Vic c 15 s XC.
64. Cooke, *op cit*, 110; Hunt, *op cit*, 131.

> "All practical experience teaches that with these companies the fewer powers given to the shareholders except in cases of gross delinquency the better... . The proprietary of an unlimited company must in reality be treated like the 'horse and mule' of commercial enterprise - creatures void of understanding which must be held with a bit and bridle lest they fall upon thee."[65]

Adam Smith, writing well before this period, had also expressed distrust of the general body of proprietors but this did not mean that he thought that it was wise to entrust great powers to the directors. Rather, he concluded that "negligence and profusion" must always prevail more or less in the management of the affairs of such a company which would therefore seldom be able to maintain competition against private adventurers[66]. Although this prejudice had not been overcome, the spirit of liberalism prevailed and the Limited Liability Act of 1855 was enacted. Inasmuch as liability could be limited before this measure was taken by express stipulation embodied in every contract entered into in the name of the deed of settlement company[67], the Act can be seen as regularising and assisting all of these organizations to achieve a state of affairs that some of them occasionally achieved in its absence. Many subsequent company law reforms will also be seen to partake of this character.

(c) After 1856

The Joint Stock Companies Act, 1856 was very similar to the companies legislation now in force. It was the first such Act to which a model

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65. British Parliamentary Papers - First Report, Royal Mercantile Law Commission XXVII (1854) No. 1791 App 45, as cited by Hunt, *op cit*, 29.
66. Adam Smith, *The Wealth of Nations*, (New York, The Modern Library, 1937), 600, that is, Book V c.1 III art 1; see also Hunt, *op cit*, 132 quoting Freshfield J from the First Report - Royal Mercantile Law Commission App 67-68.
67. See for example *Hallett* v *Dowdall* (1852) 21 LJ QB 98.

set of Articles of Association was appended. The Act did, however, leave several provisions which are now found in the body of the Act to take their place in the Table of Articles. As an instance of this, although the Act imposed certain duties on directors[68], it did not require a company to appoint directors. It did, however, require annual general meetings to be held[69]. Article 46 appearing in the Schedule to this Act is virtually identical with Article 73 in Table A of the Uniform Companies Act[70]. Among the duties of the directors imposed by the articles were the duties to keep accounts which should be presented to the shareholders in general meeting[71].

When the Joint Stock Companies Act, 1856 was adopted it was seen as establishing a legal framework for large joint enterprises. It was not until the twentieth century that any statutory provision was made for the smaller or proprietary company. However, many small firms adopted the company format. Indeed, Payne, an economic historian, points out that British big business was not to become a reality for another thirty years[72].

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68. See for example Joint Stock Companies Act (1856) 18 & 19 Vic c 47 s XXXII.

69. Joint Stock Companies Act (1856) 18 & 19 Vic c 47 s XXXII.

70. Joint Stock Companies Act (1856) 18 & 19 Vic c 47 sched B art 4.

71. Joint Stock Companies Act (1856) 18 & 19 Vic c 47 sched B arts 69-73.

72. Payne, P.L., *"Emergence of the Large-Scale Company in Great Britain 1870-1914"* (1967) 20 Ec Hist Rev 519, 520; Payne, P.L., *British Entrepreneurship in the Nineteenth Century*, (Studies in Economic History) (London, Macmillan, 1974) 18 stating that by 1885 limited companies accounted for at most between 5 and 10 per cent of the total number of important business organizations. In the first cited work at 526, Payne suggests that one of the factors restraining the growth of big business was the reluctance of businessmen to raise new capital through procedures which would threaten their control over their family firms. This reluctance was reflected, he says, in the typically British pattern of amalgamations where the old managers retained an unduly large say in the control of the business. This pattern is illustrated by the facts of *Holdsworth (Harold) and Co (Wakefield) Ltd* v *Caddies* [1955] 1 WLR 352.

Robert Lowe, a president of the British Board of Trade, stated the philosophy, not only of the 1856 Act, but of all subsequent companies legislation enacted in Britain and Australia, when he said in the debate preceding the introduction of that Act that, "having given them a pattern" as contained in the scheduled articles of association, "the state leaves them to manage their own affairs and has no desire to force on these little republics any particular constitution"[73].

Despite the disavowal of an intention to impose any particular constitution on the business company, the use of the word republic is significant. Spencer, writing at about the same time, stated that the parliamentary design was almost purely democratic but cynically described the process by which management powers would become paramount[74]. Other contemporary economists also expressed concern about the separation of ownership and control in this form of business organization[75]. Nevertheless, Payne states that there was little evidence of any significant divorce of control from ownership before the end of the century[76]. This fact may explain why the Court of Appeal, faced with the question of the division of power in 1906, had no precedent to guide it: the question had not really arisen before.

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73. R. Lowe in Hansard CXL 134.
74. Spencer, H.,*"Railway Morals and Railway Policy"* (1854) Vol C Edinburgh Rev 420-421: "The direction ceasing to fulfil its theory as a deliberative body whose members possess like powers, falls under the control of some one member of superior cunning, will or wealth, to whom the majority become so subordinate that the decision on every question depends on the course he takes. Proprietors, instead of constantly exercising their franchise, allow it to become on all ordinary occasions a dead letter, retiring directors are so habitually re-elected without opposition and have so great a power of insuring their own re-election without opposition that the board becomes practically a close body and it is only when mis-government grows extreme enough to produce a revolutionary agitation among the shareholders that any change can be effected."
75. Karl Marx,*Das Kapital*, III (Hamburg, 1894) C 23.
76. Payne, P.L., *British Entrepreneurship*, *op cit*, 21.

C. THE DIVISION OF POWERS UNDER THE PRESENT LEGISLATION

The Australian Companies Acts currently in force contain provisions stipulating that certain actions are to be taken only on the authority of a resolution passed in general meeting. In addition, certain duties are imposed upon the directors and it follows, by necessary implication, that they will have the power to carry them out.

The company has a statutory duty to keep such accounting records as correctly record and explain the transactions and financial position of the company[77]. The Act does not specifically impose this duty upon either organ of the company, although if default is made the company, any director of the company who failed to take all reasonable steps to secure compliance by the company, and every officer of the company who is in default, shall be guilty of an offence[78]. The directors are further charged with the statutory duty of laying a report and balance sheet before the company in annual general meeting[79]. The directors, therefore, have the power to cause the company to keep accurate records.

Other powers are left to be divided between the two organs by the company's articles. If any question arises as to the allocation of particular power to either organ, one must first consult the governing legislation. If there is no relevant provision there, one next turns to the articles of association. At this point it becomes relevant to ask whether there are any *a priori* assumptions which will influence the court in construing the articles. Following the plan of attack outlined above, this question will be examined after we have briefly surveyed the

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77. UCA s 161A.
78. UCA s 161A.
79. UCA s 162.

legislation itself.

Powers reserved to the general meeting include the power to alter the memorandum and the articles of association[80]. The power to alter the articles of association is not subject to any restrictions expressed by the legislation, but limitations are imposed by the requirement that the articles of association should be consistent with the legislation and with the company's memorandum and by equitable considerations which will not be considered here[81]. The power to alter the memorandum is more restricted. The memorandum can only be altered as provided by the statute[82].

The shareholders in general meeting are also given certain powers over the company's relations with its officers. Specifically, the Act provides that the general meeting must appoint the auditors[83] and has exclusive power to remove these officers[84]. Powers over the relationship of the company and the directors are more limited. The Anglo-Australian legislation, unlike the legislation in force in North America[85], does not specify that the directors shall be elected by the shareholders in general meeting. Thus, despite the fact that in analysing the control exercised by the general meeting over the company references are frequently made to the power to elect the directors[86], this power has no statutory basis. Some consideration should be given

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80. UCA s 131.

81. See Dickerson, R.W.V., Howard, J.L., Getz, L., *Proposals for a New Business Corporation Law for Canada,* (Ottawa, Information Canada, 1971) vol I para 344-346.

82. *Allen* v *Gold Reefs of West Africa* [1900] 1 Ch 656.

83. UCA s 166(3).

84. UCA s 166B.

85. See Mod Bus Corp Act Ann 2d s 36; Can Bus Corp Act s 101(3); Bus Corp Act (Ont) s 126.

86. See for example *Imperial Hydropathic Hotel (Blackpool) Ltd* v *Hampson* (1883) 23 Ch D 1; *Mendes* v *Commissioner of Probate Duties (Vic)* (1967) 122 CLR 152.

to remedying this deficiency. It is true that the absence of a statutory requirement leaves the company free to enter into agreements with its financiers or others, by which it accepts nominee directors. Although the position of the nominee director is not free from difficulties[87], it may be that companies should not be precluded from entering into such agreements but, it is suggested, the general meeting should at least be given a statutory right to elect a majority of the board of directors whoever nominates the candidates.

In a public company the shareholders in general meeting have a statutory right or power to remove the directors by ordinary resolution and there is no requirement that such a removal should be for cause[88]. The companies legislation also gives the general meeting power to approve payments to any director as compensation for loss of office or in connection with the transfer of the whole or any part of the undertaking and without such approval the payment will be illegal. The legislation does not, however, have anything to say about the remuneration of directors generally. Although the Table A articles provide that this shall be determined by the company in general meeting[89], it appears that the articles could give the board sole power in this regard. While this may be unobjectionable in the case of a proprietary company, it is suggested that directors in public companies should have to refer this question to the general meeting.

Where a compromise or arrangement is proposed between a company and its members the court will order that a meeting of members, or of the class

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87. See *Scottish Co-operative Wholesale Ltd* v *Meyer* [1959] AC 324.
88. UCA s 120.
89. UCA Fourth schedule Table A reg 70.

of members, be held and approval of the compromise or arrangement by a three-quarters majority will be a condition of a court order authorizing it to be carried out[90]. The general meeting is also empowered to pass a resolution for the voluntary winding up of the company[91]. Without such a resolution, a court's supervision is necessary for dissolution.

Eisenberg, as discussed above, has argued strongly that the general meeting should be given jurisdiction over changes in the structure of the corporation. Such changes include combination, that is, amalgamation or merger of two or more companies, and contractions or divisions[92]. This is a complex question and this thesis will not attempt to explore its complexities. However, the provisions of the current legislation should be noted. The term compromise or arrangement used in the Australian legislation includes reconstructions or amalgamations[93] but there is no provision in the Anglo-Australian legislation requiring the approval of a general meeting for the sale of the whole or a substantial part of its undertaking, whether in or out of the course of ordinary business. Such provisions are found in the North American legislation[94] but, as will be seen below[95], the Anglo-Australian courts have interpreted the directors' powers of management as enabling them to arrange such a sale without approval. The Jenkins Committee has recommended that provisions requiring the authorization of the general meeting for such a sale be adopted[96]. They considered requiring such

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90. UCA s 181.
91. UCA s 222(1)(a) and s 254.
92. Eisenberg, *Structure, op cit,* 215, 275; see also Iaccobucci, *op cit,* 418-471.
93. UCA s 183.
94. Mod Bus Corp Act Ann 2d s 79; Can Bus Corp Act s 183(2); Bus Corp Act (Ont) s 193.
95. See below, 129-130.
96. Great Britain, Board of Trade, *Report of the Company Law Committee* (1962) para 111, hereinafter cited as the *Jenkins Report*.

authorization for fundamental changes in the scope of the company's activity but rejected the suggestion on the basis that it would be too difficult to implement. The Jenkins Committee also recommended that the power to issue shares be placed under a special form of control exercisable by the company in general meeting, on the ground that such a step was necessary to round out the general meeting's control over the company's capital structure[97], but no action has been taken on these recommendations as yet.

In North America, companies legislation generally stipulates that the directors have the power and the duty to manage the business of the company[98]. Anglo-Australian legislation includes no such general provision. Powers of management are left for allocation to the articles of association. The Australian Table A articles allocate this power to the directors by virtue of article 73, which is discussed in detail below, and this provision will be adopted almost universally by business companies. In this respect it is considered that the Anglo-Australian provision is preferable. There are several reasons for this conclusion, perhaps the most important of which is the fact that the British and Australian legislation in question does not apply exclusively to business companies. Furthermore, there is a general tendency for power to gravitate into the hands of the board of directors and it is therefore unnecessary to make such a statutory grant of power.

It may be noted that recent amendments to certain pieces of the North American companies legislation have the effect of making the general

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97. *Jenkins Report, op cit*, para 113.
98. Mod Bus Corp Act Ann 2d s 35; Can Bus Corp Act s 97; Bus Corp Act (Ont) s 132.

rule subject to exception[99].

D. TWO LEGAL VIEWS OF THE RELATIONSHIP BETWEEN BOARD AND GENERAL MEETING

Before turning to examine various specific problems in the division of powers, an examination of those cases which reveal judicial attitudes to the relation between the two organs is in order. Two distinct views of the position of the general meeting can be distinguished. The earlier view saw the general meeting as the supreme body of the company possessing supervisory powers over the board of directors who managed the daily affairs of the company but who were bound to obey the instructions of the general meeting. The second and later view sees the general meeting and the board of directors as co-ordinate bodies each of which is sovereign within the scope of its own powers. A third view, which as yet has found no reflection in judicial decisions, sees the general meeting as the constituency of the board of directors but would deny it any wider powers than those of electing some or all of the directors. Inasmuch as it is considered impossible to discern clearly a line of demarcation between those cases decided under modern companies legislation and those decided before 1856, no attempt to observe such a distinction has been made below. If such a distinction is valid, it was not immediately perceived by the courts.

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99. Mod Bus Corp Act Ann 2d s 35.02. The general provision is applicable only "unless otherwise provided" - an amendment introduced in the 2nd edition, 1969 Can Bus Corp Act s 97: the general stipulation may be circumvented by unanimous shareholder agreement.

1. THE SUPERVISORY ROLE OF THE GENERAL MEETING

Although it is not the current view, it was once thought that inasmuch as the general meeting was the company, the acts of the directors were always subject to control by the general meeting. Before turning to examine the authorities which have displaced this assumption, the evidence for it will be briefly surveyed.

In 1843 in the course of his judgment in *Foss* v *Harbottle*[100], Vice-Chancellor Wigram stated that the deed of settlement made the directors the governing body of the company, subject to the superior control of the proprietors assembled in general meeting. The private act of incorporation in question provided that the business affairs of the company should be under the control of the directors and forbade any proprietor who was not a director to meddle or interfere in the management of the company[101]. It must be noted that there is a clear distinction between the right of the individual proprietor to take part in management and the right of the general meeting to do so and this distinction would explain why Vice-Chancellor Wigram might have found the prohibition irrelevant. Although the deed appears to limit the meeting's powers to those matters specifically enumerated, Vice-Chancellor Wigram assumed that the proprietors in general meeting had power not only to originate legal proceedings but also to control the directors' conduct of any proceedings which they might have originated.

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100. (1843) 2 Hare 461. 67 ER 189.

101. *Foss* v *Harbottle* (1843) 2 Hare 461, 67 ER 189. The relevant section (s 37) of the company's constitutive act read as follows: "The business affairs and concerns of the company shall from time to time and at all times hereafter be under the control of five shareholders (to be appointed directors) who shall have the entire ordering, managing and conducting of the company...and no proprietor, not being a director, shall on any account or pretext whatsoever, in any way meddle or interfere in the managing, ordering or conducting the company...but shall fully and entirely commit, entrust and leave the same to be ordered, managed and conducted by the directors...".

In 1847, in *Exeter & Crediton Railway Co* v *Buller*[102], the question for decision was whether the board or the general meeting would decide who would lease the railway line that the company had been incorporated to build. It is important to note that the decision could not later be reconsidered as it would determine the gauge of the railway to be built. In approaching the issue, Lord Cottenham raised the question of which body, board or general meeting "is to be considered the corporate body"[103]. He decided that the general meeting was to be considered the corporate body, a decision whose width is restricted when interpreted from the context to mean that the general meeting was the corporate organ with the authority to make the decision in question. The basis of the decision was that both the Act incorporating this particular statutory company and the general act which applied to all statutory companies[104] provided that the exercise of the directors' powers was to be subject to the control of the general meeting but prevented the general meeting from invalidating prior acts. Lord Cottenham issued an interim injunction prohibiting the board of directors from acting before the general meeting was held, because otherwise the provision as to the control of the general meeting could be rendered nugatory by the quick action of the directors[105].

The general meeting which was subsequently held decided against the plan favoured by the board of directors and as the directors refused to accept these instructions the matter was referred back to the court. It

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102. (1847) 16 LJ Ch 449.
103. *Exeter & Crediton Railway Co* v *Buller* (1847) 16 LJ Ch 449, 450.
104. Company Clauses Consolidation Act (1845) 8 & 9 Vic c 16.
105. *Exeter & Crediton Railway Co* v *Buller* (1847) 16 LJ Ch 449, 451.

was held that the facts that: (a) the resolutions called for a reversal of the company's original policy, (b) the resolutions would materially increase the company's expenses, (c) the change in policy was dictated by people who were not originally shareholders, and (d) these shareholders were acting on motion of another company, were all irrelevant. The board was bound by the directions given by the general meeting under the provisions of the Companies Clauses Consolidation Act, 1845. The court did not inquire into the *bona fides* of the shareholders, apparently assuming that they could not damage the company without damaging their own interests and refusing to contemplate the possibility that the interests of the shareholders who were connected with the other company might be better served by sacrificing one company to the other.

The decision in *Wilkins* v *Roebuck*[106] in 1858 is worth noting because, despite the fact that the relevant deed of settlement strictly limited the general meeting's powers of supervision and apparently intended to confide residual powers to the board of directors, the judge felt it necessary to construe the document to give the board a specific power to do the challenged act. A similar decision by the New South Wales Supreme Court in 1871[107] stressed shareholder acquiescence in the directors' actions in similar circumstances.

On the question of whether the general meeting can attach a condition to a specific grant of authority which it makes to the board of directors, the case of *Fraser* v *Whalley*[108] may be referred to. In that case the general meeting had authorized, with a particular purpose in sight, the issue of certain shares. The facts reported do not make

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106. (1858) 4 Drew 281, 62 ER 109.
107. *City Bank* v *Australian Paper Co* (1871) 10 NSWSCR 235.
108. (1864) 2 H & M 101, 71 ER 361.

clear whether or not the resolution that authorized the issue included a reference to the purpose or whether this purpose merely provided the motivation for the authorization. The directors sought to take advantage of the authorization after the particular purpose had become impossible of realization in circumstances of "indecent haste and scramble" strongly suggesting that their motivation was to ward off a looming challenge to their position. It was held that they should have renewed their application to the general meeting. This decision has two aspects. It can be, and generally has been[109], viewed as a decision based on a finding that the directors had abused the power by using it in their own interests. The decision could also have been based on the fact that the purpose envisaged by the general meeting limited the grant of power. In the light of the particular facts there was, however, no necessity to consider this aspect. The question does not seem to have arisen again, but it is suggested that if it did arise today, the court would need to find first that the purpose for which the resolution was passed was evident on its face and was not merely the motivational background. Only then would the question arise whether the grant of authority was conditional on the purpose being served. It would be possible to argue that the general meeting's action and the board's action, increasing the capital and issuing the shares, were completely separate things, and that the purpose for which one was done did not affect the second transaction. This discussion, however, has diverged from the historical treatment which which we are here concerned.

The cases cited above evidence a unified approach to the question of relations between the general meeting and the board of directors.

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109. See for example *Punt* v *Symons* [1903] 2 Ch 506; *Piercy* v *S. Mills & Co* [1920] 1 Ch 77; *Hogg* v *Cramphorn* [1966] 3 All ER 420.

Regardless of the manner in which the corporate body was constituted, this approach emphasised the status of the general meeting as the pre-eminent corporate organ, the body of owners of the company. In 1882 the first hint of a new approach can be detected[110]. But before considering it, the decision in *Isle of Wight Railway Co* v *Tahourdin*[111], which takes its place at the culminating point of the line of cases already traced, will be examined.

The decision in *Tahourdin's* case has since been distinguished[112] on the basis that the railway company in question was incorporated by a special Act and was accordingly governed by the Companies Clauses Consolidation Act, 1845. The relevant provisions in that Act, sections 90 and 91, have been outlined above[113]. The validity of this distinction is doubtful. The Court of Appeal did not, in deciding *Tahourdin's* case, make reference to either of the Acts cited. It is suggested that this distinction is an instance in which the court deciding the later case sought a way to dispose of a contrary authority because views had changed rather than because there was a genuine difference in the relevant facts. This suggestion is supported by the fact that the only difference of substance between the form of the provision in the Companies Clauses Consolidation Act, 1845 and the form of the article found in Table A is the omission from the article of the adjectival clause "especially convened for the purpose" which was used in the section to modify the noun "meeting". This difference is not, on its face, large enough to justify such a difference in interpretations.

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110. *Imperial Hydropathic Hotel (Blackpool) Ltd* v *Hampson* (1882) 23 Ch D 1 as discussed below at n 117 and accompanying text.
111. (1884) 25 Ch D 320, hereafter referred to as *Tahourdin's* case.
112. *Automatic Self Cleansing Filter Syndicate Co Ltd* v *Cunninghame* [1906] 2 Ch 34.
113. See above, 95–96.

The question at issue in *Tahourdin's* case was whether a general meeting could properly be held upon a requisition which proposed to set up a committee of the general meeting to inquire into the management of the company with power to require the directors to follow its recommendations. Kay J in the first instance held that a general meeting could not transfer the functions of the directors to a committee and granted an injunction to prevent the meeting. On appeal the decision was reversed on the basis that while it might not be possible to give a committee management powers, it was possible to set up an investigative committee which would report back to the meeting. The general meeting itself had "undoubtedly, a power to direct and control the board in the management of the affairs of the company"[114]. A shareholder who wanted to alter the management of company affairs would be advised, according to Cotton LJ, to "go to a general meeting and if they agree with you they will pass a resolution obliging the directors to alter their course of proceeding"[115], and consequently it was unthinkable that the court should restrict the right to call a general meeting.

In invoking the power of the general meeting in all these cases the courts avoided any reference to provisions which in some of these cases limited the power of the general meeting fairly stringently. The decisions rest on the basis that the general meeting is the body of owners of the corporate funds, that the directors derived their powers from this body and stood in relation to it in the position of agents

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114. Isle of Wight Railway Co v *Tahourdin* (1884) 25 Ch D 320, 331-332.
115. Isle of Wight Railway Co v *Tahourdin* (1884) 25 Ch D 320, 330-331.

and must therefore obey their commands[116].

It was recognized at this stage that to allow the individual shareholder to intervene in corporate affairs would render fulfilment of the corporate purpose practically unobtainable but each shareholder, so the theory went, had voluntarily surrendered individual rights of control in return for a voice in the decisions of the general meeting which would control the directors. The possibility that a majority in general meeting might serve their own interests at the expense of those of the minority did not become a matter of concern until the Privy Council overturned the decision of the Canadian Supreme Court in *North West Transportation Co* v *Beatty*[117] in 1887, and held that a shareholder voting in general meeting need consult nothing but his own interests even though in his capacity of director he was bound to act in the interests of the company. A contract of the company in which the shareholder-director was interested could be ratified by the general meeting on a resolution carried by virtue of his votes.

To summarise the position adopted in these early cases in the terms of our earlier discussion of group theory, it would seem that these cases adopt the view that the principle of majority rule is paramount and that the centralization in question was properly characterized as a delegation being both voluntary and, unless embodied in a specific grant of

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116. Aicken, K.A., *"Division of Power between Directors and General Meeting"* (1967) 5 M U L Rev 448, 449: "The view appears to have been entertained in the early stages of modern company law that the directors were agents of the members, in a sense agents of all the members and perhaps more particularly agents of the majority of members. This view, of course, would produce the result that a majority of members at a general meeting...had complete control of the directors in relation to the ordinary conduct of the company's business."

117. (1887) 12 App Cas 589.

enumerated powers, reversible on particular questions by ordinary resolution.

2. THE GENERAL MEETING AND THE BOARD AS CO-ORDINATE BODIES

During the second half of the nineteenth century, nothing suggested that the registered company under modern company law[118] differed greatly from the statutory company governed by the Companies Clauses Consolidation Act, 1845. In the twentieth century, however, a new view of the relationship between the general meeting and the board of directors has gained general acceptance.

The first hint of the new approach may be seen in the decision in *Imperial Hydropathic Hotel (Blackpool) Ltd* v *Hampson*[119]. The issue was whether the general meeting had inherent power to remove the directors. Rather than resolving the question by reference to a general concept of the relation between the two corporate bodies, the court had reference to the specific provisions of the company's articles. There was no provision in these articles allowing the general meeting to remove directors and it was held that the fact that the articles could be altered did not mean that they could be ignored in a particular case. This holding is not compatible with the notion that the directors are merely agents for the general meeting. Mere agents are dismissable at the will of their principal regardless of any contractual rights which may arise[120].

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118. The Companies Act (1862) 25 & 26 Vic c.89, replaced the Joint Stock Companies Act (1856) 18 & 19 Vic c.47 and was the first of a series of Companies Acts in which there have been no major changes.

119. (1882) 23 Ch D 1.

120. This point is made in the course of the discussion on the relation between the proxy holder and his principal in Part VI.

The first case to clearly establish the new concept, and the leading authority in this area, is *Automatic Self Cleansing Filter Syndicate Co Ltd* v *Cunninghame*[121]. The action was brought by a shareholder in the name of a company to compel the board of directors to comply with the terms of a resolution which he had proposed and which had been passed by the general meeting, directing the company to enter into a particular undertaking.

The company's articles of association gave the directors specific power to sell the undertaking as well as giving them general powers of management subject to regulations to be made by extraordinary resolution. The directors, acting in the belief that the contract in question was not in the best interests of the company and relying on the fact that the power in question was given directly to them by the articles, refused to comply with the resolution.

The court both at first instance and on appeal had reference to the articles of association but the judgments are inconsistent with the view, later expressed[122], that emphasis was put on the fact that an extraordinary resolution was needed to control the directors in the exercise of their powers.

Warrington J, in the first instance, held that the articles vested powers of management in the directors and that, inasmuch as the articles could only be altered and the directors could only be removed by special resolution, an ordinary resolution could not control the directors in the exercise of their powers. The directorate could not be reduced to a

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121. [1906] 2 Ch 34, hereafter referred to as *Cunninghame*.
122. See for example Aicken, *op cit*,

mere instrumentality or overridden at the will of a mere majority or there would be no point in safeguarding their tenure of office. He did not specifically refer to the question of the general meeting's power to control the exercise of management powers by extraordinary resolution. Inasmuch as his decision relied on the impossibility of removing directors by ordinary resolution it would not apply to any public company, as there is now a statutory right to remove directors of such companies by ordinary resolution[123], or to any proprietary company which has adopted a similar provision in its articles. However, it is suggested that the argument can be stated in wider terms, that directors are to be seen as occupying an office from which they can be removed but in which they cannot be controlled. A parallel may be drawn with the position of trustee. A trustee may be removed where the beneficiaries are all *sui juris*[124] and is expected to have regard to the wishes or instructions of his beneficiaries[125] but cannot be required to act under dictation[126].

This wider interpretation of the basis of the decision can be supported by reference to the appeal judgments. Thus Collins MR held that the majority at an ordinary meeting could not alter the mandate given the directors by the articles of association. This could be done only by means of the special machinery provided to allow alterations of the

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123. UCA s 120.
124. *Re Brockbank; Ward* v *Bates* [1948] Ch 206.
125. Finn, P.D., *Fiduciary Obligations* (Sydney, Law Book Co, 1977) citing UCA s 237(1) and Bankruptcy Act, 1966 (Cwth) s 177(1) which requires the trustee in bankruptcy to have regard to resolutions passed at creditors' meetings.
126. *Ex parte Brown, In re Smith* (1886) 17 QBD 448, as cited by Finn, *op cit*, 23.

articles. He acknowledged that for some purposes the directors were agents but raised the question of for whom they so acted. The directors, he held, were in theory agents of the corporate entity who in practice obtained and held their position as a result of the consensus of members or shareholders and thus could not be said to be the agents of the majority[127]. Cozens-Hardy LJ based his judgment on the fact that the articles constituted a contract between the shareholders. He denied that the directors occupied the position of agents[128], rather he found that their position was analogous to that of managing partners. A distinction exists and must be drawn between holding that the directors derive their powers from a contract between the shareholders and holding that they derive their powers from the general meeting, but this point will be more fully developed later.

The principles traceable to the *Cunninghame* case were not immediately accepted by all authorities. In 1909 in *Marshall's Valve Gear Co Ltd* v *Manning, Wardle and Co Ltd*[129], Neville J expressly declined to adopt the reasoning that had been used in the earlier case, holding that the observations found there extended beyond and were inconsistent with the law as it stood at the time. He cited authority for the proposition that "in the absence of any contract to the contrary" the majority of shareholders in a company have the ultimate control of its affairs and decided the case before him on that basis[130]. However, the facts of the case reveal that the decision could have been made on another basis. The issue was whether an action brought in the name of the company by a

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127. *Automatic Self Cleansing Filter Syndicate Co Ltd* v *Cunninghame* [1906] 2 Ch 34, 44.
128. [1906) 2 Ch 34, 47.
129. [1909] 1 Ch 267.
130. [1909] 1 Ch 267, 272.

shareholder who held the majority of shares in the company and who was also one of the four directors was properly constituted. The action was against a company in which the three directors who opposed it were interested. The court assumed that their decision was *bona fide* in the interests of the company but pointed out the conflict of interest situation. There can be no question but that these facts would justify the decision without reference to the fact that the action was supported by the shareholder who commanded the majority in general meeting. It should be noted that the two cases do not conflict in principle. To hold as in *Cunninghame* that the board of directors is not subordinate to the general meeting in the exercise of its powers is not to deny that, in the absence of contract, the general meeting has the ultimate control of the company's affairs. The contrast lies in the different attitudes and in the fact that the two courts could be expected to approach the construction of the article[131] giving general powers to the board in different ways. Neville J, it seems, would if given the opportunity have held that the Table A articles gave the general meeting power to pass regulations controlling the directors.

The approach taken in *Cunninghame* was endorsed by the House of Lords in *Quinn & Axtens Ltd* v *Salmon*[132] in 1909. The articles in point in that case limited the powers of the board of directors by forbidding it to act where either of the two managing directors dissented in writing from its decision. The board made certain decisions from which Mr Salmon dissented; a general meeting attempted to pass resolutions which would be similar in effect to those which the board wanted to bring into force.

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131. UCA Fourth schedule Table A reg 73.
132. [1909] AC 442 affirming *Salmon* v *Quinn & Axtens Ltd* [1909] 1 Ch 311.

Loreburn LC held that as the dissent in question did not prevent the board from managing the business, there was no basis for remitting the matter to the company in general meeting. This was a reference to the doctrine that where the board of directors is non-existent or incapable of acting, the general meeting will have power to act, a doctrine which will be discussed in detail below[133]. Loreburn LC suggested, *obiter*, that where management powers are entrusted to the board of directors the general meeting would not have the power to give either particular or general directions to it, regardless of the wording of the article in question[134]. It is suggested that more is needed to establish that this is the law than an *obiter* statement made without reference to any earlier decisions. *Exeter & Crediton Railway Co* v *Buller*[135], discussed above, is one authority which is directly contrary to the suggestion.

In *Thomas Logan Ltd* v *Davis*[136], a 1911 decision, it was held by Warrington J that the special powers conferred on the directors by other articles were not subject to the proviso written into the standard form article which made the board's powers of management subject to control by the general meeting. This constituted an *obiter* rejection of the *obiter* suggestion made by Lord Loreburn in *Quinn & Axtens Ltd* v *Salmon*, but it also marked a complete reversal of direction accomplished within a space of five years. In *Cunninghame* the question was whether the directors in the exercise of their specific powers were subject to control by the general meeting. Five years later, in *Thomas Logan Ltd* v *Davis*, a distinguished judge is concerned to preserve some power for the general meeting. The Court of Appeal upheld the decision on appeal but

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133. See below, 140–143.
134. *Quinn & Axtens Ltd* v *Salmon* [1909] AC 442, 444.
135. (1847) 16 LJ Ch 449 as discussed above at 107.
136. (1911) 104 LTR 914.

specifically refused to comment on Warrington J's reasoning. His reasoning was, however, adopted by the Supreme Court of New South Wales only two years later[137].

The principle in question was invoked by Greer LJ in a case in which the Court of Appeal decided that the general meeting could not effectively instruct the board of directors to discontinue legal proceedings. His statement of the position is worth quoting because it is, with respect, the best available statement of the law in this area. He held that

> "A company is an entity distinct alike from its shareholders and its directors. Some of its powers may be reserved for the shareholders in general meeting. If powers of management are vested in the directors, they and they alone can exercise these powers. The only way in which the general body of the shareholders can control the exercise of the powers vested by the articles in the directors is by altering their articles, or, if opportunity arises under the articles, by refusing to elect the directors of whose actions they disapprove. They cannot themselves usurp the powers which by the articles are vested in the directors any more than the directors can usurp the powers vested by the articles in the general body of shareholders."[138]

Although this statement is seen as being the best to be found on the topic, the use of the word "reserved" is deprecated on the basis that it can give rise to two conflicting and contentious implications. It comes close to summing up all the problems in this area of the law. It can give rise to an implication that all powers of the company were originally vested in the general meeting from whence some were transferred to the board of directors, although the use of the phrase "powers vested by the articles in the general body" later in the passage tends to negate this implication. The use of the word "reserved" can also imply that

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137. *Dowse* v *Marks* (1913) 13 SR (NSW) 332, 341 per Harvey J: "Being matters of internal management only not placed by the articles beyond the control of a simple majority of shareholders the wishes of that majority must prevail."
138. *John Shaw & Sons (Salford) Ltd* v *Shaw* [1935] 2 KB 113.

every power not specifically allotted to the general meeting is vested in the board of directors. The articles of a company may, as the standard form articles do, vest those powers not required to be exercised by the general meeting in the board of directors, but they need not necessarily do so. The proposition that the board is not a subordinate body in the corporate structure will not depend on this disposition.

The other English decision usually considered as forming part of the line of authority currently under examination is *Scott* v *Scott*[139]. In that case the validity of certain resolutions passed by the general meeting was in issue. The first of these directed that certain payments be made to the shareholders in advance of the declaration of a dividend. The articles gave the directors express power over interim dividends as well as powers of management and it was held that this resolution was invalid. The second resolution directed that an investigation into the financial affairs of the company over the past two years be carried out. This resolution was, it was suggested, an attempt to do by ordinary resolution what could only be done by statute[140], and furthermore constituted an interference by the general meeting with the financial affairs of the company which had been entrusted to the powers of the board of directors, and was therefore inoperative. No reference was made to former case law but Clauson J did observe that "it must be borne in mind that the professional view as to the control of the company in general meeting over the actions of directors has, over a period of

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139. [1943] 1 All ER 582.
140. Companies Act (UK) (1928) 19 & 20 Geo V c.23 s 137.

years, undoubtedly changed"[141]. This observation, which is relevant to any question of construction, has been widely cited[142].

The English authorities have been traced but Australian authorities on the point are much scantier. The decision in *Dowse* v *Marks* has been cited above. Reference may also be made to the judgment of Jordan CJ in *Clifton* v *Mount Morgan Mines Ltd*[143], in which he took the opportunity to express his views on the question in these words:

> "A company incorporated by registration is a legal entity distinct from its members. It is incapable of acting except through the medium of agents. The Articles of Association...prescribe the various agencies which may act on behalf of the company, the manner in which these agencies may be set in motion and the scope of their respective authorities...there is no universal rule that the shareholders in general meeting may by ordinary resolution bind or represent the company with respect to anything and everything."

He held that shareholders acting by ordinary resolution could not do anything denied by the articles to a general meeting, and conferred either on the directors exclusively or on the general meeting only when it acts by an enlarged majority[144].

The fundamental difference between what may be called the nineteenth century view and the view espoused in *Cunninghame* and subsequent cases lies, it is submitted, in the fact that the board is seen as deriving its powers not from the general meeting but from the company's constitution. Nineteenth century courts seem to have laid importance on the fact that the members of the general meeting were the owners of the

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141. *Scott* v *Scott* [1943] 1 All ER 582, 584.
142. See for example Sullivan, *op cit*, 577; Slutsky, B.,*"The Relationship between the Board of Directors and the Shareholders in General Meeting"* (1969) 3 U BC L Rev 81.
143. (1940) 40 SR (NSW) 31, 43.
144. Ford, *op cit*, [1408].

company and to have taken the view that, therefore, their will as represented by a majority decision should prevail.

The following justification of the twentieth century view is offered. It is the members of the general meeting, and not the general meeting itself, who own the company. The individuals who are to form the company, promotors, plan to divide company powers between the board of directors and the general meeting in which the individual members will have a voice. Because it is through the general meeting that the individual owners will have an influence over corporate decisions, the companies legislation requires that certain crucial decisions be made in general meeting and the promotors may decide to add others to the list. But decisions made by the board of directors, as, also, resolutions passed by the general meeting, represent the will of the owners of the corporation. Both organs were provided for at the same time and they are co-ordinate in authority except insofar as a power entrusted by the articles to the general meeting is delegated by it to the board of directors. This scheme of alloting powers to the general meeting for delegation to the board is theoretically possible but in fact is rarely or never adopted.

The essence of the unincorporated association, as of the partnership, in contrast to the registered company, consists of the meeting or association of members[145]. It has been pointed out that modern company law derives equally from corporation and from partnership principles but it is Lindgren's view, accepted here, that the partnership view of the company was decisively rejected in the twentieth century decisions cited

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145. *Australian Coal and Shale Employees Federation* v *Smith* (1938) 38 SR (NSW) 48.

above and that a view derived from corporation law is now dominant, in this area of company law at least[146].

This theory, it is submitted, explains the reference to corporate entity in the judgment of Greer LJ quoted above[147], which Ford finds obscure[148]. The distinction between the unincorporated group and the corporate body is essential when the relationship between the general meeting and the board of directors is considered. Where, as under the Table A articles, the company constitution undertakes to divide company powers between the two branches of the company structure, then the company so formed is a dyarchy in which neither organ derives its powers from the other.

Gower states that the old idea that the directors are merely agents while the general meeting is the company requires modification, that it appears now that both bodies may "be" the company, or, in other words, that both are organs, not agents, of the company[149]. He suggests that an analogy may be drawn between this type of division of powers and that existing under a federal constitution[150]. This analogy is not perfect but is in point when it comes to pointing out that although the body of shareholders may pre-date the company structure as New South Wales pre-dates the Commonwealth of Australia, still, under the constitution both bodies are co-ordinate. The question of which body is to exercise those powers not specifically granted to either does not affect this position as is demonstrated by a comparison between Australia and Canada. The general meeting as such owes its existence to the corporate constitution just as

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146. Lindgren, K.E.,*"History of the Rule in Royal British Bank* v *Turquand"* (1975) 2 Mon L Rev 13, 40.
147. *John Shaw & Sons (Salford) Ltd* v *Shaw* [1935] 2 KB 113; see above, 119.
148. Ford, *op cit,* [1408].
149. Gower, *op cit,* 132.
150. *Ibid,* 133.

New South Wales derives its status as a member of the Commonwealth from the Constitution of the Commonwealth.

Pennington states that the directors are sovereign within the limits of the powers conferred on them by the articles. It is his opinion, however, that if powers were vested in both organs of the company concurrently, the decision made in general meeting would prevail over that of the directors because "the members in general meeting are the superior authority"[151]. While the question is academic in that there do not seem to be any such powers in existence, in the context of this theoretical discussion it is worth some consideration. The basis for the assertion of the general meeting's superiority is not given. It is possible that what is referred to is the fact that the general meeting through its power over the articles and over appointment of directors retains ultimate control of the company. This fact, however, would not mean that in the situation envisaged the decision of the general meeting would necessarily prevail in the absence of a resort to the powers of ultimate control. In no other way may the general meeting of a company formed under Table A articles be said to be the superior body, and it is submitted that conflicting decisions in any area of concurrent powers will result in deadlock necessitating resort to the two means of ultimate control referred to above unless the articles provide, as a means of resolving such situations, that the decision of either body shall prevail. If such a provision were to be made there would be no requirement under the common law that the provision should stipulate that the general meeting's decision should prevail.

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151. Pennington, R.R., *Company Law*, 3rd ed (London, Butterworth, 1973) 499-500.

It was stated above that in a situation where the power can be traced not to a voluntary agreement among the members but to an arrangement imposed from outside the organization, the use of the term delegation is inappropriate. It is therefore to be noted that Aicken points out that for this reason the concept of delegation has no place in a discussion of the division of power between the general meeting and the board of directors notwithstanding that an appropriate majority in general meeting can alter this division[152].

Sullivan concedes that it is possible to make the directors autonomous of the general meeting under the law as it stands now[153], but contends that this has not been done in respect of general management powers under the Table A articles as they stand. It is his view that the shareholders in general meeting are not a mere constituency but the supreme organ of the company, possessing not only the right to elect and dismiss directors and to alter the articles of association, but also an ever-present power to intervene in matters of management[154]. It is submitted that this is not a disagreement as to principle but merely a disagreement as to the interpretation of the relevant article in Table A and that this is also true of Goldberg's position[155]. The question of the interpretation of the Table A articles will be considered below[156] and the views of these two authors on this topic will be expounded there. For present purposes it is sufficient to note that the view expounded in the paper represents the present orthodoxy and has not been dissented from.

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152. Aicken, *op cit,* 459.
153. Sullivan, *op cit,* 571.
154. *Ibid,* 570.
155. Goldberg, *op cit.*
156. See below, 126 *et seq.*

E. SPECIFIC PROBLEMS WITH THE DIVISION OF POWERS

The first problem with which this section is concerned is the interpretation of the article entrusting management powers to the board of directors, regulation 73 of the Australian Table A articles and its British equivalent, regulation 80. The doctrine which allows the general meeting to act where the board is unable or unwilling to do so and the question of which corporate organ controls corporate litigation will also be discussed in this section.

1. REGULATION 73, TABLE A

As this subsection of the thesis will be concerned with a detailed discussion of this regulation, it is appropriate to set out its terms in full. The regulation provides that:

> "The business of the company shall be managed by the directors, who may pay all expenses incurred in promoting and registering the company and may exercise all such powers of the company as are not, by the Act or by these regulations, required to be exercised by the company in general meeting, subject nevertheless to any of these regulations, to the provisions of the Act and to such regulations, being not inconsistent with aforesaid regulations or provisions, as may be prescribed by the company in general meeting; but no regulation made by the company in general meeting shall invalidate any prior act of the directors which would have been valid if that regulation had not been made."

(a) "Business of the Company"

The directors are, under the terms of this article, to manage the business of the company. But how is the term defined? It is unquestionable that the conduct and management of existing affairs is included within the scope of the phrase. The difficulty comes in deciding what else the term covers. In approaching this question, the presumption, in

twe twentieth century at least, has been that any transaction or decision to be made by the company falls within its boundary unless there is specific authority to the contrary.

There is clear authority to the effect that unless the articles contain a clause giving the board of directors specific power over remuneration of its members, these questions will fall to be decided by the general meeting[157]. It therefore appears that decisions as to such matters as the appointment, remuneration, and removal, of individual directors only fall to be made by the board when there are specific provisions to this effect in the articles[158]. The general meeting, it appears, has an inherent power to appoint and nominate the directors[159] unless such power is removed by the articles either by implication or expressly. Further, under general fiduciary principles, the directors cannot without the authorization of the general meeting speaking for the *cestuis que trustent* remunerate themselves but such authorization may be general, incorporated in the articles, or express and particular in the form of a resolution[160]. The general meeting does not have an inherent power to remove the directors but may derive such a power from statute or from the articles[161].

Does the power to manage the business of the company include the power to change that business, that is, to extend into new fields of endeavour

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157. *Foster* v *Foster* [1916] 1 Ch 532.
158. Provision is made in UCA Fourth schedule Table A reg 68 for the board to have the power to appoint directors to fill casual vacancies.
159. *Grant* v *John Grant & Sons Pty Ltd* (1950) 82 CLR 1, 22 where Latham CJ refers to "the company's" inherent power to do so, in the context clearly referring to the general meeting's power; see also *Isaacs* v *Chapman* (1916) 132 TLR 237.
160. See *Colhoun* v *Green* [1919] VR 196, 201 and *Re Duomatic Ltd* [1969] 2 Ch 365.
161. *Imperial Hydropathic Hotel (Blackpool) Co Ltd* v *Hampson* (1882) 23 Ch D 1; see also *Bersel Manufacturing Co Ltd* v *Berry* [1968] 2 All ER 552.

or to contract the scope of the company's business by selling off a part or the whole of the company's undertaking? As to the first question, the Privy Council was asked, in 1908, to hold that the board of directors was going beyond its provence in recommending the extension of the company's business into new fields. It declined to do so, holding that it is within the right and duty of the board of directors to advise the members as to the prudence of such proposals[162]. This power could not be derived from any other article in that case, nor is there a relevant provision in the Table A articles, but it was not specifically traced to the article conferring management powers and it is possible that this is one of the powers the board derives from the common law[163]. In any case, there is a major difference between the power to recommend extensions of the business and the power to decide to extend the business without referring the matter to the general meeting. On the propriety of the latter, there appears to be no case authority. Current practice condones such an assumption of power but it is suggested that its desirability should be reviewed.

As far as contractions of the company business through sale of the undertaking are concerned, Dickerson states that the common law position appears to be that directors have complete powers to dispose of the entire undertaking of a company without consulting the shareholders[164]. There are decisions, made in cases where an objection against a sale of the business or part thereof was lodged by debenture holders, which are authority for the proposition that such a sale is within the ordinary

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162. *Campbell* v *Australian Mutual Provident Society* (1908) 24 TLR 623.
163. *Harris* v *Shepherd* [1975] 1 ACLR 50, 55.
164. Dickerson, *op cit*, para 370, *contra* Eisenberg, *Structure*, *op cit*, 256. Dickerson appears to state the position applying under British precedent.

and proper course of business[165]. More immediately in point is a nineteenth century Victorian decision to the effect that where neither the legislation nor the articles of association makes any relevant provision the directors do not need to seek authority from the general meeting for a sale of part of the property of the company[166]. Circumstances alter cases, however, and there are situations in which it would be impossible to maintain that such a sale was in the ordinary course of business.

It has been held that the directors' powers are conferred to allow them to conduct, not to destroy, the business of the company. On this basis the directors' power to commence winding up a company by selling off its property before consulting the general meeting has been denied[167]. An early decision to the effect that the board had power to sell off a shipping company's vessels may be distinguished on the basis that there was a special power in the articles[168]. There is a Canadian case holding that the board had power to take actions preparatory to a dissolution without consulting the general meeting[169]. The judge there did point out that the questionable assignment did not necessarily lead to dissolution but did not rely on this argument to found his decision. The decision seems to have been influenced by the view that the directors owed certain duties to the company's creditors, a view not widely supported by Anglo-Australian authority despite a recent decision of the High Court[170].

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165. *Re H.H. Vivian & Co Ltd* [1900] 2 Ch 654; *Re Borax Co* [1901] 1 Ch 326.
166. *Baw Baw Sluicing Co* v *Nicholls* (1883) 9 VLR 208.
167. *Re Standard Bank of Australia* (1898) 24 VLR 304; *Re Bermacley Products Pty Ltd* [1942] ALR 276; *Re Wolfe & Son Pty Ltd* [1972] QWN 50.
168. *Wilson* v *Meirs* (1861) 10 CBNS 348, 142 ER 486.
169. *Harvey* v *Whiting* (1887) 14 SCR 515 per Gwynne J: "It is the management of the affairs of the company and the power to make any description of contract which the company may legally make which is vested in the directors."
170. *Walker* v *Wimbourne* (1976) 50 ALJR 446; see note in (1977) 40 Mod L Rev 226.

Both the American Model Business Corporations Act[171] and the Canadian federal legislation[172] draw a distinction between a sale in the ordinary course of business and a sale outside this category, requiring shareholder approval for the latter. Eisenberg states that these provisions were enacted to overcome the common law rule that sales of substantially all the assets were *ultra vires* without unanimous shareholder approval[173]. This was because it breached an implied contract among the shareholders to further the corporate enterprise. This common law rule, however, does not seem on the authorities above to have been applied in Canada. It is suggested that similar provisions should be adopted in Australia. Furthermore, companies should be encouraged to include in their articles provisions calling for shareholder approval of all transactions that would significantly alter the nature of the business pursued by the company whether by way of expansion or contraction. There will be problems in defining a significant alteration but the solutions to these problems could come from the companies themselves. To be of any practical significance, such provisions would, however, have to apply to changes that did not destroy the substratum of the company, as changes of that magnitude will found actions for dissolution of the company[174].

The powers of management entrusted to the directors by regulation 73 are expressed to be powers of management of the business of the company. It might be possible to argue that these powers are confined to running the enterprise owned by the company. Such a suggestion would give the board of directors full powers to deal for the company with relations between the company and outsiders but would deny them powers to make decisions

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171. Mod Bus Corp Act Ann 2d ss 78 and 79.
172. Can Bus Corp Act s 183(2).
173. Eisenberg, *Structure, op cit*, 256-257.
174. *Re Tivoli Freeholds Ltd* [1972] VR 445; *Cotman* v *Brougham* [1918] AC 514.

on questions arising within the company itself. The board would still be able to make such decisions where the articles contained specific provisions to this effect. Such specific powers are contained in the Table A articles[175], so the argument is practically irrelevant. Moreover, it would tend to be negated by the fact that in *Scott* v *Scott*[176], the court referred to the articles entrusting the management of the business to the directors in order to settle a dispute as to the general meeting's ability to order the board to make certain payments to the shareholders. This decision does not, however, decide the point because it was pointed out in the judgment that such payments would threaten the board's ability to carry on the enterprise.

(b) Powers not Required to be Exercised by the General Meeting

The directors are authorized by regulation 73 to exercise all the powers of the company not required to be exercised by the general meeting. In the absence of this provision, the general meeting of the company, under a common law principle derived from early corporation cases[177], would have the power to exercise in the name of the company all powers not specifically entrusted to the board of directors. This principle was held to apply to registered companies by Jordan CJ in *Clifton* v *Mount Morgan Mines Ltd*, where he said that:

> "As a general rule the shareholders assembled in general meeting may by ordinary resolution validly act on behalf of the company so as to bind the company with respect to all matters as to which no special provision is made or as to which any special provision if made is unavailable."*178*

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175. UCA Fourth sched Table A regs 13, 18, 19, 22 and 28.
176. [1943] 1 All ER 582, 584.
177. *Attorney-General* *Davy* (1741) 2 Atk 212, 26 ER 531; *R* v *Varlo* (1775) 1 Cowp 248, 98 ER 1068.
(1940) 40 SR (NSW) 31, 43. Note that Jordan CJ dissented on a question of fact.

The question arises whether the provision contained in article 73 displaces the common law principle. Gower maintains that it does[179]. But there is no binding authority to this effect. It could be argued that this clause is subordinate, and not parallel, to the clause entrusting the directors with the management of the business. If so, the power conferred would be limited by the purpose for which it is conferred and if, as mooted above, these powers are limited to dealing with the company's enterprises, then this grant of unreserved powers would be similarly restricted. This construction would, however, run counter to the general tendency in the commercial world to enlarge the power of the directorate, a tendency which was noted as long ago as 1878[180]. The requirement of legal certainty also militates against such an interpretation. Just what powers would be saved for the general meeting is unclear. This provision therefore appears to displace the common law principle.

(c) The Words of Limitation

The powers conferred on the directors by article 73 are expressed to be "subject nevertheless to any of these regulations, to the provisions of the Act and to such regulations being not inconsistent with the aforesaid regulations or provisions as may be prescribed by the company in general meeting". These words of limitation are the source of the chief controversy about the effect of the article.

The general presumption is now that the reference to "such regulations..." which, at first sight, appears to preserve the general meeting's power to

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179. Gower, *op cit*, 132.
180. See *Eley* v *Positive Government Life Association Co* (1875) 1 Ex D 20, 27.

control the board of directors in the exercise of their general powers is, in fact, meaningless[181]. However, contrary views have been expressed[182], and the presumption is still not accepted by certain commentators[183].

This presumption is now so strong that it was relied on in the recent New South Wales case of *Liego* v *Berner*[184] in the face of the alteration of the standard form to make the directors' powers subject to the Companies Act: "these articles and such regulations...as may be prescribed by the company in general meeting". Wootten J held that:

> "At first signt it might appear that on the construction of this article the general meeting did have power to bind the directors in their managerial functions by the making of 'regulations' which were something different from 'articles' and which might include any regulatory decisions of the general meeting. On fuller consideration of the articles, however, I conclude that the apparent contrast between 'articles' and 'regulations' is transparently the result of faulty drafting. It seems to me rather more likely that the revising drafts omitted to make a similar change of terminology by inadvertence...than that he was seeking by a subtle change in terminology to alter the historic meaning of the word 'regulation' in such articles and to reverse the common relationship between meetings and boards of directors."*185*

It is possible to distinguish the decision itself, as the point in issue was whether the directors could be restrained from putting certain resolutions to the shareholders until further information had been given and the facts that the objection was raised at the eleventh hour and that the plaintiff was not clearly entitled to the relief sought are

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181. See *Quinn & Axtens Ltd* v *Salmon* [1909] AC 442.
182. See for example *Marshall's Valve Gear Co Ltd* v *Manning, Wardle & Co Ltd* [1909] 1 Ch 267 as discussed above, 116.
183. Sullivan, *op cit*; Goldberg, *op cit*.
184. [1976] 1 NSWLR 502.
185. [1976] 1 NSWLR 502, 505-506.

sufficient to support it. Wootten J did not refer to the past controversy and it is therefore an open question whether he was aware of it.

When discussing the effect of the words of limitation embodied in article 73, many authorities[186] have commented on the contrast between the words in question and those found in section 90 of the Companies Clauses Consolidation Act, 1845. That section provided that "the exercise of all such powers shall be subject also to the *control* and regulation of any general meeting *specially convened for the purpose*". If a company were to adopt this phraseology today the courts would, presumably, allow the general meeting to control the exercise of the directors' general powers by ordinary resolution. Nevertheless, the difference in question, which consists of the addition of the words indicated by italics, appears too small to justify the different interpretation.

The case of *Quinn & Axtens Ltd* v *Salmon*[187] was the first in which specific attention was given to the phrase found in the modern article. Lord Loreburn LC stated there that:

> "I would require a great deal of argument to convince me that the word 'regulations' in this article does not mean the same thing as articles."

He was influenced in so holding by the fact that the first of the articles of association in question referred to the articles as regulations[188]. Warrington J, as has already been noted[189], rejected the

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186. See *Automatic Self Cleansing Filter Syndicate Co Ltd* v *Cunninghame* [1906] 2 Ch 34.
187. [1909] AC 442.
188. [1909] AC 442, 444.
189. *Thomas Logan Ltd* v *Davis* (1911) 104 LTR 914, 916: "I turn to the articles to see whether the company has delegated the power to the board or whether it has, as it undoubtedly has, with regard to some of the powers of the directors, retained the power to control them by an ordinary majority in general meeting."

contention that the general meeting lacked the power to control the board of directors in the exercise of its powers of management.

In *Dowse* v *Marks*[190], Harvey J accepted Warrington J's interpretation of a similar article and distinguished the decision of the House of Lords in *Quinn & Axtens Ltd* v *Salmon*[191] on the basis that the articles in that case were described in clause one as regulations while, he stated, the articles in the present case were referred to as such or as "these presents". In so finding, however, Harvey J had first to interpret the word "regulations" as used in the articles to be a wider reference than to the articles alone. Aicken has stated that this ground of distinction was insufficient and artificial and that the reasoning in the case was marred by the fundamental misconception that the directors received their powers by delegation[192] but he makes no comment on Harvey J's use of the redundancy argument to the effect that as it was unnecessary to state that the power contained in the article was liable to be modified by an alteration of articles, something more must be meant.

In *Scott* v *Scott*[193], however, Clauson LJ, without citing previous authority, adopted an attitude towards the article that strongly resembled that taken by Lord Loreburn LC. It was held in *Scott* v *Scott* that the words in question did not affect the duty of management imposed by the article but the effect that the words would have was not stated. An interpretation which might clarify this point is derived from an article by Goldberg[194]. He suggested that the duty of the directors is

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190. (1913) 13 SR (NSW) 332.
191. [1909] AC 442.
192. Aicken, *op cit*, 458.
193. [1943] 1 All ER 582.
194. Goldberg, *op cit*.

in the day to day management of the business, and that while the power reserved by the article to the general meeting does not allow them to interfere with any particular transaction, it does allow them to decide general questions of policy, thus laying down the limits within which the directors must contain themselves[195]. This suggestion is consistent with the normative model of corporate government outlined by Eisenberg[196], but whether the interpretation is what was intended by Clauson LJ remains unclear.

Clauson LJ also stated that if the duty to manage the business was subject to the restrictions so stated, then the question arises whether the company by prescribing such a regulation by ordinary resolution, as distinct from by alteration of the articles, would not be acting in contravention of the articles, one of which was the article which entrusted the business to the board of directors[197]. This statement also raises difficulties. It would seem that Clauson LJ must have been referring to the rules of stautory construction governing provisos and saving clauses, whereby, if the limitation which was repugnant to the operative clause was held to be a saving clause it would be treated as void while if it was a proviso it would repeal the preceding or operative clause[198]. The applicability of these rules to articles of association is uncertain and if, as would appear probable, the articles are deemed to be of the same class as wills and contracts, their construction would be governed by the attempt to ascertain intention and not by the nearly obsolete rules of stautory construction. Furthermore, it is not clear

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195. Goldberg, *op cit*, 178; see also Sullivan, *op cit*, 577.
196. Eisenberg, *Structure*, *op cit*, 14-15; see above, 79 *et seq*.
197. [1943] 1 All ER 582.
198. Edgar, S.G.G., *Graies on Statute Law*, 7th ed (London, Sweet & Maxwell, 1971) 219-220.

that the words of limitation would constitute a saving clause, nor on what basis Clauson LJ gives the operative clause such primacy.

As has been stated by Goldberg, Hornsey and Sullivan[199], the other early twentieth century cases, which are often assumed to have definitively interpreted the standard form article, are all affected by the presence of other relevant clauses in the articles giving the directors special powers or placing special limitations on these powers[200]. A more recent authority, which may come closer to giving Wootten J a basis for the assumption he made is *Omega Estates Pty Ltd* v *Ganke*[201], a 1963 decision of the New South Wales Supreme Court, in which the question arose whether a resolution of the general meeting "that the directors be urged to prosecute Mr Ganke" was sufficient to authorize the company to bring proceedings. Else-Mitchell J held that the resolution in question was insufficient on the basis that the members of a company in general meeting could not exercise powers which were vested in the directors by virtue of an article equivalent to article 73.

Although this decision makes it clear that the general meeting cannot exercise such powers, it is submitted that it does not solve the problem of the interpretation of article 73. That it is still possible to regard the problem of the interpretation of the article in question as unresolted is demonstrated by Sullivan's recent article[202]. Sullivan cites authority[203] for the proposition that both views are still

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199. Goldberg, *op cit,* 179; Hornsey, *op cit,* 476; Sullivan, *op cit,* 574-577.

200. This remark applies to *Automatic Self Cleansing Filter Syndicate Co Ltd* v *Cunninghame* [1906] 2 Ch 34, *Salmon* v *Quinn & Axtens Ltd* [1909] AC 442, and *John Shaw & Sons (Salford) Ltd* v *Shaw* [1935] 2 KB 113.

201. [1963] NSWR 1416.

202. Sullivan, *op cit,* 578.

203. *Re Argentum Reductions Ltd (UK)* [1975] 1 WLR 186.

competing for conclusive judicial approval. He states his own preference for the view expressed in *Marshall's Valve Gear Co Ltd* v *Manning, Wardle & Co Ltd*[204]. He justifies this preference on the basis that that decision gives effect in straightforward terms to the natural meaning of the regulation on which it is squarely based, in contrast to *Scott* v *Scott*[205], where there were additional reasons for the decision and in which no reference was made to previous authority. It was Sullivan's view that:

> "When an appellate court does resolve this issue it will find that under article 80 shareholders in general meeting can give controlling directions to the board in matters of management...subject to the proviso that the management function must reside in the directors."*206*

No one would argue that the general meeting could independently exercise the powers referred to. The suggestion that is advanced by Sullivan, Goldberg and others is that the general meeting can give binding directions to the board. This suggestion is not the same as a suggestion that the directors' actions in compliance with such a direction or regulation would become merely ministerial. The directors cannot be deprived of their discretion or made subservient to the general meeting but the recognition of the general meeting's power to set policy and lay down guidelines is not necessarily inconsistent with the concept of the general meeting and the board as co-ordinate bodies.

Pennington states that the reference in article 73 to regulations made by the company in general meeting may be the vestigial remains of the power to make by-laws which used to be reserved to members by the deeds

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204. [1909] 1 Ch 267.
205. [1943] 1 All ER 582.
206. Sullivan, *op cit*, 578.

of settlemnt of companies formed at common law. These by-laws were, he states, usually procedural and he suggests that "regulations" made by the company under this proviso would also need to be procedural, which requirement would leave little scope to these regulations in view of the extent of the modern articles[207]. An examination of the American cases demonstrates[208], however, that the scope of by-laws is not always as restricted as Pennington suggests, and it is suggested that, for example, the general meeting of Queensland Mines Ltd might pass a by-law requiring management to have regard to the provision of safeguards before concluding a contract for the sale of uranium. If it were accepted that article 73 allows the general meeting to make by-laws which may lay down rules of policy, then it would need to be made clear that if the intervention of the general meeting were so frequent and detailed as to exclude discretion in the implementation of the by-law or regulation, it would be unjustified under the terms of the article[209].

Regardless of the arguments advanced on either side of this controversy, if the articles are to be construed in the light of the parties' intentions in adopting them, it may be that the general assumption[210] has become effective by means of its own force. However, it should be remembered that it is a matter of construction, not a matter of law, and in the light of *Liego* v *Berner*[211], concern arises that the tendency may now be to give the assumption undue force. If the general assumption is felt to reflect the commercially desirable position, it is suggested that the statutory form should be amended so that the words will reflect the meaning and non-lawyers will not continue to be misled.

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207. Pennington, *op cit*, 502.
208. 18 & 19 Am Jur 2d Corporations ss 161, 1146.
209. Sullivan, *op cit*, 578.
210. Ford, *op cit*, [1408].
211, [1976] 1 NSWLR 502.

2. INCAPACITY OF THE BOARD

Where for any reason the board of directors is wholly incapacitatied or disabled from exercising its powers, the residual power of the shareholders meeting revives. The authority for this statement is the case of *Barron* v *Potter*[212]. The facts were that the two directors of the company, who were also the shareholders, were unable to agree. The articles gave the board the power to appoint additional directors and enabled the chairman of the board of directors to exercise a casting vote at board meetings. B refused to attend any meeting of the board. P therefore purported to hold a meeting in B's presence, without his concurrence, and by exercising his casting vote to appoint additional directors. B, on the other hand, called an extraordinary general meeting at which he succeeded in having a resolution passed appointing another set of additional directors. The question arose which appointment was valid. The argument that the company had surrendered the power to appoint additional directors to the board of directors so as to be unable to exercise it in any circunstances was rejected. The situation was distinguished from the case where there is a board ready and willing to act and, it was held, "for all practical purposes there is no board of directors at all"[213]. "If directors having certain powers are unable or unwilling to exercise them...there must be some power in the company to do itself that which under other circumstances would otherwise be done"[214].

This authority was followed in *Foster* v *Foster*[215], in which the issue

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212. [1914] 1 Ch 895.
213. [1914] 1 Ch 895, 902.
214. [1914] 1 Ch 895, 903.
215. [1916] 1 Ch 522.

was whether the general meeting could deal with the question of the appointment of a managing director where that power had been entrusted to the board of directors. In that case the board was split over the question but the chairman of the board, by exercising a casting vote, had purported to appoint herself to the position. The court held that the general meeting could ratify the action of the board and, in the alternative, that as the board could not act itself because of the internal friction and faction, the decision in *Barron* v *Potter* was in point.

Recently, in *Alexander Ward & Co Ltd* v *Samyang Navigation Ltd*[216], the House of Lords considered the question of whether the liquidator of a company could adopt proceedings which had been started in the name of the company without proper authority during a period in which the company had had no directors. Before this could be done it had to be shown that the company would have been competent to commence these proceedings. Lord Hailsham LC held that the general meeting, in the absence of an effective board, has a residual authority to use the company's powers. In so holding he rejected counsel's attempt to draw a distinction between those cases where the directors were unable or unwilling to act and those, such as the instant case, in which there were no directors at all.

If a distinction, such as that suggested between cases where the directors were unwilling or unable to act and cases where there were no directors at all, is to be drawn, it is suggested that it would be more logical to hold that the general meeting could exercise the powers entrusted to the board of directors in the latter rather than the

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216. [1975] 1 WLR 186, noted (1976) 39 Mod L Rev 327.

former case. It is tempting to argue that where a power has been entrusted to the board of directors the general meeting should not be allowed to exercise it at least where there is a board of directors in existence. It seems inequitable that Mr Barron should be able to circumvent the provisions of the company's constitution by refusing to discharge the duties of his office. However, it may be argued that quorum provisions are *inter alia* designed to prevent the board from acting when the directors fail to agree.

Nevertheless, it is hard to reconcile the theory that the board and the general meeting are co-ordinate bodies with the idea that the general meeting may exercise the board's powers if and when board members are unable to do so and even harder where board members are merely unwilling to do so. Justification for the former may perhaps be found in commercial expediency, which puts a high value on avoiding situations where no action is possible, inasmuch as action is possible in the second situation if agreement could be obtained and, as additional alternatives, the deadlock may be resolved by amending the articles of association or winding up the company. The justification is, it is submitted, inadequate to justify disregarding the company constitution. This is particularly so when it is remembered that the general meeting's powers will be exercised by a mere majority.

A reluctance to allow the general meeting to exercise the functions allotted to the board of directors might manifest itself in a suggestion to the effect that in the absence of an effective board, the general meeting should only be allowed to act to remedy the problem, as by appointing additional members of the board. However, Lord Hailsham's comments in *Alexander Ward & Co Ltd* v *Samyang Navigation Ltd* do reinforce

the doctrine of reserved powers[217]. It therefore seems unlikely that the argument advanced above against the dictates of commercial expediency will have much chance of success. It is submitted, however, that the doctrine of reserved powers discussed above is inconsistent with the twentieth century concept of the division of company powers.

3. THE CONTROL OF COMPANY LITIGATION

Further difficulties arise when the question concerns the control of company litigation. When, through registration, the company obtains recognition as a legal person, it obtains the power to sue and be sued in the courts. A concomitant of the fact that the company has this power is the rule that where a wrong is done to the company the company itself is the proper plaintiff, a rule that forms one branch of the so-called rule in *Foss* v *Harbottle*[218]. However, this rule does not settle the question of how the company is to exercise this power. While the nineteenth century view that the general meeting, as the supreme corporate body, could control the directors in the exercise of all their powers prevailed, no special problem arose in connection with the control of company litigation. The general meeting had control in all cases and although it might be that the directors under their powers of management could initiate an action, the general meeting could effectively instruct them to discontinue it. When the general meeting and the board of directors are seen as being co-ordinate bodies, the general meeting loses its power to instruct the

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217. See for example Gower, *op cit*, 136-137; Paterson, W.E. and Ednie, H.H., *Australian Company Law*, 2nd ed (Sydney, Butterworths, 1971) art 73/1 and Pennington, *op cit*, 505.

218. (1843) 2 Hare 461, 67 ER 189.

board to discontinue such an action when it clearly falls within the board's power to initiate it[219]. It is less clear, however, whether the general meeting may effectively initiate a legal proceeding themselves where the directors have taken no action[220]. The most difficult problem in the area arises when the question is whether the company will seek a remedy for a wrong done to it by its directors. Elementary principles[221] apply to prevent the wrongdoers from controlling the company in deciding whether to seek a legal remedy for the wrong done to it. However, it is unclear whether the general meeting can, by affirming the directors' actions, prevent a challenge to the transaction from succeeding if individual shareholders' rights are involved. This is the problem of ratification raised in such cases as *Hogg* v *Cramphorn Ltd*[222], *Bamford* v *Bamford*[223] and *Winthrop Investments Ltd* v *Winns Ltd*[224]. The law in this area has certain implications for the division of powers between the board of directors and the general meeting and it is with these that this paper is concerned. This limitation is stressed because of the vast number of cases and comments in this area, a thorough examination of which might well form the subject of a doctoral thesis.

(a) Litigation under the Control of the Board

Where the right of the company which the legal proceedings are designed to invoke or enforce does not arise out of a wrong done to it by its

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219. *John Shaw & Sons (Salford) Ltd* v *Shaw* [1935] 2 KB 113.
220. The resolution in question in *Omega Estates Pty Ltd* v *Ganke* [1963] NSWR 1416 stopped short of initiating an action, merely urging the directors to do so.
221. See *Dey* v *Pullinger Engineering Co* [1921] 1 KB 72; *Remfrey* v *Aloha Cruises Pty Ltd* [1968] QWN 44.
222. [1967] Ch 254.
223. [1968] 2 All ER 655, affirmed [1970] Ch 212, [1969] 1 All ER 962.
224. [1975] 2 NSWLR 666.

directors, it would appear to be established that it is the board of directors that has power to control the litigation. Various decisions, some of which have been cited already in the discussion of the general theory or of article 73, are found to support this statement.

Thus it was decided by the Court of Appeal in 1935 that where the directors are given specific power over company litigation, the general meeting cannot instruct them to discontinue such action[225]. In 1963 the New South Wales Supreme Court held that it was within the directors' power under article 73 to commence litigation and that a resolution of the general meeting urging them to do so was insufficient authority for such proceedings in the absence of a resolution of the board of directors acceding to the request[226].

However, there is English authority for the proposition that where the board fails to commence proceedings, the general meeting's resolution will effectively authorize such an action irrespective of whether the board had properly exercised its discretion in deciding not to take such action[227]. If the power to commence legal proceedings falls within the scope of article 73, as it appears to do where internal relationships are involved, this decision is clearly wrong. Even if the general meeting could control the directors' powers in minute detail under the terms of the words of limitation found in the article the company still has no power to act without a resolution of the board of directors.

In 1965, Hudson J of the Victorian Supreme Court, deciding an action in

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225. *John Shaw & Sons (Salford) Ltd* v *Shaw* [1935] 2 KB 113.
226. *Omega Estates Pty Ltd* v *Ganke* [1963] NSWR 1416.
227. *Marshall's Valve Gear Co Ltd* v *Manning, Wardle & Co Ltd* [1909] 1 Ch 267.

which the plaintiff shareholder sought to assert a personal right, held *obiter* that the plaintiff, although a majority shareholder, could not have obtained from the general meeting a valid authority to bring the action in question. The power to decide whether such an action should be brought was vested in the directors under an article equivalent to article 73 and this could not be overridden by any ordinary resolution[228].

A recent decision of Fullagar J's may be referred to[229]. An attempt was made by the liquidator of a company holding the entire beneficial interest in a subsidiary to have the subsidiary wound up without going through the formality of holding a general meeting. It was held that by virtue of article 73 of Table A the directors held the powers of management of the company to the exclusion of the shareholders until such time, if ever, as the shareholders, acting within the articles and the Act, or unanimously, moved control into their own hands[230]. The shareholder had, therefore, no right to act for the company in seeking a court order to wind up the company and this in spite of the fact that the court's jurisdiction was invoked under the provision in section 222(1)(a) which authorizes the court to order the winding up if the company has by special resolution resolved that it be wound up.

Unfortunately this decision fails to resolve the point in issue precisely because no general meeting was held. What would the holding have been if the general meeting had been held and had resolved for winding up, and the directors had refused to seek the necessary court

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228. *Kraus* v *J.G. Lloyd Ltd* [1965] VR 232, 236.
229. *Re Action Waste Collections Pty Ltd* (1976) 2 ACLR 253.
230. (1976) 2 ACLR 253, 259.

order? The situation is unlikely to arise but if it did, it is submitted that the court would distinguish between the situation where the board's powers are merely ministerial and those where the board retains a discretion.

The fact that the suggestion, made in 1909, that the general meeting can authorize the company to take legal proceedings, cannot be decisively put to rest or supported reflects the fact that the point in issue lacks practical significance. In almost all cases where the decision of the board not to sue is unsatisfactory the individual shareholder will be able to bring either a personal or a derivative action. In many cases the difficulties in securing a resolution from the general meeting will outweigh even the difficulties of bringing a derivative action. At the moment, however, let it be noted that although the decision in the case of *Foss* v *Harbottle*[231] itself was founded on the premise that the general meeting had power to bring an action in the company's name, the rule derived from that case is not necessarily dependent on that premise. The exceptions could apply equally where the original decision is made by the board instead of the general meeting[232].

(b) Ratification

The elements of ratification in the simple agency situation are straightforward and well understood. Where a person purports to perform an act in the capacity of agent for a named party, that party may later adopt the action, although no prior authorization existed, if certain conditions are fulfilled. These conditions are that there must have been a

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231. (1843) 2 Hare 461, 67 ER 189.
232. Ford, *op cit*, [1411].

competent principal at the time the agent acted; that the action must be adopted with full knowledge of the circumstances or with an intention of adopting it regardless of circumstances; and that the adoption must be by a party who is capable of doing the act in question whether he be principal in his own right or a duly authorized agent for the named principal[233]. Ratification is, by virtue of a legal fiction, deemed to be equivalent to a prior authorization[234]. The principle that a body of persons not competent to authorize an act cannot give such an act validity by ratifying it was held to apply to companies by the Privy Council in 1877[235] but the decision did not rely on this principle.

Where the general meeting has the power to authorize a certain act by means of an ordinary resolution, it must be undisputed that they can also adopt or ratify such an act by such a resolution[236]. Suggestions that a larger majority is necessary[237] are seen, on examination, to have been made only where the act does not fall within the original competence of the general meeting.

(c) The Modern Problem: Pseudo-Ratification

The question of ratification raises no new problems in the company law field, where the power to do the impugned act vests originally in the general meeting. The principal is the company but the principal may

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233. Treitel, G.H., *Law of Contract*, 4th ed (London, Stevens & Sons Ltd, 1975) 496-500.
234. *Firth* v *Staines* [1897] 2 QB 70; *Davison* v *Vickery's Motors Ltd* (1925) 37 CLR 1; *Danish Mercantile Co* v *Beaumont* [1951] Ch 680.
235. *Irvine* v *Union Bank of Australia* (1877) 2 App Cas 366.
236. *North West Transportation Co* v *Beatty* (1887) 12 App Cas 589, 593.
237. *Spackman* v *Evans* (1868) LR 3 HL 171; *Evans* v *Smallcombe* (1868) LR 3 HL 249; *Re Beaconsfield Heights Estates Co Ltd* (1896) 22 VLR 97.

may ratify the actions of one agent through the agency of another if that second agent originally had the power to do the act in question[238].

However, where the articles vest the original power in the directors, the question arises whether the general meeting has a constitutional authority to approve the exercise by the directors for a collateral or otherwise improper purpose of their fiduciary powers[239]. If the general meeting does possess the authority to approve an improper exercise of the powers of the board of directors, how is this to be reconciled with the concept established in *Cunninghame's* case[240] that the shareholders have no power to interfere with or control the use of these powers in ordinary situations. One of the preconditions for ratification proper, that the person or body ratifying the action in question is competent to do that act, is absent, thus the term pseudo-ratification has been adopted here.

This problem did not arise in the nineteenth century when the general meeting was seen as occupying a supervisory role in relation to the board of directors. In the light of that concept of internal relations of the company it was possible to apply the principles of ratification evolved under agency law. However, this view of company relationships is is no longer entertained, and so company law in this area is faced with a new and modern problem.

Buckley J was the first to suggest, in his judgment in *Hogg* v *Cramphorn Ltd*[241], that the general meeting might ratify an improper exercise of the

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238. The general rule that an agent cannot delegate is inapplicable here as the general meeting will always act by delegating its powers.
239. See for example *Bamford* v *Bamford* [1968] 2 All ER 655, affirmed [1970] Ch 212, [1969] 1 All ER 962.
240. *Automatic Self Cleansing Filter Syndicate Co Ltd* v *Cunninghame* [1906] 2 Ch 34.
241. [1967] Ch 254.

directors' power to issue shares. Problems arose because under the law as it stood then, and now, the general meeting could not control the use of this power. To hold that they could nevertheless approve an improper use of it seemed anomalous[242]. However, the suggestion so obviously met a practical difficulty that efforts have since been made to reconcile it with theory. These have taken two forms, the reserve powers approach and the waiver of company rights approach. It is also possible to suggest a third or co-ordinate powers approach which is in effect a modification of the reserve powers approach. Each of these theories is less than completely satisfactory.

(i) Reserve Powers

The first judicial attempt to find a theoretical basis for pseudo-ratification was that of Plowman J in *Bamford* v *Bamford*[243]. This judgment was strongly influenced by the arguments presented to the court which centred on the issue of whether the general meeting had reserve powers to issue shares by simple majority. It was conceded that, in the absence of anything in the articles, a company had inherent power to allot its unissued shares by ordinary resolution[244]. Dispute centred on the contention that the articles vested the power to allot shares in the directors alone and therefore the directors had no power to delegate the power to shareholders in general meeting. Any concurrent power of "the company itself" was necessarily excluded. The line of cases which stands for the proposition that the general meeting cannot override or usurp the authority of the board of directors was reviewed

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242. Wedderburn, K.W., "*Shareholders' Control of Directors' Powers: A Judicial Innovation*" (1967) 30 Mod L Rev 77, 82.
243. [1968] 2 All ER 655.
244. [1968] 2 All ER 655, 660.

before it was held that no attempt had been made to do so. What had happened was that the general meeting had answered a question referred to it by the board of directors. The objection that this was to alter the nature of the power by freeing it from the restraints of fiduciary obligation was dismissed on the ground that the power entrusted to the directors, limited as it was by the requirement that it be exercised in the interests of the company, was less extensive than the company's inherent power. This left a residual power in the company to issue shares other than for the best interests of the company, a power limited only by the requirement that it not be exercised so as to conflict with the express power[245]. Plowman J held that the company in general meeting had exercised this residual power.

There are many unresolved difficulties inherent in this judgment but at least it was potentially consistent with the organic or twentieth century view of the division of power. As Lindgren has explained,

> "Constitutional organic theory cannot accommodate the possibility of ratification by the general meeting by positing the board as agent of the corporate entity. It can, however, embrace a notion of the general meeting as the general constitutional organ of the body corporate which will have power both to implement and to ratify implementation of all those parts of the company's capacity which are not...vested exclusively in the board of directors."*246*

If the company is deemed to have a power which the directors cannot exercise, then that is a power which, under the reserve powers theory, can be exercised by the company in general meeting.

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245. *Bamford* v *Bamford* [1968] 2 All ER 655, 665.
246. Lindgren, K.E., *"The Ampol-Howard Smith Affair"* (1947) 11 U WA L Rev 384, 385.

Lindgren objects to the suggestion that the company has a power to allot shares other than in its own best interests[247]. Inasmuch as company powers are limited by reference to the objects stipulated in the memorandum[248], this objection is well founded. However, it is suggested that powers should not be defined by reference to the purpose for which they are used. The power to allot shares is, it is suggested, abused, not exceeded, when shares are allotted other than in the best interests of the company. The law does not, however, prevent natural individuals from acting without reference to their own interests and at least one early case can be cited in which a court refused to ask whether the general meeting's decision was in the interests of the company[249]. Thus it is suggested that problems arise precisely because the company is not acting for itself but through agents. Agents will not be allowed to abuse their powers. The directors, therefore, will be prevented from issuing shares other than in the best interests of the company. The shareholders, under the authority of *North West Transportation Co* v *Beatty*[250], need not consult the interests of the company in making the decision. This is a concept which does create difficulties, but it should be noted that the power of the majority, as distinguished from the individual shareholders, to act against the interests of the company is limited by the concept of fraud on the minority[251]. Of course this suggestion needs a much deeper examination than has been attempted here. but the suggestion is offered for what it is worth and it is hoped that

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247. Lindgren, *The Ampol-Howard Smith Affair, op cit*, 385.
248. *Ashbury Railway Carriage and Iron Co* v *Riche* (1875) LR 7 HL 653, [1874-80] All ER Rep 2219.
249. *Exeter & Crediton Railway Co* v *Buller* (1847) 16 LJ Ch 449 as discussed above, 107.
250. (1887) 12 App Cas 589.
251. Ford, *op cit*, [1701]-[1707].

it can be taken up on another occasion.

The major difficulty with the first instance decision in *Bamford* v *Bamford* or, at least, the difficulty which caused Plowman J's reasoning to be rejected by the Court of Appeal lay in the fact that the general meeting had not purported to allot the shares itself[252]. The point has also been made by a commentator who queries whether Plowman J would have allowed the shareholders to initiate the allotment[253].

(ii) Powers held in Conjunction

The objection that the general meeting did not purport to initiate the allotment can be overcome by arguing that what the general meeting did was not to exercise a reserve power over which it had sole jurisdiction but to concur with the board of directors in exercising a power held in conjunction by both bodies.

The basic argument here would be that, under the memorandum, the company obtains certain powers which must be exercised by one or both of its organs. The company's powers are divided between its organs by the articles of association but a problem arises where, although a power is allocated to the board of directors, the board is unable to exercise it effectively because of an improper purpose or some other supervening cause. The general meeting cannot exercise a power which has been allocated to the board of directors. The result, unless some solution is found, will be that the company is left in possession of a power that it cannot use. It is conceded, therefore, that joint action by both company organs will be effective where neither organ can act alone.

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252. *Bamford* v *Bamford* [1969] 1 All ER 969, 973.
253. Prentice, D., "*Comment: Bamford v Bamford*" (1968) 47 Can Bar Rev 658, 661. See also *Winthrop Investments Ltd* v *Winns Ltd* [1975] 2 NSWLR 666, 682.

The judgment of Harman LJ in *Bamford* v *Bamford* on appeal is consistent with this approach. He held that:

> "The power to allot shares is clearly something within the powers of the company and it is therefore an *intra vires* power and one which the company can ratify."*254*

Harman LJ appears to have made no attempt to reconcile his decision with any theory of division of powers. However, unless the suggestion put forward here is adopted, his judgment can only be interpreted as a reversion to nineteenth century theories.

The judgment of Mahoney JA in the recent New South Wales case of *Winthrop Investments Ltd* v *Winns Ltd*[255] appears to offer direct support for the theory of powers held in conjunction. He conceded that in normal circumstances the power in question would be one which the directors had exclusive power to exercise but held that certain aspects of company business, including the power to approve a transaction which involved a benefit to the directors, must by implication remain with the shareholders in general meeting. However, it is conceded that the other judgments in the case are not equally consistent with the suggested approach.

If this approach is adopted, the effect of a resolution passed by the general meeting approving a voidable act of the board of directors would be to put the transaction beyond question, unless the resolution of the general meeting is itself impeachable. Not only the company's own rights to seek a remedy in respect of the challenged act but also the rights of all individual shareholders to do so either in their own right

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254. *Bamford* v *Bamford* [1969] 1 All ER 969
255. [1975] 2 NSWLR 666.

or in that of the company would vanish. If the general meeting, when the question was referred to it, were to refuse its approval, the act of the directors would remain voidable. The refusal to approve would not *ipso facto* cause the transaction, if carried through, to be avoided, but attention would have been drawn to it. It would remain open to challenge by the liquidator, or by a dissident shareholder, and in the event that such a challenge were mounted it is likely that the fact that approval was sought and refused and that the directors persisted with the transaction would carry evidentiary weight.

Such an approach contemplates that the decision of the board must be made independently of the decision by the general meeting. Although it is logically irrelevant which decision is first in point of time[256], it would only be necessary to appeal to the general meeting where the fiduciary obligations of the directors would prevent their decision from being effective. It would be necessary, therefore, for the board members to disclose to the shareholders those factors which, at least putatively, necessitate such a referral[257]. They would be enabled to circumvent the disqualification imposed by the fiduciary nature of their office but not to ignore it.

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256. Pennington, *op cit*, 505; see also McPherson, B.H., "*Duties of Directors and Powers of Shareholders*" (1977) 51 ALJ 460, 466.

257. See *Winthrop Investments Ltd* v *Winns Ltd* [1975] 2 NSWLR 666, 703 where Mahoney JA considered the suggestion that the resolutions of the general meeting be considered as a consent presently operative to validate in advance the proposed transaction, a suggestion which was apparently put forward to overcome the deficiencies of notice. Mahoney JA did not indicate whether in those circumstances disclosure requirements would be relaxed.

(iii) Waiver of Rights

A legal person, under our adversary form of litigation, may elect to seek a legal remedy for any wrong done to him or it. It is implicit in this statement that the option of deciding not to seek a remedy is also open. A waiver of legal rights takes place when a decision not to start legal proceedings becomes binding on the elector.

When a wrong has been done to the company by a member or members of the board of directors, the board cannot exercise the company's power of election by means of a decision founded on the votes of the wrongdoers. The fiduciary duty of board members would prevent such an election from binding the company[258]. A solution to this problem is to give the power of election in such cases to the general meeting. This is, some suggest, the sole effect of what is here called pseudo-ratification.

Russell LJ's decision in *Bamford* v *Bamford* rested on this ground. The wrong as the Court of Appeal saw it had been done to the company alone[259]. He held that

> "impropriety by the directors in the exercise of their undoubted powers is a proper matter for waiver or disapproval by ordinary resolution."[260]

Samuels JA of the New South Wales Supreme Court also based his decision in *Winthrop Investments Ltd* v *Winns Ltd* on this theory. He assumed that the shareholders had a dispensing power which they could use to validate an improper act of the directors but held that the power was limited by its purpose which was to release the rights which the company would

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258. See *Winthrop Investments Ltd* v *Winns Ltd* [1975] 2 NSWLR 666, 669 per Mahoney JA citing *Regal (Hastings) Ltd* v *Gulliver* [1942] 1 All ER 378; see also *Furs Ltd* v *Tomkies* (1936) 54 CLR 583.
259. [1969] 1 All ER 969, 976.
260. [1969] 1 All ER 969, 976.

otherwise be able to assert[261].

There are problems relating to the effect that such a waiver will have on actions or legal proceedings initiated by the individual shareholder. These problems are relevant to the question of the division of powers between the general meeting and the board of directors only inasmuch as the answer arrived at may provide a policy argument for denying the general meeting any power of decision. For this reason a thorough analysis of these thorny problems is not offered here. Some reference to these questions is, nevertheless, necessary.

If the resolution of the general meeting "ratifying" the transaction in question is seen as a waiver of company rights, then any derivative action which an individual shareholder might institute would obviously fail unless for some reason the general meeting could not effectively waive the company's rights. This would be the position where, for example, such a waiver would constitute a fraud on the minority[262]. The suggestion that the possibility of such a waiver will not be sufficient to act as a bar to a derivative suit[263] seems compatible with the decisions and desirable from the point of view of policy.

When pseudo-ratification is seen to operate as a waiver of company rights it must be regarded as a form of estoppel. There is no new act, nor is there any new basis of validity for the act; and the estoppel only binds the company itself. It is, therefore, clear that waiver of

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261. *Winthrop Investments Ltd* v *Winns Ltd* [1975] 2 NSWLR 666, 681, 684.
262. See cases discussed by Ford, *op cit*, chapter 17, for example *Cook* v *Deeks* [1916] 1 AC 554; note fraud on the minority is not a question of whether the directors have made full disclosure.
263. Wedderburn, *op cit*, 82.

company rights cannot affect any personal rights the shareholders might have. Those who vote to waive company rights, however, might also be seen to waive their own personal rights at the same time. The cases suggesting that ratification can only be effected by unanimous shareholder agreement[264] may be explained on this basis.

Dissatisfaction with the concept of allowing the general meeting to waive the company's legal rights to a remedy against directors who breach their fiduciary duties has been expressed in various quarters. The Bullock Committee, concerned to protect and institutionalize the employee's interest in the company, suggests that before such a ratification is allowed, the approval of both board and general meeting should be required[265]. This suggestion is compatible with the co-ordinate powers approach suggested above. It is also possible to adapt it to the waiver of rights approach although it would be necessary to clarify the question of whether the wrongdoers might themselves have a voice in such a decision.

Another sort of criticism comes from those who, like McPherson[266], suggest that the general meeting should not have the authority to permit directors to misappropriate assets, to misuse their powers or to retain for themselves the benefit of doing so. It may be that there are grounds for distinguishing between these different categories of questionable transaction, holding that only some of them are ratifiable. Setting this question aside, it is submitted that, although it may "seem

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264. *Provident International Corporation* v *International Leasing Corporation* (1969) 89 WN (Pt 1)(NSW) 370, 382 per Helsham J: "I do not think that a general meeting can resolve that the directors should act in abuse of their powers or that such an abuse can be ratified where it has resulted in a breach of duty of a fiduciary nature owed to some person not a party to the resolution to ratify." See also *Union Bank* v *South Canterbury Building & Investment Co Ltd* (1894) 13 NZLR 489.
265. Great Britain, Department of Trade, *Report of the Committee on Industrial Democracy*, (1977) para 7.31, hereinafter referred to as the *Bullock Report*.
266. McPherson, *op cit*.

slightly ridiculous that the law should impose on directors a set of obligations which they are at liberty to ignore if they control the general meeting"[267], the fact remains that modern courts have recognized, and modern managements have welcomed, the suggestion that the general meeting does have certain powers of "pseudo-ratification". However they are explained, these powers are likely to continue to be recognized.

(d) Summary: Control of Company Litigation

This power is not specifically allotted to either the board of directors or the general meeting under the companies legislation and the Table A articles as they stand at the moment. It is clear, however, on case authority that the board of directors may initiate legal proceedings against outsiders under the power they derive from article 73 and its equivalents. When they do so the general meeting cannot effectively instruct them to discontinue such activities. It is equally clear, under the law as to reserve powers discussed above[268], that the general meeting will have the power to authorize proceedings in the name of the company when there is no board of directors or when the board is unable to act. It remains unclear whether the general meeting will have power to commence proceedings against outsiders where the board declines to do so. No occasion has arisen in which a court has been asked to decide a case on exactly these facts. The situation is more confused where the company derives a right of action against some or all of the members of the board of directors. This can happen in two situations: where the board of directors has no power to do what they have purported to do, in

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267. McPherson, *op cit*, 469.
268. *Alexander Ward & Co Ltd* v *Samyang Navigation Co Ltd* [1975] 1 WLR 673, as discussed above, 141-143.

which case if the action is within the powers of the company, the general meeting itself must have power to perform the action in question. If the general meeting had the power to do the action, the ordinary principles of agency apply and they may ratify the action of the board of directors even though both bodies are agents of the company. The second situation arises when the board of directors would have power to perform the act in question but for a vitiating factor such as improper purpose. This paper does not canvass the questions of what will amount to a vitiating factor or whether indeed this concept is correct. If the second situation arises, "pseudo-ratification" would seem, on authority, to be available, but neither the theoretical basis nor the exact effects of such a resolution are clear. It seems that either the resolution operates as nothing more than release or waiver of the company's rights not affecting the status of the transaction itself, which remains voidable if a shareholder can establish an individual right against the board, or the resolution operates to change the status of the transaction so that it is no longer voidable but becomes a valid act of the company. If the resolution is, in fact, capable of validating the transaction it must be because in such circumstances the general meeting has power to carry out the transaction by itself, or because the general meeting has power to act in conjunction with the board of directors to exercise a power which the board cannot exercise by itself under the circumstances which obtain. It is submitted that there are reasons to prefer the second of these explanations. These include the fact that this explanation is more compatible with the twentieth century concept of the board of directors and the general meeting as co-ordinate bodies.

F. THE PROPER SUBJECT CONCEPT
AN AMERICAN INNOVATION

1. RELEVANCE OF THE CONCEPT

In the foregoing sections an attempt has been made to define the powers of the general meeting and the board of directors. The question has been which organ of the company will have the power to commit the company to a course of action. A related, though not identical, problem is the question of which matters may be considered by each organ. The board of directors can and usually does consider all questions submitted to the general meeting including such things as alterations of articles over which they have no specific powers at all. Further, the board of directors can and usually does make recommendations to the general meeting as to the action it should take on these matters. The general meeting's power to consider matters which must be decided by the board of directors is much less frequently used.

Does the general meeting have the power to consider such matters, subject to compliance with notice provisions? Neither the Uniform Companies Act nor the British Companies Act has anything specific to say on this subject, and case law is not much better[269]. Reasons for the lack of case law on the subject are not hard to find. Where the board of directors wishes to seek the views of the general meeting on a question of policy, the propriety of such action is unlikely to be questioned by

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269. Getz, L., "The Structure of Shareholder Democracy" in Zeigel, J.S., *Studies in Canadian Company Law*, (Toronto, Butterworths, 1967) vol 2, 262: "There is no Anglo-Canadian jurisprudence that would support [the conclusion that matters of business policy are reserved to the directors]. All the case law concerns specific attempts to instruct the directors in respect of particular transactions and none is capable of sustaining the view that general policy is, exclusively, in the hands of the directors."

any party and, if it were, it would be almost unthinkable for any jurisdiction to prohibit the board from seeking an advisory opinion, at least[270]. Passing note might be taken of a recent New South Wales case in which a shareholder sought an injunction to prevent voting on an advisory resolution submitted by the board of directors to the general meeting until more information had been given[271]. The injunction was refused. Where a shareholder submits a proposal for a policy resolution there is more likely to be a conflict, but the rebuffed shareholder is unlikely to bring the matter before the courts because he lacks any economic incentive to do so[272].

In North America much greater attention has been given to the questions of what matters the general meeting may discuss and what resolutions it may pass. The concept of "proper subject" has there been defined but this has not happened within the context of the state corporation laws.

Instead, it has occurred within the scope of the federal securities legislation. Under the Securities Exchange Act, 1933, the Securities and Exchange Commission was set up. One of the powers it was given was the power to make and enforce rules governing the solicitation of proxies. The Securities and Exchange Commission developed a rule requiring corporate managements to include in their proxy solicitation materials any resolution proposed by a shareholder that constituted a "proper" subject for action by the shareholders.

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270. Schulman, S., "*Shareholder Cause Proposals: A Technique to Catch the Conscience of the Corporation*" (1971-72) 40 Geo Wash L Rev 1, 64.
271. *Liego* v *Berner* [1976] 1 NSWLR 502.
272. Schwartz, D.E. and Weiss, E.J., "*An Assessment of the Securities and Exchange Commission Shareholder Proposal Rule*" (1977) 65 Geo LJ 635.

This rule serves a function analogous to the provision in the Australian Companies Acts requiring managements in certain circumstances to give notice of resolutions which shareholders propose to put forward at the next annual general meeting[273]. However, probably because of the relative ease and availability of administrative enforcement procedures, the American provisions seem to have been much more widely used[274]. One American commentator, discussing recent usage of the rule, has stated that since at least 1970 there have been three separately definable classes of shareholder proponents. The first class are the champions of the minority shareholders, the corporate "gadflies" concerned with such things as pre-emptive rights, cumulative voting, and reports to shareholders. The second class is made up of individual shareholders who submit proposals on matters of specific concern. The third class of proponents consists of individuals who represent organizations seeking to further specific social goals, such as concern for the environment or equal opportunity for some disadvantaged group[275]. There can be no argument as to the desirability of allowing the first two groups to bring matters before the meeting and so long as the proposal made by the third group is related to the company's business, a requirement that is discussed below, the same holds true.

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273. UCA s 143.

274. Australian statistics are not available. The annual reports of the Securities and Exchange Commission show that in 1956 143 proposals were submitted of which 102 were included in proxy statements (United States of America, *Twenty-Second Annual Report of the Securities and Exchange Commission*, (1956) 34); that in 1957 216 proposals were submitted of which 177 were included (United States of America, *Twenty-Third Annual Report of the Securities and Exchange Commission*, (1957) 75); that in 1958 211 proposals were submitted of which 165 were included (United States of America, *Twenty-Fourth Annual Report of the Securities and Exchange Commission*, (1958) 79). In 1976, of the proposals submitted, 477 were included, while 268 were omitted (United States of America, *Forty-Second Annual Report of the Securities and Exchange Commission*, (1976) 62).

275. Black, L.S. and Sparks, A.G., *"The SEC as Referee - Shareholder Proposals and Rule 14a-8"* (1976) 2 J Corp L 1, 3-4.

Although the Securities and Exchange Commission is obliged to use a consultative process in the introduction of amendments to the regulations, it remains relatively easier to amend administrative regulations than it would be to amend legislation. Accordingly, the rules defining proper subject have been repeatedly revised and are therefore very fully developed.

Although the history of these revisions will not be traced here in detail[276], it may be noted that the formulation adopted by the Securities and Exchange Commission in 1954 stood unaltered until 1972 when major alterations were introduced. Further changes to the rules were made in 1976. In 1977 the Securities and Exchange Commission undertook a re-examination of the rules relating to shareholder communications in which the shareholder proposal rule again arose for review. However, no changes to this rule have as yet resulted from this latest review[277].

Canadian legislation[278] also embodies a detailed definition of the proper subject concept that is modelled on the American shareholder proposal rules as they stood before the 1972 revision.

It is suggested that such a detailed definition should also be incorporated into Australian company law. This would have the effect of

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276. See Silvers, M.H., *"Shareholder Proxy Rules: An Available Means to Increase Corporate Social Consciousness"* (1976) 1 Glendale L Rev 317, 319.
277. Securities and Exchange Commission Release No 34-13482 (5.4.77); Securities Reg and Law Report (BNA) No 401 G-1; Securities and Exchange Commission Release No 34-13901 (8.31.77): Securities Reg & Law Report (BNA) No 418 H-1; Securities and Exchange Commission Release No 34-14970 (7.19.78): Securities Reg & Law Report (BNA) No 462 F-1.
278. Can Bus Corp Act s 108.8.6(c). See Getz, *op cit*, 255-264.

expanding the matters which the general meeting could consider inasmuch as the general rule now seems to be that where the board of directors under regulation 73 of the Table A articles has the power to decide a matter, then the general meeting will not consider it unless asked to do so by the board of directors. This is not considered to be either desirable or necessary.

Because it is suggested that a comparable definition of "proper subject" be incorporated into Australian company law, an analysis of this definition is now undertaken. Under both the Canadian and the American provisions, corporate managements must include any proposals submitted by a shareholder in its proxy materials unless it can establish that there are grounds on which it can be excused from compliance. There are three major substantive grounds, that is, grounds having to do with the subject matter of the proposal on which management may rely. Proposals may be omitted if they are unconstitutional, or if they relate to ordinary business matters or general causes.

2. CONSTITUTIONALITY OF PROPOSALS

The term "constitutionality" has been adopted from Getz[279]. A proposal will be unconstitutional when it would involve the general meeting in passing a resolution which it is forbidden to pass under the relevant companies legislation or under the constitution of the company itself. Thus the Securities and Exchange Commission's rules allow corporate management to omit a proposal which is not a proper subject for action by the

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279. Getz, *op cit*, 253-255, 261.

shareholders under the law of the issuer's domicile[280]. The reference to issuer is a reference to the corporation which issues the proxy solicitation materials to which the rules relate. This provision, which was first adopted in 1954, is preserved in the rules as they stand today and is also found in the Canadian Act[281].

The stockholder proposal rule is not designed to upset the theory of division of powers outlined above, nor does it allow the company's members to exercise powers entrusted to the directors. Rather, it is designed to allow the general meeting to exercise what powers it does have independently of the board of directors and in addition to allow the general meeting to act as a consultative body on the motion, not only of the board of directors, but also of the individual shareholder who should have some avenue for gathering a consensus of his fellows on matters that concern the company.

(a) The Relationship between State Law and the Shareholder Proposal Rules in the United States

The difficulties in reconciling the law relating to the division of powers and the laws governing the scope of the shareholder proposal were compounded in the United States by jurisdictional problems. These problems were created by the fact that it was state law that defined the division of powers and federal administrative rules that defined the scope of the shareholder proposal.

Despite the reference in the shareholder proposal rule defining proper

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280. Code of Federal Regulations s 240.14 a.8(c)(1).
281. Can Bus Corp Act s 131.

subject to the law of the issuer's domicile[282], the relationship between the two remained unclear. There were two reasons for this perplexity, first, the presence of other clauses in the rule which might seem to further restrict the range of proper subject and secondly, the decision in the case of the *Securities Exchange Commission* v *Transamerica Corporation*[283].

The facts in that case were that Transamerica refused to include certain proposals in its proxy statement. The Commission took action to enforce its proxy rules. The court of first instance held that all but one of the proposals were improper in that they were not permissible under state law. The appeal court, however, held that none of the proposals could be excluded. In particular it held that there was no logical basis to conclude that the proposal as to post-meeting reports was not proper under state law. The significance of the decision was, therefore, that it put the onus of proving that a subject was not proper on those seeking to exclude the proposal.

There is no agreement among the commentators as to whether state law is more or less restrictive than the Commission rules. Thus L. Gilbert protested strenuously against the proposed 1954 amendments because he saw them as threatening to replace the "Transamerica rule" with the rule of state law under which, he asserted, virtually no subjects would have been proper for shareholder proposals[284]. Others disagreed with this view of state law, asserting that far from allowing proposals not

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282. Code of Federal Regulations, s 240.14 s.8(c)(1).
283. (1947) 163 F 2d 511 (Civ Ct of Aps).
284. Gilbert, L.D., *"The Proxy Proposal Rule of the Securities and Exchange Commission"* (1955-56) 33 U Det L J 191, 195, see also 211.

proper under state law the Commission exceeded its functions by excluding matters proper under state law[285]. A commentator writing in 1971 rejected the proposition that the Commission allows proposals not proper under state law, and found justification for a restrictive rule in the argument that the process involves certain costs and that, whereas at a meeting the stockholders can decide to adjourn when they decide no useful purpose is being served by the discussion, there is no other limit on the right to have a proposal included in a proxy statement[286]. It is submitted that this difference is explained by the differing interpretations of state law. Those who see the stockholder proposal rule as being wider than the substantive law take the view that state law prohibits stockholders from considering anything not positively put within their province.

It has been suggested[287] that the prohibitory aspects of state law are not likely to be violated and that, therefore, the adoption of a federal test for inclusion of proposals would not seriously affect the division of powers between management and the shareholder[288].

(b) Precatory Proposals

The Commission has recently appended a note to the clause permitting exclusion under state law, to the effect that a proposal that may be improper under the applicable state law when framed as a mandate or

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285. Bayne, D.C., "*Basic Rationale of Proper Subject*" (1957) 34 U Det L J 575.
286. "*Note: Proxy Rule 14a - 8, Omission of Shareholder Proposals*" (1971) 84 Harv L Rev 700.
287. Schulman, *op cit*, 64.
288. *Ibid*, 62.

directive may be proper when framed as a recommendation or request[289].

Two cases support this proposition. In the first of these, decided in 1912, it was held that any action by the shareholders collectively, relating to the details of the corporate business, is necessarily in the form of an assent, request or recommendation which can only be enforced indirectly through the general meeting's power over the election and removal of directors[290]. The court in the second case held, by a majority, that the fact that the resolution of the general meeting would have no direct effect did not make the expresiion of opinion invalid. The general meeting was entitled to put the directors who would stand for election on notice as to its views[291].

Manne, taking an almost unique view among commentators, states that the authority which shareholders seem to have under state law to submit precatory resolutions with a social content may be highly illusory and attributes the popularization of the notion that precatory proposals were more likely to pass the proper subject to Louis Loss. It is his view that the burden of persuasion should be on those seeking to establish their validity.[292].

Loss himself takes the view that this is an area in which policy should negate a "higgling" approach. He argues that the rule is apt to have a healthy indirect effect upon corporate management, that the opportunity to submit proposals even of an advisory nature affords a safety valve

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289. Code of Federal Regulations s 240-14 a - 8(c)(1).
290. *Continental Securities Co* v *Belmont* (1912) 99 NE 138 (NY Ct of Aps).
291. *Auer* v *Dressel* (1954) 118 NE 2d 1390 (NY Ct of Aps).
292. Manne, H.G., *"Stockholder Proposals Viewed by an Opponent"* (1972) 24 Stan L Rev 481.

for stockholder expression at a price to management which seems to be relatively slight[293].

Friedman takes the view that it is desirable to allow stockholders to make known their views to their elected representatives[294], thus linking the rationale of the precatory proposal to the shareholders' power to elect and remove directors. This point was picked up by Bayne who also pointed out that the stockholder's advisory proposal functioned as a device to force management to explain its stand in all major issues, thus linking it to the broad disclosure purposes of the securities legislation[295].

The argument that there is no point in establishing a right to advance precatory proposals inasmuch as, even if the company were to adopt them, the accomplishment would be insignificant, loses its force in the light of the fact that such proposals, whatever their form, have little or no chance of being adopted and thus the proponent's concern in all cases must be primarily with having the matter debated[296]. It may make little difference to him what form the proposal that achieves this object takes[297].

It has been stated that shareholders appear to exercise three functions at the annual meeting: (1) they vote on those items which require shareholder approval; (2) they submit their own binding resolutions

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293. Loss, L., *Securities Regulation*, 2nd ed (Boston, Little, Brown and Company, 1961) Vol 2, 920.
294. Friedman, D.M.,"*SEC Regulation of Corporate Proxies*" (1950) 63 Harv L Rev 796, 804-805.
295. Bayne, *op cit*, 604; see also Ledes, J.G.,"*A Review of Proper Subject under the Proxy Rules*" (1957) 34 U Det L J 520.
296. "*Note: Proxy Rule 14a - 8, Omission of Shareholder Proposals*" (1971) 84 Harv L Rev 700, 719.
297. "*Note: Liberalizing SEC Rule 14 a-8 through the Use of Advisory Proposals*" (1971) 80 Yale LJ 845, 850.

on matters of corporate policy; and (3) they question and advise management regarding its handling of corporate affairs[298]. The first function is provided for by the companies legislation. The third is usually accorded in practice. Any management mindful of the practical necessity of fostering good shareholder relations is unlikely to question it. The second proposition is established by the shareholder proposal rules and if it is granted it would not be unreasonable to recognize the role of the advisory proposal[299], especially in the light of the difficulty of drawing the line between the conduct of ordinary business and the setting of policy.

If, however, the note now appended to clause (c)(1) of the stockholder proposal rule can be taken as stating the position now established under state law, the Commission's role in establishing this position must be recognized[300].

Although, as noted above, there is Australian case law supporting the proposition that management can seek to have advisory resolutions passed, it would not yet be possible to assert definitely that a shareholder proposal of such a resolution would be proper, but there would seem to be no reason why Australian courts should not be ready to accept such a proposition. In Australia, as in America, the shareholders through their control of election and removal of directors have ultimate control over company policy and it would seem that they should be able to advise the directors of their wishes. At the moment the directors are known to confer with holders of substantial minority

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298. *"Note: Liberalizing SEC Rule 14a-8 through the Use of Advisory Proposals"* (1971) 80 Yale LJ 845, 846.
299. *Idem.*
300. Securities and Exchange Commission Release No 34-12999 (12.1.76); Securities Reg & Law Report (BNA) No 380, E.1, E.4.

interests in the company and no principle forbids them from accepting advice so the source of the advice would seem irrelevant.

3. ORDINARY BUSINESS MATTERS

If precatory proposals are to be allowed, should the subject matter of such a proposal be significant in determining its permissibility? The proxy rules adopted by the Securities and Exchange Commission in 1954 provided an express exception to the proposition that the general meeting could vote on resolutions embodying recommendations or requests addressed to the board of directors as these would not upset the substantive law of division of powers. This exception was to the effect that a recommendation or request that management take action with respect to a matter relating to the ordinary business operations of the issuer is properly excludable from the proxy materials[301]. This clause is preserved, subject to a change in wording, in the version of the proxy rules adopted in 1976[302].

None of the American commentators writing in recent years would challenge the idea that day to day business transactions are outside the scope of the general meeting's discussions; nevertheless, the exclusionary clause in question has not gone unchallenged. Dissatisfaction has been expressed in three areas: the definition of the phrase "ordinary business operations"; the prohibition of advisory resolutions, if such is intended[303]; and the application of the test by the

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301. Code of Federal Regulations s 240.14a-8(c)(3).

302. Securities and Exchange Commission Release No 34-129999 (12.1.76); Securities Reg & Law Report (BNA) No 38, E.1.

303. *Note, op cit,* 80 Yale LJ 845, 856 where it is stated that the use of the ambiguous phrase "recommendation or request" makes it uncertain whether "the exclusion was intended merely to reiterate state's law delegation of final authority as to ordinary business matters to the board of directors or was intended to limit advisory proposals as well."

Commission staff.

"Ordinary business operations" may, it seems, be interpreted to mean either those operations peculiarly within the discretion of the directors or those operations to which the executive staff of the company could bind the company without reference to the board of directors, that is, day to day transactions[304]. The position taken by Schwartz and Weiss is that if the board will decide a question the shareholders should be allowed to advise[305]. The Commission has stated that the phrase is not necessarily synonymous with the phrase "within the usual and normal functions of the board"[306], but it also stated on another occasion that the significance or importance of a decision is not relevant to the question of whether it constitutes an ordinary business operation[307].

The objection that the phrase "ordinary business operations" has not been properly defined tends to shade into the objection that it is not being consistently interpreted and applied. Thus Bayne, in his study of exclusions by the Commission in 1956, cites five proposals excluded on this ground, objecting that only three of these were properly excluded. Those properly excluded, in his opinion, would have required the company to keep its checking account in a certain bank, to answer letters within ten days and to incorporate a specific amendment into its pension plan. Those he deemed improperly excluded would have required the inclusion of more detailed information in the annual report and set policy on profit sharing as remuneration to employees in the film industry. It is Bayne's

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304. *"Note: Shareholder Participation in Corporate Management"* (1950) 40 Va L Rev 901, 916.
305. Schwartz and Weiss, *op cit,* 672.
306. Clusserath, T.M., *"The Amended Stockholder Proposal Rule: A Decade Later"* (1964-65) 40 N D Law 13, 36, citing Div Letter, March 23, 1954.
307. *Ibid,* 36, citing Div Letter, March 23, 1960, Div Memo, March 18, 1960.

view that any doubt should be resolved in favour of permitting the general meeting to determine the corporate policy[308]. Schwartz and Weiss, looking at more recent proposals, have also objected to the interpretation being given to the rule on the grounds that the Commission should not ignore social context in determining what is ordinary and that, in context, it might be that a proposal to require General Motors to install safety equipment on passenger vehicles was not ordinary business[309].

The decision of the court in *Medical Committee for Human Rights* v. *Securities and Exchange Commission*[310] is relevant. The proposal in question requested the directors to amend the corporate by-laws to prohibit the manufacture of napalm. The court remanded the case for reconsideration by the Commission because the merits of the proposal had not been argued before it but, in the course of the judgment, certain comments on the rationale of the tests were made. It was held that management could not exercise its specialized talents effectively if corporate investors assert the power to dictate the minutiae of daily business decisions, but a distinction was drawn between

> "management's legitimate need for freedom to apply its expertise in matters of day to day business judgment and management's patently illegitimate claim of power to treat modern corporations...as personal satraps implementing personal political or moral predilections."*311*

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308. Bayne, *op cit*, 600-601. Note that Bayne stated that "the shareholder should determine policy", an obvious but confusing example of naming the part for the whole.

309. Schwartz and Weiss, *op cit*, 672.

310. (1970) 432 F 2d 659 (DC Cir), rendered moot by subsequent action by parties. The case is hereafter referred to as the *Medical Committee* case.

311. (1970) 432 F 2d 659, 681.

The ordinary business matters test is often, as in the course of the decision just quoted, supported by a statement that specialized skills are involved in making routine business decisions and that it is impossible to present enough detailed information in the proxy statement to allow the shareholders to reach an informed and intelligent decision[312]. Slavin argued that the substantive test of proper subject came down to the question of whether threshold facts had to be determined before an ultimate conclusion could be arrived at[313]. However, when advisory resolutions are in question, it can be argued that these considerations lose weight. Thus Schulman asserts that the capacity of the shareholder body to analyse the issue need not be equal to that of management, that the question should be rather whether the proposal raises issues upon which shareholders would have enough interest and understanding to express themselves meaningfully[314]. When the resolution in question does not bind the company these arguments are acceptable and the question becomes one of expense alone. Is it desirable to allow the shareholders to give non-binding advice to the directors on ordinary matters which the directors are more competent to decide if the expense must be borne by the company? Inasmuch as the distinction between ordinary business matters and policy decisions is often difficult to draw, if it is accepted that policy determinations are rightly within the power of the general meeting, then it would seem that such advisory proposals should be allowed[315].

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312. See for example Ledes, *op cit*, 556; *Note*, 84 Harv L Rev, *op cit*, 719.
313. Slavin, J.J.,"*Proper Subject in a Nutshell*" (1957) 34 U Det LJ 615, 619.
314. Schulman, *op cit*, 54; see also *Note*, 84 Harv L Rev, *op cit*, 717.
315. *Note*, 80 Yale LJ, *op cit*, 856; see also "*Note: Shareholder Proposals: The Experience of Rule 14 a-8*" (1971) 59 Geo LJ 1343. Bayne, *op cit*, 600-601, 604-605.

Because of the form of the proposal in the *Medical Committee* case, doubts have arisen as to whether proposals to alter the company's constitution will be allowable where resolutions dealing with the same subject matter but not so framed would be disallowed under the ordinary business operations test. This doubt has not, apparently, been resolved[316], but it is clear that such a result would be illogical and the suggestion has been rejected by several commentators[317], if not yet by the Commission or the courts.

4. GENERAL CAUSES

The considerations involved in shareholder proposals connected with general causes, whether social, political or otherwise, have not yet assumed any real significance in the Australian context, although, in the light of isolated reports such as those issuing from the Queensland Mines meeting[318], they may soon do so.

The position taken by the Commission in 1945 was that it was the purpose of the proposal rules to place stockholders in a position to bring before their fellows matters of concern to them as stockholders in the corporation, not to allow them to obtain a consensus on questions properly debatable in other forms. This principle is unexceptional but, in 1953, a proxy rule was formulated which would exclude proposals motivated either by a personal grievance or primarily for the purpose of promoting general causes. In 1972 the rules excluding general cause

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316. See for example Commission determinations on proposals submitted to *Newmont Mining Corporation* (March 20, 1973) CCH Securities Law Reporter [79.325], (March 27, 1974) CCH Securities Law Reporter [79.760]

317. Allen, P.H.,"*The Proxy System and the Promotion of Social Goals*" (1970-71) 26 Bus Law 481, 493; Getz, *op cit*, 263-264.

318. See above, 79-83.

proposals were amended to substitute for the subjective test of motivation certain objective tests. The subjective tests are preserved, however, in the Canada Business Corporations Act[319].

The subjective test was objectionable for two reasons. First, it ignored the difficulty inherent in any attempt to determine motivation. It was felt to be especially objectionable that such a difficulty should be ignored where the shareholder whose motives were suspected would not be given any opportunity to argue his own case[320].

Secondly, the test ignored the fact that the cause will be relevant to several different types of proposals. Proposals dealing with general matters entirely unrelated to the business of the corporation and proposals calling for corporate action to achieve a general good, such as to stabilize the international economy, are not proper subjects, but proposals which relate to the normal business of the corporation, and inject into the decision-making process moral, political or social issues, should not because they reflect such issues be excludable[321]. A case in point might be the proposal considered in *Peck* v *Greyhound Corporation*[322] calling for the bus company to desegregate its seating. The decision in that case cast no light on the general causes test, however. The dictum in the *Medical Committee* case is in point[323]. There appears to be no justifiable basis on which it can be said that the moral predilections of management should be observed instead of those of the shareholders unless, perhaps, it can be argued that management's decisions in this area are more likely to serve desirable

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319. Can Bus Corp Act s 131(5)(b).
320. Getz, *op cit*, 258; *Note*, 84 Harv L Rev, *op cit*, 725.
321. *Note*, 84 Harv L Rev, *op cit*, 725, 726.
322. (1951) 97 F Supp 679 (NYDC).
323. See above, 174.

social goals and there is as yet no support for such an assertion.

The objective tests were amended in 1976 by excising the reference to general causes preserved in 1972 and providing that a proposal may be omitted if it is not significantly related to corporate business or if it is beyond the corporation's power to effectuate. These tests are not subject to the objections considered above but they are not free of problems. In particular, it is not yet clear when an economic test of "significantly related" will be applied[324]. It is, however, generally felt that these tests are at least potentially satisfactory .

G. CONCLUSION

In the course of the discussion of the division of powers between general meeting and board of directors, it has been shown that although at one time the board of directors was regarded as being the agent of the general meeting and subject to its dictation, this view is no longer held. The board of directors and the general meeting must now be regarded as co-ordinate bodies which derive authority from the corporate constitution which is imposed on the company from outside.

When it comes to the specific division of powers, the Companies Acts of Britain and Australia for the most part leave this to the articles, thus providing a large degree of flexibility. Under the Table A articles, which, in this area, have been almost universally adopted, the management of the business is entrusted to the board of directors. This provision is not, however, conclusive of all questions in the area. In

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324. See Schwartz and Weiss, *op cit*, 661-669.

particular, certain commentators have expressed dissatisfaction with the interpretation of the clause which appears to make the board of directors subject to the direction of the general meeting. Further, problems have arisen in regard to the control of litigation, particularly when the company has a right of action against the directors. Any solution to the problems inherent in the control of litigation are outside the scope of this paper but an attempt has been made to explore the issues.

As far as the dissatisfaction expressed with the interpretation of article 73 is concerned, it is suggested that this stems from the premise that the general meeting should be able to exercise some control over corporate policy more direct than that inherent in any power to elect and remove directors. North American materials on shareholder proposals have been examined for the light they can throw on the scope of the general meeting's control of policy. It has appeared from this examination that the view is taken that a resolution to effect anything that the substantive law does not forbid the general meeting to accomplish may properly be offered to and, by implication, passed by that body. Further, where the substantive law forbids the general meeting to act, it has been interpreted to allow it to advise. However, certain further restrictions have been put upon the power of the general meeting to advise by the rules adopted by the Securities and Exchange Commission.

It may be pointed out, by way of interest, that the resolution referred to in the introduction as offered to the general meeting of James Hardie (Asbestos) Co would not be a proper subject under the Securities and Exchange Commission Rules. Nor, under the ordinary business matters test,as it currently stands, would an advisory resolution to the same effect be proper. However, a resolution recommending to the board that

worker safety be a prime consideration and, possibly, that it would be desirable to compensate any workers who had suffered in health as a result of their employment should be permissible. The general meeting of Tooth's Ltd. should also be able to pass, or at least to consider, policy resolutions reflecting a shareholder's policy interests. However, the Queensland Mines instance presents other problems: not only were the shareholders there motivated by a concern for what would be considered general causes, but it is questionable how far any resolution they might care to offer would be compatible with the company's *raison d'etre* or substructure. A proposal, for example, that a company formed to mine uranium should cease to do so would not seem to be a proper subject for consideration by its general meeting. Real questions arise whenever general causes are involved as to whether the general meeting is the appropriate forum. Nevertheless, it is suggested that it should be accepted in Australia that the general meeting has certain powers over company policy.

PART III THE MAJORITY RULE PRINCIPLE AND THE GENERAL MEETING

Part II was devoted to an examination of the law governing the division of the company's decision-making powers between its general meeting and its board of directors. When a decision falls within the power of the general meeting it will usually be made under the principle of majority rule. In this part of the thesis the focus is on the operation of this political principle as it is affected by the distribution of voting rights in the general meeting.

When a resolution comes before the general meeting, what in fact happens is that the resolution is put to the meeting, votes are registered in a predetermined manner and the chairman declares whether or not the resolution has been passed according to the numbers mustered. In Australia, under the Table A articles, votes are in the first place registered by show of hands. But if there is a sufficient demand, resort may then be had to a poll in which votes will be cast according to the number of shares held[1].

By way of contrast, it may be noted that in the United States of America nearly all matters must be decided by a poll vote[2].

Unless the statute or the articles make other provision, all that is necessary to secure the passage of a resolution in general meeting is a simple majority, that is, a majority of more than fifty per cent of the votes cast. In certain cases the articles or the statute will stipulate for some kind of special majority. The Australian Companies Acts define

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1. UCA Fourth schedule Table A reg 51.
2. Aranow, E.R. and Einhorn, H.A., *Proxy Contests for Corporate Control*, 2nd ed (New York, Columbia University Press, 1968) 303, 360-361.

a special resolution as a resolution of which special notice has been given and which has been passed by a majority of not less than three-fourths of such members as, being entitled to do so, vote on the question[3]. The articles may stipulate for various other special majorities such as a two-thirds majority, or a majority not only of all votes cast but of all votes which might have been cast. Yet more rare is a stipulation of unanimity before a resolution can be adopted, but such stipulations are sometimes found in private company situations such as in joint venture companies.

This thesis makes no attempt to explore the interrelationship between interests and the right to vote in company meeting, a question which involves the consideration of issues which are not strictly legal. Moreover, it seems unnecessary to expound here the basic law defining the nature of a share in a company[4]. The focus here is on the distribution of voting rights in business companies in practice and theory.

A. THE DISTRIBUTION OF VOTING RIGHTS IN PRACTICE AND THEORY

1. THE AUSTRALIAN PRACTICE

Statutory provisions governing the distribution of voting rights in companies are not included in either the Australian or the British Companies Acts. The Table A articles appended to these acts, which are adopted by almost all companies, provide that on a vote show of hands

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3. UCA s 144.
4. See *Borland's Trustee* v *Steel Brothers & Co Ltd* [1901] 1 Ch 279; *Archibald Howie Pty Ltd* v *Commissioner of Stamp Duties* (1948) 77 CLR 143, 152; Bastin, N.A., "*The Enforcement of a Member's Rights*" (1977) JBL 17, 21-22.

every person present at a meeting shall have one vote and that on a poll every member represented at the meeting shall have one vote for each share he holds. These rights are, however, "subject to any rights or restrictions for the time being attached to any class of shares"[5].

There appears to be nothing on the face of the statute to prevent a company bestowing voting rights on a non-member. However, there is a recent case in which the Australian High Court lent tentative support to the proposition that a company will be unable to bestow voting rights on persons who do not hold shares. The question arose in a case which involved the validity of an article conferring special voting rights on A who was a major shareholder but who, under the articles as they stood, would have retained his voting rights even if he had divested himself of his shares. In the course of upholding the article in question, the opinion was expressed that these voting rights might be forfeit if A was to cease to hold membership status although they were not directly attached to any shares, but these opinions were *obiter*[6]. A clear distinction does exist between the right to vote in general meeting and the right to appoint a director of the company. Although the election of directors is one of the most important powers which can be conferred upon the general meeting, there is clear authority[7] for the proposition that this power may be exercised by an outsider under appropriate articles.

In the absence of statutory provision, the Stock Exchange requirement that company articles provide that holders of ordinary shares be entitled

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5. UCA Fourth schedule Table A reg 54.
6. *Kolotex Hosiery (Aust) Pty Ltd* v *Commissioner of Taxation (Cwth)* (1975) 49 ALJR 35.
7. See for example *Levin* v *Clark* [1962] NSWR 686; *Re Broadcasting Station 2GB Ltd* [1964-65] NSWR 1648.

to vote at any general meeting[8] and that voting rights be apportioned on a one for one basis with shares[9] assume great importance. This last requirement is a new prerequisite for admission to the Official List which became effective in July 1978 and does not affect companies which are already listed. It will ensure that in all newly listed public companies voting rights will be conferred on shareholders in proportion to their interest in the company and to the exclusion of all others.

Because the Stock Exchange requirement that voting rights bear a one to one relationship is so new, listed companies whose articles confer voting rights on a sliding scale will still be found. In the appendix to his 1958 study of one humdred and two Australian companies, Wheelwright[10] noted the rules as to voting power that applied to each company. On the present writer's tabulation, fifty-one of these companies maintained a straight one to one relationship between voting rights and shares when differences between classes of shares are ignored. Twenty-six companies used some form of sliding scale of voting rights, no report was given as to five companies, and the remaining twenty adopted some other departure from the straight one to one rule. Among those companies reported to be using sliding scales were David Jones Limited, Woolworths Limited, Tooth and Co Limited and Toohey's Limited[11], thus this system has been used by several significant Australian companies.

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8. Associated Australian Stock Exchanges Listing Requirements (1978) s 1 B 18.

9. Associated Australian Stock Exchanges Listing Requirements (1978) s 1 B 19A.

10. Wheelwright, E.M., *Ownership and Control of Australian Companies: A Study of 102 of the Largest Public Companies Incorporated in Australia,* (Sydney, Law Book Co, 1957).

11. The writer's telephone inquiries produced the information that Woolworths Limited and David Jones Limited still used the same scale while the company secretary of Toohey's Limited reported that the company used a one to one scale and as far as he knew always had.

There is no common North American rule, but the one to one voting rule appears prevalent. Although there are statutory provisions governing voting rights in all jurisdictions, these provisions are usually[12] made subject to the provisions of the company articles, charter or by-laws. There are, however, certain jurisdictions in which the statutory provision is mandatory. In Ontario the holder of a common share who appears on the corporation records is entitled to one vote for each share held by him[13] regardless of any provision in the articles of association. The articles may limit the rights attached to special classes of shares. In certain of the American states, the state constitutions have been construed to guarantee voting rights to shareholders[14]. Nevertheless, the Stock Exchange requirements usually assume the same significance in this field as they hold in Australia, as a result of what has been called "the curious omission in American statutory imperatives" of the requirement that voting rights should be granted to all of the common shareholders[15].

2. THE THEORY OF SELF-INTEREST

Theoretical justification of the policy which grants voting rights to shareholders may be found in the concept that the shareholders have a community interest in furthering the aims and objectives and guarding the welfare of the corporate entity. The shareholder or his predecessor in title, who contributed to the capital fund of the company in the

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12. Mod Bus Corp Act Ann 2d s 33 first paragraph; Can Bus Corp Act s 134(1).
13. Bus Corp Act (Ont) s 122(2).
14. See West Virginia's constitution art XI s 4 as construed in *State ex rel Dewey Portland Cement Co* v *O'Brien* (1956) 96 SE 2d 171 (W Va Ct of App); noted (1957) 59 W Va L Rev 374.
15. Conard, A.F., *Corporations in Perspective*, (New York, Foundation Press Inc, 1976) 320.

expectation of sharing in corporate profits will, it is assumed, be guarding his own interests by promoting the best interests of the company[16]. This theory of self-interest may be sufficient guide to solving the problems which arise when considering the distribution of voting rights, the problem of the ideal relationship between proportion shareholding and proportional voting power and the problem of determining the validity of various devices designed to separate ownership from control, all of which will be considered below. However, it is insufficient as a guide to controlling the shareholder's use of the vote.

John Stuart Mill's theory of representative government offers some interesting light on the question of the propriety of controlling the shareholder's use of his vote. Mill advocates the principle of participation on the ground that the rights and interests of an individual are only secure from being disregarded when the person himself is able and habitually disposed to stand up for them[17]. This argument is supported by two assumptions which are that any individual will prefer his own interests and that the individual will tend to know his own interests better than anyone else[18]. Nevertheless, Mill does point to two positive dangers which representative government entails: these are, first, general ignorance and incapacity in the controlling body and, secondly, the danger of the controlling body being under the influence of interests not identical with the general welfare of the community[19]. As a solution to these problems Mill relies on the principle of competence, arguing

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16. Sneed, E.,*"The Stockholder May Vote as He Pleases: Theory and Fact"* (1960) 22 U Pitts L Rev 24.
17. Mill, J.S., *Considerations on Representative Government,* (London, Longman, Green, 1865) 54, 55.
18. Thompson, D.F., *John Stuart Mill and Representative Government,* (Princeton University Press, 1976) 14-15.
19. Mill, *op cit,* 110; Thompson, *op cit,* 63 *et seq.*

that a democracy should give as much weight as possible to superior intelligence and virtue in the political process[20]. Mill does not assume that the franchise is a right each citizen may use as he pleases but rather treats the power to vote as a trust or duty inasmuch as the power to vote is a power over others and as such cannot be exercised except in the general interest[21]. Apparent interests which may contradict the general interest are allowed a role in the political process but only as a precaution against their being ignored and in the hope that they will be modified to fall into line with the general interest.

The idea that a shareholder's voting powers constitute a trust or a duty has been rejected by the courts. A shareholder, unlike a director, is not regarded as being in a fiduciary position when he exercises his vote[22]. The right to vote in general meeting is, it has been held, one of the property rights inherent in ownership of a share and it is "to be enjoyed and exercised for the owner's personal advantage"[23]. The archetypal authority for this proposition is found in the case of *North West Transportation Co* v *Beatty*[24]. In that case a shareholder-director used his voting rights in general meeting to ratify a contract which he had made with the company. The Privy Council, reversing the Supreme Court of Canada, held that this was permissible. Following this decision the position has appeared to be, for the better part of a century, that a shareholder may vote as he pleases. However, while

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20. Mill, *op cit*, 106-107; Thompson, *op cit*, 54 *et seq*.
21. Mill, *op cit*, 198-201; Thompson, *op cit*, 96-99.
22. *Peter's American Delicacy Co* v *Heath* (1936) 61 CLR 457, 504; see also *Pender* v *Lushington* (1877) 6 Ch D 70.
23. *Peter's American Delicacy Co* v *Heath* (1936) 61 CLR 457, 504.
24. (1887) 12 App Cas 589.

paying lip service to this principle the courts have, on a number of occasions, found excuses to modify its application[25].

The recent English case of *Clemens* v *Clemens*[26] would appear to have raised the issue anew. In that case the minority shareholder in a two-woman company was successful in obtaining a declaration that certain resolutions were oppressive and an order setting them aside. The court found that the resolutions in question, which authorized the company to issue new shares to the directors, who were previously not shareholders, and to an Employees' Trust, were calculated to reduce the plaintiff's percentage voting power to the point where she would be unable to prevent the passage of special resolutions. It was held that the major majority shareholder, in the circumstances, was not entitled to exercise her majority vote in whatever way she pleased. However, no attempt was made to enunciate a principle of limitation other than to say that the power was subject to equitable considerations which may make it unjust to exercise it in a particular way[27]. In effect, the passage of the resolutions in question was found to constitute a fraud on the minority, a concept with which the courts are not unfamiliar[28], although it was not governed by the statutory provisions. Foster J expressly held that "Whether I say that these proposals are oppressive to the plaintiff or that no one could honestly believe they were for her benefit matters not"[29].

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25. Sneed, *op cit.*
26. [1976] 2 All ER 268.
27. [1976] 2 All ER 268, 282.
28. See *Peter's American Delicacy Co* v *Heath* (1936) 61 CLR 457; *British Equitable Assurance Co* v *Baily* [1906] AC 35, 42; *Greenhalgh* v *Arderne Cinema* [1951] Ch 286.
29. *Clemens* v *Clemens* [1976] 2 All ER 268, 282.

The reader is referred to an article by Sneed in which he examines two categories of what he calls legal rules, those which support the premise that a stockholder may vote as he pleases and those which appear to run counter to it. Sneed concludes that the courts will honour the assumption that the shareholder may vote as he pleases only so long as the transaction is found to be intrinsically fair or the shareholder's vote is non-conclusive, but that when these preconditions are violated there will be found to be potent and effective limitations upon the shareholder's voting power[30].

Because this proposition is considered so basic, no attempt is made here to muster case law in support of it. The writer accepts Sneed's argument as in accordance with principle and suggests that it follows that the company form may more closely approach a Millsian democracy than any political state now constituted

B. THE CONCEPT OF CONTROL

"Corporate control" is a term used to denote the power which is exercised by a clearly identifiable individual or group of individuals who by some means or other manage to exercise powers of direction or dominion over the affairs of a company. Because corporate control may be exercised in a number of ways, it is a very difficult concept to define legally[31].

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30. Sneed, *op cit*, 52-54.
31. Pickering, M.A., *"Shareholders' Voting Rights and Company Control"* (1965) 81 LQR 248.

"Control", Berle says, "is a function of the ownership of voting stock"[32]. He distinguishes two types of control: "absolute control", which exists when a majority of the stock is held by a single owner or by a few stockholders who by agreement or tacit consent act together, and "working control", which rests on the influence the existing board of directors can be expected to wield over corporate meetings and elections. Working control may be exercised either by the holder of a substantial minority interest in the company with whom the board of directors maintains a close relationship or, where there is no substantial minority holding, by the board itself. Where control is exercised by the board itself is is labelled "management control"[33].

Pickering has adopted another basis for classifying types of control, distinguishing between legal and *de facto* means of control. "Control with a legal basis is obtained by the acquisition of a majority of the voting rights which may be exercised in general meeting"[34]. One way of achieving a legal form of control is by ownership of a majority of the shares. This has been recognized by the courts that have held that shareholders who hold such a proportion of voting rights as to be able to secure the passage of resolutions in general meeting will be deemed to have control of that company inasmuch as they will be able, in the last result, to elect and remove the directors[35].

There are, according to Pickering, two other major ways of achieving control with a legal basis. These are, first, to concentrate voting power in the hands of certain shareholders by giving them proportionately greater voting rights than other shareholders. This is done by

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32. Berle, A.A., "*Control' in Company Law*" (1958) 58 Col L Rev 1212, 1213.
33. *Idem.*
34. Pickering, *op cit*, 249.
35. See *Mendes* v *Commissioner of Probate Duties (Vic)* (1967) 122 CLR 152.

creating two or more classes of shares with different voting rights. One distinction which is commonly made is that between preferential shares and ordinary shares when voting rights attached to the preferential shares are not to be exercised unless the dividends owing on such shares are in arrears. No objection is usually taken to such a distinction inasmuch as it is considered that the holders of such shares enjoy compensating advantages in lieu of voting rights. Objections are much more frequently made against the use of non-voting equity or ordinary shares and this issue will be returned to below[36].

The second way in which control can be achieved, without ownership of a majority of shares but with a legal basis, is by the use of inter-member control arrangements. These include the voting agreement, the voting trust and irrevocable proxy[37]. What these devices have in common is their independence of the memorandum and articles of association of the company. Attention will be given to certain features of these devices below[38].

There are three general forms of *de facto* means of control. These are: control secured by an informal agreement between two or more shareholders, control resting on a substantial minority shareholding, and control resting on personal influence[39]. In so far as minority control is concerned, it may be noted that the exact proportion of votes which will be sufficient to give *de facto* control of a company varies widely from company to company and, further, that while "minority control, by definition, may always be displaced...the practical difficulties of

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36. See below, 210-216.
37. Pickering, *op cit*, 263.
38. See below, 213-225.
39. Pickering, *op cit*, 269.

achieving this, against a united board of directors, in particular may be very nearly insuperable"[40].

The holder of corporate control exercises a function, he does not possess or enjoy a proprietary right. Berle states that:

> "The function of control is necessary and essential in the corporate system. Directors have to be chosen by someone. Absent, a stockholder with absolute control, some mobilizer must be found to secure consensus where stockholders are scattered... . Control is to a stock corporation what political parties are to a democracy."*41*

Authority for the statement that the holder of corporate control does not possess a proprietary right to that control is found in the decision of the Australian High Court in *Ashburton Oil NL* v *Alpha Minerals NL*[42]. In that case the board of directors, on learning that a majority interest in the company had been acquired by an outsider, attempted to issue shares to prevent the takeover before registering the share transfers. The share issue was invalidated on the basis that the applicants as share owners had a right to relief against an improper exercise of this power but it was held that the majority holding gave the appellants no greater and no differing right to relief[43] than that which any shareholder would have had. A careful distinction must thus be drawn between the voting rights, conferred by the shares, in which the shareholder does have a proprietary interest, and the control those voting rights confer. The latter is temporary and may be destroyed by a decision to issue more shares or by a new combination among the other shareholders. The

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40. Pickering, *op cit*, 271.
41. Berle, *op cit*, 1215-1216.
42. (1971) 45 ALJR 162.
43. (1971) 45 ALJR 162, 162 per Barwick CJ.

advantage of a controlling interest is not property that a shareholder is entitled to have preserved by the intervention of the court[44].

Nevertheless, it appears that it is possible to buy and sell the control of a company. Such a transaction occurs when the vendor sells a block of shares which is large enough under the circumstances pertaining to the company concerned to allow the purchaser to control the company thereafter. Because that block of shares carries control of that company, the purchaser will be willing to pay more for that block of shares than he would be willing to pay for each individual share. It is, however, considered inequitable to allow the vendor to realize more for his shares than the minority shareholders can realize for their own, and various attempts have been made to prevent him from doing so. In Australia these efforts have taken the form of an attempt to draft a statutory code to control takeovers[45], while in the United States the courts have also devoted a fair amount of attention to this and other problems of company control[46].

Included among these other problems of control, and more important for the purposes of this thesis, is the problem of ensuring that control is not improperly acquired[47]. There are American decisions to the effect that control could not be legally acquired by merely buying stockholders'

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44. *Ashburton Oil NL* v *Alpha Minerals NL* (1971) 45 ALJR 162, 167 per Menzies J; see also at 167 per Windeyer J: "The argument...seemed to proceed as if a majority...had some kind of proprietary right to have their dominant position preserved... . I know of no such right."
45. See NSW Parliamentary Paper No 144 of 1969-80, Company Law Advisory Committee, *Second Interim Report to the Standing Committee of Attorneys-General on Disclosure of Substantial Shareholdings and Takeover Bids*.
46. Berle, *op cit*; see also *Perlman* v *Feldman* (1955) 219 F 2d 173 (2nd Cir); *Jones* v *Ahmanson* (1969) 460 P 2d 464 (Cal SC); Andrews, W.D., *"The Stockholder's Right to Equal Opportunity in the Sale of Shares,"* (1965) 78 Harv L Rev 505; Ratner, D.L., *"The Government of Business Corporations: Critical Reflections on the Role of 'One Share, One Vote'"* (1970) 56 Cornell L Rev 1, 16-17.
47. Berle, *op cit*, 1216-1218; Aranow and Einhorn, *op cit*, 483-488.

votes[48]. Of even more practical importance is a multitude of decisions to the effect that control may not be attained by gaining votes through direct false representation[49].

There are two English decisions which stand for the proposition that a contract to vote shares in a certain way when linked to a legitimate interest in the company is enforceable[50], but it is suggested that Anglo-Australian courts would nevertheless look on open buying of votes unfavourably. The question of false representations as affecting company voting has not so far been regarded as a problem of company control in England or Australia, and what limitations have to date been imposed in Australia have their basis in the fact that the person making the representations is usually a director and as such in a position of fiduciary responsibility[51]. A recent New Zealand decision[52], which gave rise to hopes that a movement in Commonwealth law towards the development of rules to prevent the abuse of power by directors and controlling shareholders was taking shape[53] inasmuch as it suggested that there seemed to be a rule that a director and shareholder in a small proprietary company, at least, might owe fiduciary duties to the other shareholders[54], was watered down on appeal when it was held that, although in the circumstances such a duty was owed, there was no general rule to this effect[55].

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48. *Brady* v *Bean* (1921) 221 Ill App 279; *Dieckmann* v *Robyn* (1911) 141 SW 717 (Mo SC); *Smith* v *San Francisco & NP Railway* (1897) 47 Pac 582, 590 (Cal SC) as cited by Berle, *op cit*, 1216.
49. Berle, *op cit*, 1216-1217; Aranow and Einhorn, *op cit*, 431-482.
50. *Greenwell* v *Porter* [1902] 1 Ch 530; *Puddephatt* v *Leith* [1916] 1 Ch 200.
51. See Part V.
52. *Coleman* v *Meyers* [1977] 2 NZLR 225.
53. See Hetherington, M.A., "*Financing an Insider Takeover*" (1976) 4 Aus Bus L Rev 220.
54. *Coleman* v *Meyers* [1977] 2 NZLR 225, 277.
55. [1977] 2 NZLR 225, 324-325, 330-331, 370.

The question of limitations on the use and abuse of company control is well worth more study but it is not proposed to pursue it here. Instead this discussion will pursue the question of whether it is right that the ownership of a block of shares that is less than the totality of the shares should give the shareholder a right to control the corporation. This involves an analysis of the bases both historical and theoretical of the one share one vote rule.

C. THE "ONE SHARE, ONE VOTE" MODEL

The term "one share one vote rule" is sometimes used to describe the pattern of allocation of voting rights which, as noted above, is most frequently adopted in practice, but so as not to egregiously confuse a rule of practice with a rule of law the term "one share one vote model" is preferred here. Where this model applies, a shareholder will on a poll have one vote for each unit of the company's nominal capital which he has contributed. Certain decisions in general meeting may be resolved by the method of a show of hands. This method gives each member personally present one vote and thus preserves a per capita voting system. Nevertheless, close decisions will be referred from the vote by a show of hands to the poll and so in the final analysis a single shareholder holding a fifty-one per cent interest in the company will always outvote any number of minority shareholders. The evolution and rationale of this model are explored here in order to answer the question whether this distribution of voting rights is desirable.

1. HISTORICAL DEVELOPMENT OF THE MODEL

Early corporations of municipal and religious character, in relation to which the principles of corporation law were developed, had as their objective the promotion of the general welfare of the group in accordance with terms of their charter. The assumption was that every man had an equal interest in securing this end and that the best decision on any question would result from allowing each man an equal voice in government[56]. The courts, being familiar with this distribution of voting rights, at first assumed that, in the absence of any particular provision to the contrary, it would pertain in business companies as in their forerunners. Ratner records that through early seventeenth century England the charters of joint stock companies generally made no specific provision for the allocation of voting rights to shareholders but left the matter to be decided by the by-laws[57]. Controversies tended to arise, however, when the distinction between per capita and proportional voting affected the result of an election. Consequently, the practice of making provision for voting rights in the charter grew and became general. Three distinct patterns of distribution emerged. Certain charters specifically provided that no shareholder should have more than one vote, but others allowed a shareholder to cast as many votes as he had shares, while a third, intermediate, course was to provide for limited proportional voting. This latter compromise became dominant in England during the eighteenth century[58]. Charters commonly provided

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56. Bergerman, M.M., *"Voting Trusts and Non-Voting Stock"* (1927) 37 Yale LJ 445, 447.
57. Ratner, *op cit* 3.
58. Du Bois, A.B. *The English Business Company after the Bubble Act, 1720-1800,* (New York, Octagon Books, 1971) 288.

that each share would confer a vote upon its holder but that no individual was to have more than a certain number of votes regardless of the number of shares he held[59]. The Companies Act of 1862 provided that, in default of regulations, each member should have one vote[60], but the scheduled articles made provision for limited proportional voting[61].

The use of limited proportional voting is now very rare in the United States of America, and in view of the recent amendment to the Associated Australian Stock Exchanges requirements can also be said to have gone out of favour in Australia[62]. This scheme of voting rights would seem to be founded on a compromise between two views or political theories, that is, between the argument that the member who stood to gain or lose more should have a proportionally greater voice in the decisions of a company organized to seek financial gain and the argument that it was imprudent to allow too great a concentration of control[63]. As a compromise its theoretical basis lacked conviction and the courts, therefore, declined to find grounds for interfering with shareholders' attempts to circumvent the restrictions. Where limited proportional voting was used, resort was had to the expedient of dispersing shares to nominee holders who would exercise the voting rights they acquired at the direction of their principal[64]. Limited proportional voting regulations became difficult to enforce and were less frequently adopted. In 1907 the Table A articles appended to the English Companies Act were altered

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59. See for example *Edols* v *Edols* (1909) 26 WN (NSW) 45; see further Du Bois, *op cit*, 316-317 nn 48-50.
60. Companies Act (1862) 25 & 26 Vic c 89 s 52.
61. Companies Act (1862) 25 & 26 Vic c 89 First sched art 44.
62. See above, 183.
63. *Baker* v *Providence & Worcester Co* (1976) 364 A 2d 838, 848 (Del Ch), reversed *sub nom Providence & Worcester Co* v *Baker* (1976) 378 A 2d 121 (Del SC).
64. See for example *Pender* v *Lushington* (1877) 6 Ch 70.

to embody the one share, one vote rule[65]. A similar historical evolution took place in the United States[66].

American case law[67] on the subject is much more copious than the Anglo-Australian equivalent but most of the decisions are fairly ancient and will not be noted here. However, one recent American case is of interest. In the wake of the collapse of the Penn Central railroad, a dispute arose as to voting rights in a minor railroad company in Delaware. The history of this company's charter could be traced back into the nineteenth century and it featured provisions for limited proportional voting. If the limitation could be set aside the trustees of the bankrupt company would control the minor company, otherwise independent stockholders would be left in control. The court in the first instance held that the limitation was inconsistent with the Delaware statute which required that each share confer a right to vote. On appeal the decision was reversed. The appeal court held that the restrictions in question were limitations upon the voting rights of the stockholder, not variations in the voting powers of the stock itself. In the hands of a smaller stockholder the same stock would confer voting power equal to other stock in the class. The court in the first instance was found to have referred to the wrong section of the statute in question and it was held that the provision that, "unless otherwise provided each stockholder shall be entitled to one vote for each share of capital stock held", allowed the company a discretion to import voting restrictions[68]. As in the United States, so in Australia, the basic

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65. Companies Act (1908) 8 & 9 Edw Vii c 69 First sched Table A reg 60.
66. Ratner, *op cit*, 5-8.
67. See annotations (1929) 63 ALR 1106.
68. *Providence & Worcester Co* v *Baker* (1977) 378 A 2d 121 (Del SC).

assumption today is that a shareholder in a business company will have a vote for each unit of the company's capital stock which he owns, but a company may still elect to provide limited proportional voting. Per capita voting, on the other hand, is preserved in non-profit corporations but is unheard of in business companies as the rule of last resort.

2. THE MODEL ASSESSED

Despite the vociferous protests uttered by some writers[69], the one share one vote model is now widely favoured. There seems to be no likelihood that the situation will be changed. The question remains whether the rule is or is not meritorious, the question of immediate practical possibilities aside. Answers to this question differ because those who answer it disagree as to what characteristics will distinguish the best corporate decision. One school of thought insists that the corporate objective should be maximization of profit regardless of any other consideration. The other school of thought maintains that in the context of a developed economy maximization of profit loses its primacy, that economists, corporations and shareholders should be encouraged to take other objectives into account[70]. Those who stress the goal of profit maximization will argue for the one share one vote model on the ground that those who will be most interested in such a goal will normally be those who stand to gain most from it and that therefore these people should have a proportionately greater voice in corporate decisions. One response of those who argue for a hierarchy of corporate objectives may

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69. Ratner, *op cit.*

70. See for example Galbraith, J.K., "Economics and the Quality of Life" in *Economics, Peace and Laughter,* (London, Pelican Books, 1975) 3.

be to assert that each individual should have an equal voice in corporate government. This argument is advanced by Ratner.

The emergence of the one share one vote model did not represent a triumph of one policy over another but was, rather, a pragmatic victory of a wealthy shareholder over a practice which limited his power. Nevertheless, the courts have since adopted a theoretical argument in favour of the model. The philosophy of government applied to business corporations remained the same as that which had influenced the regulation of the earlier "political" corporations. The belief in majority rule was unshaken, although there was substituted for the general interest which the individual is presumed to have in the successful functioning of government the interest which an investor has in the success of a money-making project. In the former case a majority in general interest is supposed to emerge from the voting contest with a wise government policy; in the latter a majority in financial interest is supposed to determine correct corporate policy as a result of a similar conflict of honest opinions[71]. Fifty years ago, dissatisfaction with an approach to corporate control and the distribution of voting rights which was based on political theory alone was expressed. The argument that the investor's right to a voice in corporate decisions was not unquestionable and that a sociological and economic inquiry into the facts of corporate life was a necessary basis for a decision as to whether the share owner's right and duty to vote should be unalienable was advanced[72].

In the intervening fifty years several studies of corporate voting

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71. Bergerman, *op cit*, 448.
72. *Ibid*, 466-467.

patterns have been carried out, among which Berle and Means' classic study[73] must be noted. These studies have tended to prove that the voting right is not fully used by shareholders but, it is submitted, this datum provides no answer to the question of which voting pattern is most desirable. Moreover, the answer to this question cannot, in the last resort, be supplied by sociology. Because the question is highly normative the answer must, in the end, be shaped by political philosophy.

As representative of the school of thought which supports the one share one vote model, an article by Manne may be cited[74]. This article attempted to apply to corporate voting theoretical advances made by two studies of political voting[75]. It was noted that inasmuch as different individuals have different intensities of feeling regarding the subjects or candidates on which they vote simple majoritrianism can result in awkward and undesirable choices. This is because a minority of forty-nine per cent feeling extremely strongly will be defeated in an election by a majority of fifty-one per cent holding only a mild preference. An argument for vote trading could therefore be made out.

Where voting power is directly related to the number of shares held, an individual who feels strongly about a corporate decision may, if he wishes, purchase sufficient shares to ensure that his wishes will prevail. This step will, in fact, only be taken where there is a possibility of sufficient financial gain to offset the necessary outlay, but if it is accepted that the profit goal is the only proper one in

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73. Berle, A.A. and Means, G.A., *The Modern Corporation and Private Property*, (New York, MacMillan & Co, 1932); see also Midgley, K., *"How Much Control do Shareholders Exercise?"* (1974) 114 Lloyd's Bank Rev 24.
74. Manne, H.G., *"Some Theoretical Aspects of Share Voting"* (1964) 64 Colum L Rev 1427.
75. Buchanan and Tulloch, *The Calculus of Consent*, (1962); Downs, *An Economic Theory Democracy*, (1957) as cited by Manne, *op cit.*

this field this fact will not constitute a drawback. Manne analysed the reasons why corporate control is sought and concluded that only one would make the value of the vote to the one who sought control worth more than the investment which the share represented. The gain which could be realized by taking over the company and giving it improved management might induce someone to seek to acquire shares whose investment value was declining[76]. An outsider who successfully takes over a company and improves its management enough to realize a profit serves not only his own interests but also those of the minority shareholders and of society at large so long as it is accepted that a company's sole object should be maximization of profit for its shareholders. The fact that each share confers a vote makes it possible for shareholders to buy and sell votes. This practice, which, it appears, is legal in Britain[77], is seen by Manne as a good thing inasmuch as shareholders with reliable information and concrete ideas about how to use this power will tend to acquire it. Further, when disagreements arise among shareholders it is possible for one side to buy the other out and this will provide an easy way out[78]. If Manne's arguments are accepted, the one share one vote model is unquestionably desirable.

Other arguments, however, have been put by Ratner. He is a representative of the school of thought that argues that profit maximization should not be the sole objective of the corporation. Ratner rejects the argument

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76. Manne, *op cit*, 1430.
77. *Puddenphatt* v *Leith* [1916] 1 Ch 200; *Musselwhite* v *C.H. Musselwhite & Son Ltd* [1962] Ch 964; see Ford, H.A.J., *Principles of Company Law*, 2nd ed (Sydney, Butterworths, 1978) [1811]. The position is otherwise in the United States of America: Sneed, *op cit*, 45-47.
78. Manne, *op cit*, 1445.

that control by the large shareholder will serve the interests of the minority shareholders. It is his view that management control is more likely to serve the interests of the minority shareholder and is easier to police. Furthermore, he points out that the entrepreneurial theory cannot be applied to the modern established corporation and that in this context the public policy argument in favour of control by the majority shareholder loses much of its force[79]. His voice joins that of others[80] who have argued that some way must be found to enforce managerial responsibility to constituencies other than the investors in the company[81]. He denounces the one share one vote system because it depersonalizes the decisional process in corporate elections. "The shareholder under the present system", he states, "is not voting as a person at all, but as the temporary trustee of a piece of paper embodying values to which shareholders and management alike have agreed to adhere in making their 'corporate' decisions whether or not they accept them in their personal lives"[82]. The one share one vote model represents, in his view, "an abberation in historical development which is widely departed from in other countries, facilitates trafficking in control and the development of unhealthy conglomerates, is vesting necessary power in the hands of financial managers who have neither the desire nor the ability to exercise it [and] inhibits democratic decision making on important social and economic issues"[83]. Ratner supports a return to the basic principle of one man, one vote. Among the advantages of this system is the fact that it would have greater potential than the one

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79. Ratner, *op cit*, 21.
80. See above, Part IE.
81. Ratner, *op cit*, 33.
82. *Ibid*, 38.
83. *Ibid*, 44.

share one vote model for producing public discussion of the social and economic policy issues that arise in the context of the election of corporate managers[84]. He further suggests that if the one man one vote model were to be reintroduced, representatives of the corporation's other constituencies could secure a voice in corporate decisions by purchasing a share in the company. He does not, however, address himself to the question of whether such a forum would be suitable for discussion of the issues relevant to these other constituents.

The present writer personally favours the use of limited proportional voting. It is true that this system is a compromise and that it is possible to circumvent its provisions to a certain extent by the use of nominee shareholders, but in practice, because of the cumbersome nature of this expedient, it is suggested that such circumvention will not totally destroy the utility of the device. The writer is persuaded that in a company where certain rights have a pecuniary value it is not fair to allow a member with a minimal interest in the company to have an equal say with a member who has a substantial investment in the company but feels that, on the other hand, no one shareholder should be allowed to disregard the desires of others with a real and substantial interest in the company. It is suggested that as long as a shareholder who holds one share is allowed one vote, the new amendment to the Associated Australian Stock Exchange Listing Requirements need not be interpreted to prevent the adoption of limited proportional voting. The basis for this suggestion is the appeal decision in the American case of *Providence & Worcester Co* v *Baker*[85] discussed above. Whatever the pattern of voting

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84. Ratner, *op cit*, 50.
85. (1977) 378 A 2d 121 (Del SC); see above, 197-198.

distribution, the development of rules governing the conduct of company meetings will be significant, but this is so especially where the one share one vote model is in force, in that the development of these rights will prevent the inequitable use of voting power to override the smaller shareholders' right to participate in corporate governance.

3. CUMULATIVE VOTING RIGHTS

One voting device which, while not replacing the one share one vote rule in principle, alters its impact is cumulative voting. This is a device which has to date been employed almost exclusively in the United States of America. It applies a formula to the election of a slate of directors which allows each shareholder to multiply the number of votes he may cast by the number of vacancies to be filled and to cast the total number of votes thus arrived at for one candidate[86]. In effect, it introduces proportional representation to the board of directors.

The history of the device will not be given at length, but it may be noted that it was introduced first in Illinois in 1876. A number of the American states subsequently adopted legislation making its use mandatory, but since 1950 this trend has reversed and a number of states have amended their provisions to the effect that where cumulative voting was once mandatory it is now optional[87]. However, cumulative voting still remains mandatory in several states.

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86. For example, if cumulative voting were in effect under the articles of MacEachern McIlraith Ltd the IEL interests which are stated to hold a 20% interest would be able to elect one director if there were five available positions. See *Sydney Morning Herald*, Thursday October 26, 1978, 15 for relevant facts.
87. Sturdy, H., "*Mandatory Cumulative Voting: An Anachronism*" (1961) 16 Bus Law 550, 552.

Even if it is accepted that a proportional representation system is appropriately applied to elections of directors of business companies, certain technical problems arise in devising such a scheme. Problems occur, for example, where a simple majority has the power to remove a director from office. Unless some precaution is taken, the co-existence of cumulative voting provisions with such provisions for removal could lead to an undesirable "revolving door" situation[88]. Problems can also arise when a company using cumulative voting desires to reduce the number of directors. While these problems are not insuperable, the more fundamental question as to the basic desirability of cumulative voting remains.

It has been said that this method of voting turns corporate politics into a numbers racket both at the time of the election and subsequently at each meeting of the board of directors[89]. It most definitely involves a system of party politics or block voting which would discourage individual assessment of the candidates for directorships. Moreover, one commentator asserts that in the application of this system to election of directors a fundamental error in political analysis has been made. The board of directors, an executive body, has been confused with a legislative body. Proportional representation is undesirable when applied to executive organs, this commentator maintains, because it tends to interfere with government by consensus[90]. The same commentator concedes that cumulative voting may be of use in the context of a close

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88. Bailey, R.G., "*Shareholder Control over Management: The Removal of Directors*" (1974) 20 McGill LJ 85, 90-95.
89. Sturdy, *op cit*, 565-567.
90. *Ibid*, 552-556.

corporation or private company but expresses the opinion that a shareholders' agreement or, in its absence, a remedial statute such as the Californian one[91] will be more satisfactory and urges the desirability of allowing the stockholders of the company to decide for themselves which voting system they should adopt[92].

The writer does not urge that cumulative voting be made mandatory in Australia but would suggest that the desirability of cumulative voting be considered. Further, inasmuch as the validity of any attempt to adopt such a system voluntarily would be doubtful[93], it is suggested that permissive provisions should be introduced[94].

D. SEPARATION OF OWNERSHIP AND CONTROL

The courts and legislatures have, historically, approached problems in this area under the influence of the theory of self-interest which, as has been seen, also influenced the evolution of the one share one vote rule. If the theory that those who own a majority of its shares will best govern the company is accepted, it follows that devices which deprive shareholders of voting power are undesirable. Devices which separate ownership and control, and which are, therefore, deemed to be

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91. Cal Corp Code ss 4651(e), 4657, 4658, 4659. See also UCA s 186 and its English equivalent s 210 as cited by Adams, T.V.,"*Should Trust Principles Apply to Close Corporations?*" (1970) 48 N Ca L Rev 336 343.

92. Sturdy, *op cit*, 576.

93. Inasmuch as such provisions would conflict with statutory provisions such as UCA s 120, but see Ford, *op cit*, [1416], [1417].

94. See Skully, M.T., "Bringing Back the Small Investor, Comment", *Sun Herald*, Sunday, 6 August 1978.

objectionable in some, if not all, circumstances include proxies, shareholder agreements and voting trusts, non-voting shares and non-equity voting shares[95].

The non-voting share and the non-equity voting share are devices which may be entrenched in a company's constitution. Where they are so employed, the separation of ownership and control is permanent, barring a revision of that constitution. Moreover, because the decision to adopt such a device is made when the company is being set up, it is usually made by the company's promoters without consultation with those who will hold the shares. Indeed, in some cases the shareholder may acquire shares in ignorance of the lack of voting power and will be debarred from protesting because of the presumption that he has notice of the contents of the company's articles.

The proxy, the voting trust and the shareholders' agreement, on the other hand, are devices which separate ownership and control to a greater or lesser extent depending on circumstances. They are extra-constitutional devices and the separation involved, at least in theory, falls short of being permanent. Moreover, in these cases it is the shareholder individually who opts to separate ownership and control and to delegate the latter to someone else, and the fact that shares may be sold subject to a voting trust does not alter this fact. It is suggested that these differences should affect the approach to each of these devices and that whereas non-voting shares are inherently objectionable, the invalidity of the voting trust, the proxy and the shareholders' agreement should not be assumed.

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95. Sneed, *op cit*, 27; Bergerman, *op cit*, 449.

Anglo-Australian jurisprudence has taken limited notice of voting trusts and shareholders' agreements, although the tendency has been to strike them down. Recent evidence of this trend is found in statutory form in the Voting Rights (Public Companies) Regulation Act 1975 (Queensland). This Act allows the Governor-in-Council, where he is of the opinion that such an agreement or arrangement exists, to make a declaration affecting voting rights and to invalidate any meeting or resolutions passed in consequence of an arrangement or agreement for "collusive" combination[96].

The proxy device, on the other hand, is comparatively well developed and one part of this thesis is devoted to a discussion of the law and policy considerations governing its use[97].

As far as the Anglo-Australian approach to non-voting shares is concerned, in the absence of statutory provisions these have been held valid. In the United States the common law position was similar, although the use of the voting trust was much more frequent and some courts, in the absence of statute, were inclined to hold them invalid in certain conditions. The American legislatures have now to a large extent pre-empted the common law in this area. Voting trusts as well as proxies have been legalized and shareholder agreements are recognized by statutes governing close corporations[98]. Thus, although the courts reportedly still view the divorce of power and property with suspicion and distrust, the legislatures have made these devices respectable[99]. In fact, one

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96. Voting Rights (Public Companies) Regulation Act 1975 (Qld) ss 4, 5 and 6.
97. See below, Part VI.
98. See below, 213 *et seq.*
99. Sneed, *op cit*, 27.

commentator has been persuaded by these provisions to go so far as to declare that the anti-separation doctrine is anachronistic[100]. Certain American states have, on the other hand, prohibited non-voting stock[101]. In only one instance, however, has any attempt been made to require that voting rights be distributed fairly and equitably. The statute in point is the federal Public Utility Holding Company Act of 1935[102]. The Securities and Exchange Commission has interpreted section 79(j)(b)(1) to mean that the relative voting strengths of different classes of security holder are to be equated with the relative investments of each class. The attempt to police the application of this requirement has involved substantial administrative problems as it is necessary both to define voting power and to determine the investment involved and also to demand appropriate remedial action where necessary[103]. Such an approach is considered to require too much administrative effort to make it suitable for widespread adoption in Australia. However, this is not true of the other measures mentioned and it is suggested that the desirability of adopting these provisions in Australia should be reviewed.

1. NON-VOTING SHARES

As stated above, the Australian Companies Acts, like their British model, do not require that voting rights be attached to shares. Where they apply, the listing requirements of the Australian Stock Exchanges do, in

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100. Adams, *op cit*, 341 citing *Lehrman* v *Cohen* (1966) 222 A 2d 800, 807 (Del Ch); see also Berger, G.D.,*"The Voting Trust: California Erects a Barrier to a Rational Law of Corporate Control"* (1965-66) 18 Stan L Rev 1210.

101. See below, 222.

102. 15 USC (1946) s 79(j)(b)(1); see also s 79(a)(b)(1).

103. Leary, L.W.,*"'Fair and Equitable' Distribution of Voting Power under the Public Utility Holding Company Act of 1935"* (1953) 52 Mich L Rev 71.

part, supply the deficiency by requiring equity shares to carry votes. Nevertheless, the non-voting equity share is valid under Australian company law. The problems involved in the use of these shares were considered by the Jenkins Committee, but the decision reached was not unanimous.

Conflicting arguments were presented by witnesses appearing before the Jenkins Committee. Those opposing the voteless equity shares not only urged the general principle but also referred to specific evils likely to arise from their use. It was said that holders of such shares would have to rely on court proceedings if the directors of their company were to abuse their powers and would have no recourse against a merely inefficient management. Moreover, the value of the voting shares would be disproportionate to the investment they represented[104].

Supporters of voteless shares urged the principle of freedom of contract and pointed out that voteless shares may serve a useful purpose in the context of the family company and death duties. Further, they argued that it would be possible to evade any prohibition of voteless shares by the use of ingenuity and called into question the existence of the rule of public policy which prescribed that shares should carry voting rights[105].

The majority of the committee concluded that the case for the abolition of voteless shares had not been made out but recommended steps to tighten the regulations applying to them. A strong minority dissent was, however,

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104. Great Britain, Board of Trade, Report of the Company Law Committee, 1962, (Jenkins Report) para 128.
105. *Ibid*, paras 128-132.

recorded[106]. It was the opinion of the minority that the growth of non-voting shares struck at the basic principle on which British company law was based, the principle that ultimate control over the directors should be exercised by the shareholders. The argument that shareholder control was rendered ineffective by shareholder apathy was considered but dismissed on the ground that apathy would disappear if things began to go wrong. Although shareholder control may be inefficient, it was held that it would not improve efficiency to free the directors from their control. The minority recommended that steps should be taken to prevent growth in the use of non-voting shares.

In the United States the New York Stock Exchange refuses to list non-voting shares and provisions originally designed to inaugurate cumulative voting have been interpreted to prohibit non-voting stock[107]. More recently the problem of non-equity voting shares[108] has been presented to a court in Illinois, a state in which non-voting shares are prohibited. The term "non-equity voting share" is used to denote a share which confers voting rights but no right to participate in profits or in the distribution of capital. Where such shares are recognized the concept of self-interest becomes inapplicable. The court upheld the use of the device in question but the decision has been severely criticized by the commentators. In the course of this discussion it was pointed out that

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106. Jenkins Report, Note of Dissent, 207-210.

107. *State ex rel Dewey Portland Cement Co* v *O'Brien* (1956) 96 SE 2d 171 (W Va App); *People ex rel Watseka Telephone Co* v *Emmerson* (1922) 134 NE 707 (Ill SC); *Wolfson* v *Avery* (1955) 126 NE 2d 701, 706 (Ill SC); *contra State ex rel Frank* v *Swanger* (1905) 89 SW 872 (Mo SC); *Shapiro* v *Tropicano Lanes* (1963) 371 SW 2d 237 (Mo SC), for comment see Note, (1957) 59 W Va L Rev 374; Bowman, L.J., "*Missouri Approves Constitutionality of Non-Voting Common Stock*" (1964) 19 Bus Law 545.

108. *Stroh* v *Blackhawk Holding Corp* (1971) 272 NE 2d 1 (Ill SC) affirming (1969) 253 NE 2d 692 (Ill App), as noted (1972) 18 Wayne L Rev 841, (1973) 44 Colo L Rev 433.

the use of non-voting shares is not necessarily inconsistent with the policy that requires holders of voting rights to have a financial interest in the corporation. Where non-voting shares are employed the control group will also hold an ownership interest in the corporation but this will not be so where non-equity voting shares are employed. The decision in question is therefore deemed to strip shareholders of the protection contained in the requirement that directors be elected by those who are motivated by self-interest to consider the interests of the company.

No real consideration has ever been given by Australian legislators to the question of whether non-voting shares or non-equity voting shares should be prohibited. The writer suggests that this question should be considered and that both devices should be prohibited except possibly in the context of the small private company where they may be adopted, after full consideration, to achieve some particular object.

2. SHAREHOLDER AGREEMENTS

When the term "shareholder agreement" is used to refer to a device for achieving company control, it means something more than a simple understanding between shareholders. The term has been defined as meaning "contracts executed by some or all of the members of a company, at the time of its formation, requiring that they vote their shares in a particular way on certain defined matters or resolutions"[109].

This definition is not, however, unanimously accepted. Another commentator states that the phrase is "the generic term for any contract

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109. Finn, P., *"Shareholder Agreements"* (1978) 6 Aus Bus L Rev 97, 97.

between or among shareholders in relation to the range of corporate activity permitted to them"[110]. The American authority, O'Neal, states that such an agreement may be entered into before incorporation and referred to as a "pre-incorporation agreement" or "promotor's contract" or after incorporation, in which case it will be known as a "shareholders' agreement"[111].

Shareholder agreements, although widely used in the context of Ameriaan close corporations, are relatively unknown in England and Australia. They have, however, been employed in these jurisdictions from time to time, as is demonstrated by the recent English case of *In re A. and B.C. Chewing Gum Ltd*[112].

The fact that shareholder agreements are regarded as having particular applicability to small "quasi-partnership" companies has two explanations, one practical, the other theoretical. The practical explanation is that shareholder agreements, unlike such devices as non-voting stock, by their very nature require consultations among individual members before they can be put into effect, and therefore the number and dispersion of shareholdings in public companies will make it more difficult for members to effect such an agreement. Unanimous shareholder agreements particularly are virtually ruled out in the context of the public company.

The theoretical objection to shareholder agreements in the context of public companies rests on the ground that they frequently attempt to

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110. Kruger, S., *"Pooling Agreements under English Company Law"* (1978) 94 LQR 557, 557.
111. O'Neal, F.H., *Close Corporations, Law and Practice,* 2nd ed (Willmette, Illinois, Callaghan & Co, 1972) vol 1 para 5.03.
112. [1975] 1 WLR 579.

provide for a departure from the corporate model. Because Anglo-Australian company law, in large part, leaves the division of powers among corporate organs to the company's memorandum and articles, this objection lacks force where these documents have been so drafted as to dovetail with the shareholder agreement in question. Where a conflict does exist between the memorandum and articles on the one hand and a shareholder agreement on the other, it may be said that "the courts will not, as a general rule, be prepared to enforce such an agreement"[113]. The objection has much more cogency, however, in the North American context where the corporate model is enshrined in statute. For this reason many of the American commentators' arguments are devoted to justifying such departures[114].

"The best protection that can be extended a client about to enter into a corporate venture," it has been argued, "is a well-drawn agreement between shareholders designed to safeguard their interests on a mutually fair basis"[115]. The same commentator further stated that "the primary purpose of a shareholder agreement is to eliminate the tyranny of the majority"[116]. To preserve the element of mutual fairness and to prevent the tyranny of the minority from replacing that of the majority it is not necessary to insist that all members of the subject company become parties to the agreement. It is, however, essential that any such

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113. Finn, *op cit*, 100.
114. See O'Neal, *op cit*; see also Elson, A., *"Shareholder Agreements, A Shield for Minority Shareholders of Close Corporations"* (1967) 22 Bus Law 449; Steadman, C.W., *"Maintaining Control of Close Corporations"* (1959) 14 Bus Law 1077; Sturdy, H.F., *"The Significance of 'Form' and 'Purpose' in Determining the Effectiveness of Agreements among Shareholders to Control Corporate Management"* (1958) 13 Bus Law 283; Morganstern, S., *"Agreements for Small Corporation Control"* (1968) 17 Clev Mar L Rev 324; Ghingher, J.J., *"Shareholders' Agreements for Closely Held Corporations: Special Tools for Special Circumstances"* (1974-75) U Balt L Rev 211.
115. Elson, *op cit*, 451.
116. *Ibid*, 452.

agreement should be open to scrutiny particularly by non-contracting minority shareholders, who should also be entitled to be apprised of all the circumstances[117].

If all these requirements are demanded of a shareholder agreement, the definition must be expanded to incorporate them. The writer therefore submits that the term "shareholder agreement" should be defined to mean: a contract executed by some or all of the members of a company which is compatible with the corporate constitution and which provides that the parties to it shall exercise the votes in respect of their shares in a particular way on certain defined matters or resolutions with the openly avowed intention of ensuring that certain corporate goals will be pursued or that certain corporate actions will or will not be taken.

If this definition is accepted, further questions arise. The writer does not propose to descend to specifics and to consider possible provisions of such an agreement in any detail, but the questions of whether such agreements will be valid and of whether they will be enforceable do arise.

There is English[118] and Canadian[119] case authority for the proposition that there is nothing improper *per se* in some or all of the shareholders agreeing among themselves to vote in a particular way in company meetings. Moreover, while there are some conflicting American authorities, this would seem to be the better view in the United States as well[120]. It is therefore to be expected that Australian courts will also take this

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117. Steadman, *op cit*, 1092.
118. *Puddephatt* v *Leith* [1916] 1 Ch 200; *Greenwell* v *Porter* [1902] 1 Ch 530; *In re A. & B.C. Chewing Gum Ltd* [1975] 1 WLR 579.
119. *Ringuet* v *Bergeron* (1960) 24 DLR 2d 449.
120. O'Neal, *op cit*, para 5.04.

view[121].

While shareholder agreements will not be invalid *per se*, it does not follow that all such agreements will be upheld. Some agreements will be found invalid on other grounds. A shareholders' agreement with a fraudulent or oppressive purpose will, it is confidently predicted, be invalid. Similarly, certain provisions in shareholder agreements will be invalid. Finn suggests that provisions which purport to bind or fetter the discretion of a company director will be invalid and suggests that if it is desired to regulate the exercise of such powers they should be invested in the general meeting[122]. An unresolved question is whether an objection will be taken to a voting agreement that appears to be inconsistent with statute. An example would be an agreement to the effect that the articles are not to be altered without unanimous agreement, although such a provision appears to be inconsistent with the Australian companies acts. Finn's suggestion, with which the writer concurs, is that this situation is analogous with the *Bushell* v *Faith*[123] situation in which articles conferring weighted voting rights to circumvent a statutory provision were upheld.

In the United States, where much more consideration has been given to the problem, the validity of a shareholders' agreement appears to rest in the final result on the purpose for which it was framed. The test of validity, which was laid down by the New York Court of Appeals in *Clark* v *Dodge*[124] was that if an agreement damages nobody, if it can cause no

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121. Finn, *op cit*, 100; Kruger, *op cit*, 560.
122. Finn, *op cit*, 100-101.
123. [1970] AC 1099.
124. (1936) 199 NE 641 (NY Ct of App).

possible harm to minority shareholders, prospective investors in shares, creditors, or, in any perceptible degree, the public, there is no reason for holding it invalid[125]. This test has been widely accepted by the commentators although apparently not unanimously adopted by the courts[126]. The other factors which the courts will consider are compatability with public policy and adherence of the agreement to state laws and the corporate charter[127].

There remains the question of the enforceability of such an agreement. A breach of a shareholder agreement, as defined, will be a breach of contract and can be expected to sound in damages. However, this remedy will be grossly inadequate both because damage will be hard to quantify and because it will fall far short of conformity with the intention of the parties. On the authority of *In re A. & B.C. Chewing Gum Ltd*[128], breach of such an agreement will provide grounds for winding the company up on the "just and equitable" basis[129] and similarly relief under section 186 of the Uniform Companies Act would appear to be available. Under the terms of section 186(2)(b), an Australian court will have authority to order a purchase of shares from one party by another. The same subsection would also seem to give the court a statutory power to order that the affairs of the company be conducted in accordance with the terms of the agreement. An alternative would be to apply for orders for specific performance. It is suggested, however, that a court will be reluctant to adopt either of the last two alternatives unless it is

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125. *Clark* v *Dodge*(1936) 199 NE 641, 642 (NY Ct of App).
126. O'Neal, *op cit*, para 5.08.
127. Morganstern, *op cit*, 327.
128. [1975] 1 WLR 579.
129. Under s 222(1)(h) UCA.

apparent that such orders will lead to a final resolution of the conflict and that such a demonstration may be difficult. To avoid or minimize the danger of having to apply to the court for a remedy it is advisable to make provision in the agreement for the settlement of disputes. Once the validity of the shareholder agreement is recognized and the problem of enforcement is solved, the company lawyer will have added to his arsenal a control device which with careful usage will allow a fine-tuning of the corporate structure to achieve the aims and avoid the problems of conflicting interests that may arise in any joint venture[130].

3. VOTING TRUSTS

A voting trust is a type of shareholder agreement which contains a built-in enforcement device and was evolved to circumvent the refusal of American courts to enforce shareholder agreements which did not contain this device[131].

A voting trust is created when the participating shareholders, pursuant to a written trust agreement, endorse and transfer their share certificates and therewith the legal title to their shares to a trustee in return for certificates of beneficial ownership, the purpose of such an arrangement being solely to allow the trustee to vote the shares. During the period of the agreement, the trustee will exercise the voting rights attached to the stock according to the terms of the agreement but will remit any dividends to the beneficial owners. Thus the main characteristics of a voting trust are: (1) voting rights are separated

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130. Ghingher, *op cit,* 211.
131. Schwartz, L.J., *"Voting Trusts and Irrevocable Proxies"* (1968) 41 Temple LQ 480-481.

from beneficial ownership of the shares; (2) the grant of voting rights is intended to be irrecoverable for a definite period of time; and (3) the principal purpose of the grant is to acquire voting control of the company[132].

Although this device has been widely used in the United States, its possibilities have been largely ignored in both Australia and Britain. There are no relevant statutory provisions and there appears to be no reported decision from any other country dealing directly with the issues which arise from the use of this device. For this reason, the following discussion focuses on the American experience.

As has been noted above, the American states have adopted legislative provisions validating and regulating voting trusts. However, the use of the voting trust pre-dated the appearance of such provisions. Inasmuch as there are no such statutory provisions in Australia, it is still relevant for our purposes to examine the attitudes the courts adopted towards the use of the device in their absence.

The main issue at this stage in the history of the voting trust was whether or not the anti-separation doctrine should be held to preclude their use altogether. The principal objections to the validity of the voting trust were that it involved a divorce of beneficial ownership of the stock from voting power, thus constituting a breach of the duty owed by the stock owners to the other stockholders to exercise personal judgment in casting their vote, that it was contrary to public policy to place the control of the corporation in the hands of those without

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132. Schwartz, L.J., *op cit*, 481-482.

direct pecuniary interest and that it might involve control of the majority by the minority[133].

Certain courts were induced to accept voting trusts on the basis that, since the trustee was the legal owner of the stock, no separation of voting power from ownership was involved[134]. In so doing they allowed themselves to be diverted by a legal fiction from considering the policy basis of the objections. The mere fact that the trustee was the legal owner of the stock did not create any likelihood that he would act in the interest of the shareholders or the corporation[135].

One study[136] of the cases which preceded voting trust legislation categorized voting trusts according to whether or not they involved minority control. Where minority control was not involved it was found that, in general, the use of the device was allowed[137]. In such circumstances the majority involvement would tend to protect the interests with which the courts were concerned. Trusts in this category were employed to facilitate corporate reorganization or capitalization, to carry out some other definite plan on which the majority had agreed, or to apportion control among the various groups involved so as to ensure representation of those interests. In the case of a voting trust which effectuated a majority agreement, the only possible ground of attack is that it makes such a decision irrevocable. But inasmuch as the shareholders who so fetter their discretion are not fiduciaries, this objection cannot be upheld.

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133. Berger, *op cit*, 1211 quoting Ballantine, *Corporations*, (1927 ed) 587; and see *Warren* v *Pim* (1904) 59 A 773, 781 (NJ Err & App).
134. *Kann* v *Rossett* (1949) 30 NE 2d 204 (Ill App); *Clark* v *Foster* (1917) 167 P 908 (Wash SC) as cited by Schwartz, *op cit*, 485.
135. Schwartz, *op cit*, 485.
136. Bergerman, *op cit*.
137. See for example *Mobile & Ohio Railway* v *Nicholas* (1893) 12 So 723; *Clark* v *Foster* (1917) 167 P 908 (Wash SC) as cited by Bergerman, *op cit*, 451-455.

Where a voting trust resulted in minority control, courts generally were found to uphold it if the object was not to achieve such control but was some other aim deemed particularly desirable[138]. The courts by taking into account the objective of the trust were ensuring that the interests protected by the anti-separation doctrine were not sacrificed. This left for consideration those instances in which the voting trust was used especially to effect minority control. There no general agreement was reached[139]. Two solutions were possible: such trusts could be ruled invalid *ab initio* or the courts could allow such a use and concern themselves with ensuring that the power of the trustees was not used oppressively or fraudulently. The judicial debate on this question was eventually pre-empted by the enactment of voting trust provisions by the legislatures of the American states.

All but one American state[140] now regulates the use of voting trusts. These statutes impose strict requirements on the grant of authority. Thus the duration of the voting trust is limited and its existence must be proclaimed. In addition, the validity of a particular voting trust continues to depend upon the objectives and purposes of the agreement[141]. Thus it remains open to any shareholder in the corporation to challenge what is considered to be an abuse of the voting trust device[142].

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138. See for example *Frost* v *Carse* (1919) 108 A 642 (NJ Err & App) as cited by Bergerman, *op cit*, 456-458.

139. Courts in Virginia and Pennsylvania at one time seemed inclined to uphold such trusts while courts in Illinois and Georgia definitely condemned them: Bergerman, *op cit*, 462 citing *Boyer* v *Nesbitt* (1910) 76 A 103 (Pa SC); *Carnegie Trust Co* v *Security Life Insurance Co* (1910) 68 SE 412 (Va App); *Warren* v *Pim* (1904) 59 A 773 (NJ Err & App); *Luthy* v *Ream* (1915) 110 NE 373 (Ill SC); *Morel* v *Hoge* (1908) 61 SE 387 (Ga SC).

140. Woloszyn, J.J., "*A Practical Guide to Voting Trusts*" (1975) 4 U Balt L Rev 245, 247-249; the exception being Massachusetts.

141. *Ibid*, 247.

142. Berger, *op cit*, 1217-1219.

Among the drawbacks of the voting trust device is the fact that with legal title to the stock, the stockholder relinquishes all his statutory rights. This negative feature is, however, avoidable where legislative provisions govern the use of the device. It is then possible to provide that the voting trustee should acquire only the right to vote and that all other rights appurtenant to share ownership remain vested in the beneficial owner of the share[143].

It is suggested that, inasmuch as there are legitimate business purposes which may be served by binding agreements as to the use to be made of the corporate vote, the desirability of enacting statutory provisions permitting the use of voting trusts in Australia should be considered. However, it may well be unnecessary to enact provisions enabling the use of shareholder agreements as well as provisions for voting trusts, and shareholder agreements would appear more desirable as they are more flexible.

It is submitted that it would be appropriate to adopt some statutory provisions governing shareholder agreements despite the fact that such agreements appear to be valid on the law as it stands in Australia at the moment. In North America the first statutory provisions for shareholder agreements were adopted in North Carolina in 1957[144], but although other states have since adopted similar provisions, it cannot as yet be said that they are standard features of American corporation statutes. The Canada Business Corporations Act[145] contains a provision which allows

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143. Schwartz, *op cit*.
144. Steadman, *op cit*, 288.
145. Can Bus Corp Act s 140.

shareholders to restrict the management powers of the directors by means of an unanimous agreement, but various aspects of this provision have been criticized[146]. In Britain the Companies Act of 1976 included provisions to enable the company to call upon specific shareholders to say whether they had entered into an agreement as to how their shares would be voted and to reveal the terms of such an agreement. The answers to such queries then become a matter of public record[147]. The intention behind the legislation, which is linked to that requiring disclosure of substantial shareholdings, is to prevent a group from using the device to gain secret control of the company. In Australia there is no need for a provision such as that contained in the Canadian statute as powers governed by statute there are here controlled more flexibly. However, Australian provisions could advantageously require that the agreement be in writing, that it be made a matter of public record and perhaps that a minimum percentage of the members of the company be parties to it.

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146. Sohmer, D., "*Controlling the Power to Manage in Closely Held Corporations*" (1976) McGill LJ 673.
147. Companies Act, 1976 (UK) s 27(3) and (5).

PART IV CONVOCATION OF THE GENERAL MEETING

To call or cause a meeting to assemble is to convoke it. The decision to convoke a general meeting is implemented by sending out a notice of meeting. The two topics of convocation and notice are therefore very closely linked and are usually treated together, although the distinction is periodically reasserted by the courts[1]. In this thesis they have been separated to allow the writer to focus first on the aspect of the authority to convoke a meeting before turning to examine the functions of notice.

As a rule, general meetings of company shareholders are convoked by the board of directors of the company in the exercise of its executive function. It is a fact testified to by the Berle and Means study[2] that company managements will, in certain circumstances, gain a control of a company not dependent on shareholding. This control, as has been seen, derives in large part from management control of the corporate proxy machinery. Nevertheless, the power to convoke or to refuse to convoke corporate meetings together with power over the agenda of such meetings derived from control over the notice of meeting can be a useful tool in any tactical battles between management and dissident shareholder groups. To prevent the abuse of this tool, companies acts in Australia[3], as in

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1. See for example *Vawdon* v *South Sydney Junior Rugby League Club* (No 406 of 1976, decision of Wootten J, NSW Supreme Court, 29 March 1976, unreported).
2. Berle, A.A. and Means, G.C., *The Modern Corporation and Private Property*, (New York, McMillan & Co, 1932); see above 3, 44.
3. UCA ss 137 and 142.

Great Britain[4], Canada[5] and the United States of America[6], contain provisions that may be resorted to to convoke a meeting independently of the action of the board of directors. These provisions enable the court or the shareholders themselves to convoke a general meeting in certain circumstances. They guard against the possibility that there may be no board of directors or that the board of directors may refuse to act.

It is difficult to gain a picture of the utility of these provisions in Australia inasmuch as no statistics are available to show how often or how successfully they have been invoked in Australia, but since 1970 four cases involving such meetings have been decided and reported[7].

The Midgley study revealed no instance in which the provisions had been resorted to in the ten years between 1960/61 to 1969/70 in the fifty-five British companies surveyed[8]. Midgley states that the negative response does not necessarily imply a general absence of discontent but may suggest that dissatisfied shareholders have had no grounds or occasion to make use of the provisions, or that the expense and difficulty of mustering adequate support is a deterrent, or that shareholders do not have sufficient knowledge, experience or confidence to organize opposition or to propose a remedy for company ills[9]. The Lawrence Committee, reporting to the Ontario legislature in 1967, also stated that these devices were

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4. Companies Act, 1948 (UK) ss 134 and 132.
5. Can Bus Corp Act ss 137 and 138; Bus Corp Act (Ont) ss 109, 110 and 111.
6. Mod Bus Corp Act Ann 2d s 28.
7. *Dominion Mining NL* v *Hill* [1971] 2 NSWLR 259; *Holmes* v *Life Funds of Australia Ltd* [1971] 1 NSWLR 860; *Taylor* v *McNamara* [1974] 1 NSWLR 164; *Turner* v *Berner* [1978] 1 NSWLR 66.
8. Midgley, K.,"*How Much Control Do Shareholders Exercise?*"(1974) 114 Lloyd's Bank Rev 24, 32.
9. *Ibid*, 32-33.

seldom resorted to and recommended certain changes in the legislation[10] to make the remedy more readily available[11]. Some consideration will be given below to the wisdom of adopting similar measures in Australia.

A. THE BOARD'S AUTHORITY TO CONVENE GENERAL MEETINGS

There are three different types of general meetings of company shareholders, the statutory meeting, the annual general meeting and the extraordinary general meeting. The statutory meeting is one which a public company is required to hold within three months of the date it commences business[12] and does not concern us here. Australian company law requires every company to hold an "annual general meeting" at least once in every calendar year[13]. Any other general meeting is known as an extraordinary general meeting[14]. Procedures for convening extraordinary general meetings will be considered below, but the first concern is with the annual general meeting.

1. THE ANNUAL GENERAL MEETING

The Australian Companies Acts make no provision as to the manner in which annual general meetings are to be convened[15], nor is this

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10. Ontario Legislative Assembly, *Interim Report of the Select Committee on Company Law* (1967), hereinafter referred to as the *Lawrence Report*, para 8.41.
11. See below, 239-240.
12. UCA s 135.
13. UCA s 136.
14. UCA Fourth sched Table A reg 43.
15. UCA s 136(1).

deficiency cured by Table A articles[16] now in force. This is despite the fact that the Table A articles to the New South Wales Act which preceded the Act now in force provided that the annual general meeting should be held at a time and place prescribed by the company in general meeting or in default at a time and place appointed by the directors[17].

The British Act contains no reference in its body to the convening of the meeting in the normal course of events but the appended articles give the directors the power to appoint a time and place[18]. The Canadian federal legislation provides that the directors "shall call" the annual meeting, a mandatory provision as clearly appears when the contrast is drawn with a provision to the effect that the directors "may call" a special general meeting[19]. The Ontario statute has no provision as to the responsibility for calling annual general meetings[20], thus resembling the Australian legislation, while the American Model Business Corporations Act provides that "an annual meeting of the shareholders shall be held at such time as may be stated or fixed in accordance with the by-laws"[21].

An American commentator states that in the case of an annual meeting, a formal call is not necessary unless the by-laws or a statute require such a call because the by-law provision for the annual meeting is deemed to be the call or convocation thereof[22]. The provision allowing

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16. UCA Fourth sched Table A reg 43.
17. Companies Act, 1936-1955 (NSW) Fourth sched Table A reg 39.
18. Companies Act, 1948 (UK) First sched Table A reg 47.
19. Can Bus Corp Act s 127.
20. Bus Corp Act (Ont) ss 106 and 107.
21. Mod Bus Corp Act Ann 2d s 28 para 2.
22. Aranow, E.R. and Einhorn, H.A., *Proxy Contests for Corporate Control*, 2nd ed, (New York, Columbia University Press, 1968) 60.

the corporation to fix the time in accordance with the by-laws is a relatively new innovation as formerly the by-laws were required to state the time for the annual general meeting[23]. The discretion so allowed is not, however, invariably entrusted to the board of directors. If the old practice of fixing the time in the by-laws is not adhered to, the discretion may be entrusted to the president of the corporation, its chief executive officer or general manager instead of to the board of directors[24].

An Australian company under the legislation currently in force might adopt the expedient of naming the time and place of the annual general meeting in the articles, but this does not seem to be normal procedure. Another alternative which, it is suggested, would not be invalid under the Act or even under the Table A articles would be for a validly convened general meeting to fix the date for the next annual general meeting as could be done under the old Table A articles. Neither procedure is likely to be adopted, however, because by doing so the company will lose a great deal of flexibility. The normal procedure is for the board of directors to convene the annual general meeting. Authority to do so can, it appears, be derived from regulation 73 of the Table A articles[25]. The power to convene an annual general meeting is clearly a power of the company "not by the Act or by these regulations, required to be exercised by the company in general meeting", and where this power has not in fact been exercised by a general meeting there is nothing to raise any question as to the effect of the proviso to that article. The conclusion that the board of directors has authority to call an annual general meeting of the company is affirmed by the penal provisions embodied in the

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23. Mod Bus Corp Act Ann 2d s 28.02.
24. See for example *Bloch* v *Gershman* (1947) 70 NYS 2d 530 (SC); *Pennington* v *George W. Pennington & Sons* (1915) 148 P 791 (Cal SC).
25. See above, 126 *et seq*.

Act providing that if default is made in holding an annual general meeting, the company and "every officer of the company who is in default" shall be guilty of an offence against the Act[26].

2. EXTRAORDINARY GENERAL MEETINGS

The Table A articles to the Australian Companies Acts specify that: "Any director may whenever he thinks fit convene an extraordinary general meeting"[27]. Individual directors have specific authority to convene extraordinary general meetings whereas no provision is made to allow the board of directors to make the decision as a body. On the other hand, nothing prohibits the board from doing so and accordingly the board can, on the reasoning outlined above, convene an extraordinary general meeting by exercising the powers derived from article 73.

By way of contrast, the British articles provide that "the directors may whenever they think fit, convene an extraordinary general meeting"[28]. It has been held that an article in these terms refers to a power which the directors as a body may exercise, and that an individual director or even two individual directors will not be able to exercise the power without consulting the others[29]. Where under such an article an attempt was made to convene an extraordinary general meeting to wind up the company without holding a board meeting, it was held ineffective[30]. It is stipulated that a director may call an extraordinary general meeting

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26. UCA s 136(4). See also Crimes Act 1958 (Vic) s 127 which makes wilful refusal of a director of a body corporate or public company to convene a meeting in accordance with any rules relating thereto a misdemeanour punishable by three years imprisonment.
27. UCA Fourth sched Table A reg 44.
28. Companies Act, 1948 (UK) First sched Table A reg 49.
29. *Browne* v *La Trinidad* (1887) 37 Ch D 1, 11 per Lindley LJ.
30. *Re Haycraft Gold Reduction and Mining Co* [1900] 2 Ch 230.

when no quorum exists[31]. The Australian position would seem to be preferable from the point of view of shareholder democracy because it increases the chance that a matter will be referred to the general meeting. If a dispute arises among members of the board it will not be possible to sweep it under the carpet by outvoting a dissident at a board meeting.

The Canadian provisions resemble the British. The Ontario statute empowers "the directors" to call general meetings at any time[32], while the federal legislation provides that the directors may call special general meetings[33]. The term extraordinary general meeting is not employed in either jurisdiction, but the contrast with the annual meeting is still drawn. The phrase "the directors" as used in both statutes will, it is suggested on the basis of the British authority cited above, be interpreted to mean the directors acting as a body. The Model Business Corporations Act also specifies that the board of directors may call a special meeting but, although it allows the corporation to grant the power to additional nominees, does not itself provide that an individual director will have that power[34]. It therefore appears that in this respect the provision contained in the Australian Table A articles is broader than that found in comparable legislation.

3. TWO PROBLEMS THAT MAY ARISE

Company powers entrusted to the board of directors must be exercised

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31. Companies Act, 1948 (UK) First sched Table A reg 49.
32. Bus Corp Act (Ont) s 108.
33. Can Bus Corp Act s 127(b).
34. Mod Bus Corp Act Ann 2d s 28 para 2.

bona fide in the interests of the company as a whole[35]. It has been specifically held that, when entrusted to an individual director, the power to convene an extraordinary general meeting is a "fiduciary power of a discretionary nature"[36]. Pennycuick J so held in a case in which he was asked to order the officer of a subsidiary company, who was alleged to be in breach of a duty of good faith owed personally to the holding company, to convene an extraordinary general meeting. He declined to make the order sought[37]. Inasmuch as it is difficult to conceive of a situation in which an exercise of the power to convoke a meeting would serve the interests of the officer concerned and not the interests of the company, it is unlikely that questions of improper purpose will arise. Where an officer refuses to call such a meeting there may be a question of improper purpose, but this will be so hard to prove that the question is unlikely to be argued. Resort to the provisions bypassing this official will usually prove more rewarding.

Much litigation has focussed on the question of whether an irregularity in one or more of the appointments to the board or in convening the board meeting will have the effect of invalidating the general meeting which it summons. In several of these cases it was found that the action of the board, though irregular, could be supported under validating provisions[38]. However, it was held *obiter* that, even if there was such an

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35. See for example *Re Smith and Fawcett Ltd* [1942] Ch 304, 306; see also Ford, H.A.J., *Principles of Company Law*, (Sydney, Butterworths, 1974), [1501], [1529].
36. *Pergamon Press Ltd* v *Maxwell* [1970] 2 All ER 809.
37. *Idem;* see also *Pergamon Press Inc* v *Ross* (1970) 306 NYS 2d 103 (SC) as relevant to the history of the case cited.
38. *British Asbestos Co* v *Boyd* [1903] 2 Ch 439; *Transport Ltd* v *Schonberg* (1905) 21 TLR 305 where articles equivalent to UCA Fourth sched Table A reg 89 applied; *Boschoek Pty Ltd* v *Fuke* [1906] 1 Ch 148 where the meeting ratified the actions of the purported directors.

initial irregularity that it could be said that the court could have intervened to prevent the board from acting, the general meeting which assembles in response to the call will have power to act when the notice was issued in the normal way by the body generally assumed to be the properly constituted board of directors[39]. To hold otherwise would be, according to Lindley LJ, to paralyse the whole course of business of the company[40]. A similar position was taken in an early New South Wales case[41] where the validity of winding up the company was challenged on the basis that the board of directors which convened the meeting to decide the question had been invalidly elected, the notice of the meeting to elect them having been too short. This challenge was held to be poorly conceived, but it was held *obiter* that a liberal view should be taken when the directors acted merely to call the shareholders together[42].

Inasmuch as there are now statutory provisions[43] allowing the court or the shareholders to convene a general meeting, there is no need to concede an irregularly constituted board the power to convene such a meeting before the event. However, it would appear to be worse than useless, after the event, to insist on convening a new meeting to reconsider the decisions taken at meetings where the shareholders have accepted the call as valid. Where the general meeting has actual knowledge of the defect affecting the exercise of the board's power, specific ratification of the board's actions is, of course, necessary. Where it is universally assumed that

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39. *Browne* v *La Trinidad* (1887) 37 Ch D 1, 10 per Cotton LJ.
40. *Ibid*, 11; see also *Southern Counties Deposit Bank Ltd* v *Rider and Kirkwood* (1895) 73 LT 374.
41. *Re the Neokratine Safety Explosive Co of NSW Ltd* (1891) 12 NSWR (Eq) 269.
42. *Ibid*, 276.
43. See below, 234-238, 251-260.

the purported board of directors is validly exercising its powers, the validity of the general meeting should be seen as independent of the validity of the board meeting. The exercise of the power to convene and give notice of general meetings may in this respect be distinguished from the exercise of any other power by such a board. Where the authority of the board to call a meeting is challenged at or before its convocation, the universal assumption does not exist and before the decisions of the general meeting will be effective, it must be proved either that the board had actual authority to convene a meeting or that the general meeting formally ratified the action in full knowledge of the defect.

B. MEMBERS' POWER TO INITIATE MEETINGS

1. POWER TO INITIATE DIRECTLY

In Australia, as also in Britain, Canada and the United States, there are statutory provisions[44] giving members of a company the right, under certain circumstances, to requisition an extraordinary general meeting. But the statutory provision that "so far as the articles do not make other provision...two or more members holding not less than one-tenth of the issued share capital...may call a meeting of the company"[45] is more basic. Where not excluded by the articles it gives the members a right to convene a meeting directly.

The question, then, is whether the Table A articles attached to the

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44. See below, 236.
45. UCA s 138(1).

Australian Companies Act do exclude such a right. It has been stated[46] that the Uniform Companies Act articles make no provision for the convocation of the annual general meeting[47]. It therefore appears that the right of two or more members, with a sufficient shareholding, to call an annual general meeting has not been excluded. Occasions for the use of this power will, however, arise very rarely. The Table A articles do make provision for the calling of extraordinary meetings by any director, and on requisition[48]. The question arises whether this regulation is sufficient to exclude the statutory provision in question. There is no express exclusion, but the fact that there is a provision on the subject may be sufficient basis for an exclusion.

Discussing a comparable section[49], a British commentator states that the relevant British articles allow this power to be used to call an extraordinary general meeting only when a quorum of directors does not exist[50]. The British articles, unlike the Australian, expressly stipulate that the members shall have this power where there is no quorum of directors[51]. This stipulation can be interpreted as an exclusion by using the *expressio unius* principle of construction. However, the commentator also supported his statement by reference to article 80 of the British Table A and this article does have an Australian equivalent[52]. If this general article is sufficient authority for the statement, the Australian Table A articles will exclude this statutory provision.

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46. See above, 227-230.
47. UCA Fourth sched Table A reg 43.
48. UCA Fourth sched Table A reg 44.
49. Companies Act, 1948 (UK) s 134(b).
50. Pennington, R.R., *Company Law*, 3rd ed (London, Butterworths, 1973) 535.
51. Companies Act, 1948 (UK) First sched Table A reg 49.
52. UCA Fourth sched Table A reg 73.

An argument could be marshalled for the proposition that the Australian Table A articles do not exclude the statutory provision entitling a company's members to convene a general meeting, but the question has little or no practical significance. The same members will be able to set the company machinery in motion by means of a requisition and by doing so will more easily accomplish their objective.

There is no equivalent provision in the legislation enacted by either the Ontario or the Canadian federal parliament. The American Model Business Corporations code provides that members holding one-tenth of the voting rights may convene a special meeting[53].

2. POWER TO INITIATE BY REQUISITION

Provisions entitling members to requisition extraordinary general meetings are potentially of great significance. Management, it has been pointed out, "would like nothing better than to be able to call meetings when it wanted them but to be under no obligation to do so when it did not"[54]. To ensure that management does not achieve this state of affairs in the face of conflicting desires of its members, various jurisdictions have enacted statutory provisions obliging company managements to convene meetings on requisition[55]. In addition to such statutory provisions, the articles of association of a company may contain a provision giving the shareholders a contractual right to requisition a meeting.

The Australian Uniform Companies Act stipulates that the directors of a

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53. Mod Bus Corp Act Ann 2d s 28.
54. Gower, L.C.B., *Principles of Modern Company Law*, 3rd ed (London, Stevens & Sons, 1969) 476.
55. UCA s 137; Companies Act, 1948 (UK) s 132; Can Bus Corp Act s 137; Bus Corp Act (Ont) s 109.

company shall, on the requisition of members holding an interest in the company sufficient to give them at least one-tenth of the voting rights in general meeting, forthwith convene an extraordinary general meeting to be held within two months of the receipt of the requisition[56]. The requisition, which may consist of several documents in like form, is to state the objects of the meeting, to be signed by the requisitionists and to be deposited at the registered office of the company[57]. If the directors do not comply with the requisition within the stipulated time, the requisitionists acquire the right to convene a meeting themselves[58] and to claim from the company the repayment of any reasonable expenses incurred in so doing[59]. The British provision[60] is virtually identical to the Australian provision. The provisions adopted recently in Ontario[61] and by Canada's federal parliament[62] are markedly different from the Anglo-Australian provisions in draftsmanship. There are fewer distinctions in substance but the differences that do exist will be noted below in the course of the detailed analysis of the Australian provisions which immediately follows this section.

American laws as to requisition rights are, in comparison, non-existent. Although company by-laws often give the stockholders a right to requisition a meeting[63], the Model Business Corporations Act contains a provision allowing shareholders to call a meeting but no provision to enable them to put the company machinery into operation. Nevertheless,

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56. UCA s 137(1).
57. UCA s 137(2).
58. UCA s 137(3).
59. UCA s 137(4).
60. Companies Act, 1948 (UK) s 132.
61. Bus Corp Act (Ont) s 109.
62. Can Bus Corp Act s 137.
63. Aranow and Einhorn, *op cit*, 72; see also *Pergamon Press Ltd* v *Maxwell* [1970] 2 All ER 809.

some of the state corporation statutes require the officers to call and convene a special meeting of the stockholders upon a request in writing of the holders of a specified percentage of outstanding voting stock[64]. Because of the relative importance of the by-law provisions, one of the more interesting questions in this area, for the American lawyer, is whether the board can amend the by-laws to increase the percentage requirements when faced with such a request[65]. This question is of little relevance in Australia and will not, therefore, be discussed.

The explanation for the comparative under-development of American law in this area may be found in the fact that the Americans have a different attitude towards the agenda of the annual general meeting. It is, generally, the American position that any member is free to raise any matter of concern at such a meeting[66]. This might well make requisition rights less important as in most cases the stockholder will be content to wait for this opportunity. However, this is not a complete answer to the suggestion that more elaborate provision should be made for such rights.

C. DETAILS OF REQUISITION PROCEDURES

1. SUFFICIENT INTEREST

The statute does not give company members an individual right to demand

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64. Aranow and Einhorn, *op cit*, 72 citing, eg, Cal Corp Code Ann s 2202; Ill Stat Ann Ch 32 s 157.26; Ind Stat Ann s 25-207; NY Bus Corp Law s 603(a).
65. Aranow and Einhorn, *op cit*, 73-74 citing *Segal* v *United Cigar Whelan Corp* (1951) 126 NY LJ 132, 133 (SC) and *Samuels* v *Air-way Electric Appliance Corp*, civ action No 543 (Del Ch)(1954).
66. See further below, 278 *et seq*.

that a meeting be held. Rather, the right to requisition a meeting is what has been called a qualified minority right[67]. To bring the statutory provisions governing requisitions into effect, the requisition must be supported by members having a sufficient interest in the company. It will not be sufficient for one member holding one of thousands of shares to sign a request that a general meeting be held. Both the Australian and the British statutes define a sufficient interest as not less than one-tenth of such paid up capital as carries the right of voting at general meetings or, in the case of a company not having a share capital, of members representing not less than one tenth of the total voting rights of all members[68]. The Australian Act, but not the British, further provides that, in either case, a requisition will be valid if signed by not less than two hundred members[69].

The stipulation, as condition precedent for the requisitioning of a meeting, that sufficient support be mustered for the requisition, is designed to prevent the harassment of company management and the dissipation of company resources on what is, for larger companies, a costly process. However, this condition precedent may well have proved too effective. Although, unfortunately, it is not possible to state how many times these provisions have been invoked in Australia, it may be noted that the Lawrence Committee in Ontario felt that a ten per cent support requirement was too high[70]. In the light of this finding both the Ontario and the Canada Business Corporations Act require only five

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67. Schmitthoff, C.M., *Palmer's Company Law*, 22nd ed (London, Stevens & Sons, 1976) 619.
68. UCA s 137(1); Companies Act, 1948 (UK) s 132(1).
69. UCA s 137(1).
70. *Lawrence Report, op cit*, para 8.4.3; see also Dickerson, R.W.V., Howard, J.L. and Getz, L., *Proposals for a New Business Corporations Law for Canada*, (Ottawa, Information Canada, 1971), hereinafter referred to as the *Dickerson Report*, para 289.

per cent, or one-twentieth of the voting rights, support for a requisition[71]. In larger companies with widely dispersed memberships, the cost and difficulty of securing support from ten per cent of the members might well prove an obstacle to even the most responsible attempts to have a meeting summoned[72], especially as some attempts to secure support may prove ineffective. Reducing the support requirement from ten to five per cent is one answer to this problem. However, the Australian alternative of stipulating a minimum number of members appears preferable as any percentage requirement may translate into an unreasonably high number of individuals in a particular case.

It should be noted that the necessary support must have been mustered and must exist at the date of deposit of the requisition[73]. Thus it would not matter if one of the requisitionists were to sell some or all of his shares between the date of deposit and the date on which the meeting is summoned[74]. Nor, on case authority[75], does the fact that a requisitionist disavows his action in so giving his support discharge the directors from the obligation of calling a meeting. But it may prevent that requisitionist from joining in calling a meeting if the board of directors neglects to do so, even if that requisitionist again changes his mind. On the other hand, in one recent American decision[76], it was held that the fact that a requisitionist was not a registered shareholder when his signature was secured was irrelevant if he was one

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71. Bus Corp Act (Ont) s 109(1); Can Bus Corp Act s 137(1).
72. *Lawrence Report*, *op cit*, para 8.4.1; Gower, *op cit*, 476.
73. UCA s 137(1)
74. There is no independent Australian case authority for this proposition but see *Glahe* v *Arnett* (1924) 225 P 796 (Idaho SC); *Smith* v *Upshaw* (1962) 124 SE 2d 751 (Ga SC).
75. *South Norseman Gold Mines NL* v *Macdonald* [1937] SASR 53.
76. *Richman* v *De Val Aerodynamics* (1962) 183 A 2d 569 (Del Ch).

when the deposit was made. Considering that there may be a prolonged period between lodgment and registration of the share transfer, this holding may be desirable, but *quaere* whether it will be followed in Australia.

2. THE PURPOSE OF THE MEETING

The requisition must specify the object for which the meeting is to be held[77], and if a special resolution is to be proposed, the meeting will not be properly convened by the directors unless they give the requisite notice[78]. Two cases[79] in which the board has purported to comply with a requisition which set out a number of objects by convening a meeting to deal with some but not all of the issues may be cited. In *Isle of Wight Railway Co* v *Tahourdin*[80] the argument for the board was that a resolution in the terms set out in the requisition would be illegal. It was held that, as the object as set out might be accomplished by a legal resolution, the objection was ill-founded and the requisitionists could proceed on the basis that the board was in default. In *Turner* v *Berner*[81], it was held, following *Tahourdin*, that if an object of the requisition cannot be lawfully effectuated at the meeting, then the directors are entitled to omit that object from the notice of meeting[82]. The directors' refusal to include in the notice of meeting the proposed resolution to the effect that the Managing Director had committed breaches of section 124(1) of the Companies Act was upheld even though

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77. UCA s 137(2).
78. UCA s 137(5)
79. *Isle of Wight Railway Co* v *Tahourdin* (1883) 25 Ch D 320; *Turner* v *Berner* [1978] 1 NSWLR 65.
80. (1883) 25 Ch D 320.
81. [1978] 1 NSWLR 65
82. [1978] 1 NSWLR 65, 72.

the judge conceded that the meeting could consider the allegations[83]. It therefore appears, although this is not spelled out in the Australian Act, that the objects for which the meeting may be requisitioned must be "proper" within the meaning of that term as used in the American proxy rules[84]. The Canadian Acts[85] contain express stipulations limiting the objects of a requisitioned meeting, the effect of which is to ensure that the meeting will only consider "proper" subjects.

3. SEVERAL DOCUMENTS

The stipulation that a requisition may consist of several documents in like form has given rise to certain problems. In one case[86], documents requisitioning a meeting for the purpose of reconstituting the board of directors were deposited together with documents which as well as specifying that purpose also stipulated that the meeting was to consider the affairs of the company in general. On the ground that the two sets of documents were not in like form the board refused to call a meeting. The court held that the objection could not be sustained as the addition made no difference in the general purport of the requisition. It therefore appears that "in like form" is to be interpreted as meaning substantially similar rather than exactly identical.

Where a requisition is comprised of several documents, the question arises whether all of these documents must be lodged at the same time. It has been held[87] that where the documents in question formed part of "one identifiable or entire activity", the fact that one set was lodged

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83. *Turner* v *Berner* [1978] 1 NSWLR 65, 71, 72.
84. See above, 161 *et seq.*
85. Can Bus Corp Act s 137(3)(c) and s 131(5)(b)-(e).
86. *Fruit and Vegetable Growers Association* v *Kekewich* [1912] 2 Ch 52.
87. *Dominion Mining NL* v *Hill* [1971] 2 NSWLR 259.

ten days before the second set would not excuse the board of directors from complying with the requisition. The obligation to do so would arise on the date on which documents manifesting sufficient support for the requisition were received.

4. TIMING OF THE MEETING

The lodging of a valid requisition obliges the directors of a company to convene an extraordinary general meeting "forthwith"[88]. In line with a recommentation of the Jenkins Committee[89], the Australian legislation now provides that this meeting should be held as soon as possible and must be held not later than two months after the receipt by the company of the requisition[90]. The requisitionists acquire default rights under sub-section (3) if the directors fail to issue the call within twenty-one days. It may be noted here that the duty to comply with the requisition falls on the board of directors, and for this reason a call issued by the company secretary in purported compliance with the requisition will be invalid[91] and a default will have occurred.

5. THE REQUISITIONISTS' POWER TO CALL A MEETING

Where the directors of a company fail to comply with a requisition, the requisitionists themselves may proceed to summon a meeting[92]. But the default must in fact have occurred. A manifestation by the directors of an intention not to comply with the requisition is insufficient. The

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88. UCA s 137(1).
89. Great Britain Board of Trade, *Report of the Company Law Committee* (1962), hereafter referred to as the *Jenkins Report*, para 458.
90. UCA s 137(1).
91. *Re State of Wyoming Syndicate* [1901] 2 Ch 431.
92. UCA s 137(3).

requisitionists may not anticipate the expiration of the stipulated period[93].

When a default has occurred and the requisitionists elect to exercise the right to convene a meeting themselves, they are deemed to be acting in an official capacity. The right that they exercise is not a personal proprietary right. The requisitionists in proceeding to convene a meeting step into the shoes of the defaulting directors and are subject to the same duty to exercise this power in the interests of the company as a whole rather than in their own personal interest. It was so held in *Adams* v *Adhesives Proprietary Ltd*[94]. The plaintiffs in that case had acquired a majority of the shares in the company to hold in a voting trust. However, under the articles, voting rights were not to accrue to them until three months after registration of the transfer. The defendants' plan was to take advantage of this fact by requisitioning a meeting and removing the board of directors within this period. On receipt of the requisition, the board convened a meeting to be held after expiration of the period of disqualification. This amounted to a failure to comply with the requisition, although it was dictated by the "overriding duty of the directors not deliberately to call a meeting for a date which would result in many of the shareholders not being able to exercise their vote"[95]. The requisitionists could not be denied their default rights but the equities were preserved when it was held that they were under the same duty as the directors not to call a meeting for a date on which many of the shareholders would not be able to vote.

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93. *Aberfeldie Gold Mining Co* v *Walters* (1876) 2 VR (Eq) 116; see also *State ex rel Kahn* v *Johnson* (1948) 199 P 2d 556 (Utah SC).
94. (1932) 32 SR (NSW) 398.
95. *Ibid*, 402.

Requisitionists exercising the power to call a meeting which arises when the directors default will be subject to the same supervision of their powers by the court as the directors[96], but it may also be suggested that the same validating provisions will apply. Thus, in an Australian case[97], section 366 was applied to validate a meeting which had been called by requisitionists after the directors defaulted. The meeting's validity was in doubt because of the accidental omission to give notice to certain shareholders.

There is a Canadian case[98] in which requisitionists who had issued a call for a meeting which was invalid because the default had not yet occurred and because the notice was not sent to all shareholders, were allowed to issue a second notice which was held valid. The argument that they had exhausted the rights they acquired from the requisition by issuing the first invalid notice was rejected. Inasmuch as the purpose of the provision is to bring corporate disputes before the general meeting for solution and not to confer a personal right, the conditions of which must be scrupulously observed, it is submitted that this authority would be followed in Australia.

Not all requisitionists need concur in calling a meeting when the directors default, but concurrence must be obtained from requisitionists representing more than one half of the total voting rights initially supporting the requisition[99]. Under this provision it may be necessary to secure the concurrence of members representing more than five per cent

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96. *Adams* v *Adhesives Proprietary Ltd* (1932) 32 SR (NSW) 398, 402.
97. *Holmes* v *Life Funds of Australia Ltd* [1971] 1 NSWLR 860.
98. *Gold Rex Kirkland Mines* v *Morrow* [1944] 4 DLR 780.
99. UCA s 137(3).

of the total voting rights. Although the requisition need only be supported by a ten per cent interest in the first place, more support may in fact have been secured and in this case, under the provision as it now stands, a correspondingly greater support for the exercise of default rights must be secured. It is submitted that the statute should be changed to stipulate that regardless of the support first secured, only one-twentieth or five per cent support need be marshalled for subsequent action, or that the Canadian example[100], which allows an individual shareholder to pursue a requisition should be followed.

6. REASONABLE EXPENSES

Where the requisitionists decide to call a meeting under this provision they acquire a statutory right to recover from the company any reasonable expenses they incur in doing so. The company, in turn, is authorized to recover the money from the directors who were in default by retaining any sums due to them in respect of their services as directors[101]. Although it may be that the sums due or to become due to the directors will not cover the expenses so incurred, the penalty does match the crime inasmuch as what the directors have failed to do is to discharge a duty of the office and it is therefore fair that they should not be paid for occupying that office. Apparently the view is not taken that the offence is one that harms the company so badly that a civil or criminal penalty is appropriate. One difficulty with the interpretation

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100. Bus Corp Act (Ont) s 109(4); Can Bus Corp Act s 137(4).
101. UCA s 137(4).

of this subsection was removed when in 1976[102] New South Wales amended its Companies Act by removing from subsection (1) a requirement that the requisitionists deposit with the requisition a sum sufficient to cover postage of notice to the shareholders. While this requirement was in force the ambit of the term "reasonable expenses" was strictly limited

It may be observed that the Australian provision as to expenses cannot be said to function as an incentive to the requisitionists, but at least the Australian shareholder is not left to wonder whether he will in fact recover his expenses. Neither the Ontario nor the Canada Business Corporations Act affords the requisitionists the same assurance. The question of whether such expenses may be recouped is one that is left to the general meeting in both cases[103]. It appears, therefore, that Canadian directors are not under an absolute duty to comply with the requisition. If the directors decide to comply with the requisition on the basis that the requisitionists have raised a real question that the general meeting should decide, then the company will meet the costs. If, on the other hand, the directors decide that there is no real question, the requisitionists pursue the matter at their own risk. In theory this provision appears to offer an additional safeguard against the dissipation of company assets on costly meetings. A danger lies, however, in the fact that the directors may fail to exercise their discretion *bona fide* in the best interests of the company as a whole. If they decide not to call a meeting even though a genuine corporate dispute exists, the majority may subsequently penalize requisitionists by refusing to support a motion

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102. Companies Act (Amendment) Act, 1976 (NSW) c1 s 3 and sched 5 s 27, the purpose of these revisions being to bring New South Wales legislation into line with that of the other Interstate Corporate Affairs Commission states.

103. Bus Corp Act (Ont) s 109(1); Can Bus Corp Act s 137(6).

that their expenses be met. Equitable principles will prevent the majority from perpetrating a fraud on the minority[104], but proving that a failure to pass such a motion constitutes such a fraud will be very difficult. The writer respectfully submits that the Australian provisions imposing an absolute duty to reimburse the requisitionists are preferable.

7. INJUNCTIONS

Suggestions have recently been made to the effect that the existence of statutory provisions for default rights would not prevent the court in an appropriate case from issuing an order compelling the directors to summon a meeting in compliance with the requisition[105]. This is because it is felt that the difficulties and expense to which the requisitionists are put may make the remedy illusory. However, no court has yet issued such an order and *obiter dicta* from an earlier day suggests that the statutory provision does exclude such a remedy[106].

In the United States, even where statutory requisition rights are provided, no provision is made to enable the requisitionist to act in the event of default. It has been held, however, that under such provisions the corporate executive has no discretion: it must call the meeting, and where this is not done mandamus is available[107], and this is the only remedy that is offered or needed[108].

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104. See *Peter's American Delicacy Co* v *Heath* (1939) 61 CLR 457; Ford, *op cit*, chapter 17.
105. *Vawdon* v *South Sydney Junior Rugby League Club* No 406 of 1976 (unreported decision of Wootten J NSW Supreme Court, 29 March 1976) page 10 of transcript.
106. *South Norseman Gold Mines NL* v *Macdonald* [1937] SASR 53, 67.
107. *Auer* v *Dressel* (1954) 118 NE 2d 590 (NY Ct Civ App); *Young* v *Janas* (1954) 103 A 2d 299 (Del Ch).
108. *Young* v *Janas* (1954) 103 A 2d 299 (Del Ch); *contra Bloch* v *Gershman* (1947) 70 NYS 2d 530 (SC).

8. RIGHTS PROVIDED BY THE ARTICLES

In addition to the statutory right to requisition a meeting, company members may also derive requisition rights from the articles of association of the company. Where such rights are conferred by the articles of association, requisitionists are free to elect to proceed in either right[109]. However, doubt has been expressed in one learned text as to whether a provision in the articles allowing a requisition supported by a smaller interest than that stipulated for in the statute would be effective[110].

In *Vawdon* v *South Sydney Junior Rugby League Club*[111], the articles provided that an extraordinary general meeting "shall be called by the secretary upon receipt by him of a requisition...signed by not less than 300 members". The meeting was to be held within forty days of receipt of the requisition and default rights arose if the meeting was not called within fourteen days. Thus the right granted by the articles differed in several respects from that afforded by statute. In particular, the requirement that at least three hundred members sign the requisition should be contrasted with the statutory provision that a requisition will be effective if signed by two hundred members. If this provision was not deemed inconsistent with the statute, why would a provision in the articles allowing one hundred members to requisition a meeting be inconsistent with the statute? The explanation can only lie in the presumption that the statute intends to lay down maximum rights rather than minimum rights, and it may be argued that the use of the expression

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109. Schmitthoff, *op cit*, 469.
110. Wallace, G. and Young, J.McI., *Australian Company Law and Practice*, (Sydney, Law Book Co Ltd, 1965) 422.
111. No 406 of 1976 (unreported decision of Wooten J, NSW Supreme Court, 29 March 1976).

"not less than two hundred members" is insufficient to support such a presumption as to the rights conferred by the articles.

The purported requisition relied on by Vawdon was in the form of a petition addressed to the directors requesting that an extraordinary meeting be held to remove and replace the board. This was received by the secretary and referred to the board. It was held that this document did not constitute a requisition in the terms of the articles in that it was directed to the board rather than to the secretary. No reference was made to the possibility that the requisition might have been effective under the terms of the statute. It would seem that, in making their election as to whether to proceed under the statute or under the articles, the requisitionists were ill-advised. The fact that in the circumstances of the case Wootten J felt that no useful purpose would be served by calling such a meeting may help to explain why this obstacle proved insurmountable.

These circumstances were that the board had taken prompt action to summon an extraordinary meeting of their own to amend the articles to allow the incumbent directors to resign and approve an interim election. Even if a valid requisition had been served on the company the meeting that was held obviously did not comply with its terms and could not be regarded as having been called in compliance with it. In the tactical battle between the dissidents and entrenched management, the difference between resignation and removal and the fact that the directors were allowed to call a meeting to accept their resignations represented a tactical victory for them.

One question which did not really arise in *Vawdon's* case but which may be referred to here is the question of whether the lodging of a requisition will prevent the board of directors from calling a meeting

without reference to the requisition. A related question is whether the fact that the board has called a meeting of its own volition immediately before the requisition is lodged will rob the requisition of its effect. Logically it is submitted that the answer should depend on how the purposes envisaged by the opposing parties relate. Once a requisition is lodged, the directors are under a duty to comply with it and should be prevented from calling a separate meeting to deal with the same issue. They should not, however, be prevented from calling a meeting for another purpose or from adding to the agenda of the meeting called in compliance with the requisition certain additional items[112]. On the other hand, the board should not be able to excuse itself from complying with the requisition because it has already called a meeting, unless that meeting will make the requisition redundent. The Canada Business Corporations Act is unique in making provision to excuse the directors from the need to comply with the requisition where prescribed steps have been taken in preparation for calling a meeting[113]. However, these provisions do not, unfortunately, guard against the contingency that the business of the meeting will be different from that contemplated by the requisition. This objection could be overcome, it is submitted, by a provision to the effect that the business set out in the requisition must be attended to at the meeting for this exception to apply.

D. THE COURTS HAVE POWER TO CALL MEETINGS

The court has an inherent power to direct that a shareholder's meeting

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112. See *Re Marra Developments Ltd* [1976] 1 ACLR 470.
113. Can Bus Corp Act s 137(3).

should be held[114]. It will exercise this power where a decision by the company in general meeting is relevant to a matter before the court[115]. Some nineteenth century decisions[116] encouraged the practice of bringing actions against directors for fraud in the name of the company. When the question arose as to whether the action was barred by the rule in *Foss* v *Harbottle*[117], the courts would order a meeting to be held. However, subsequent rulings as to costs where the meeting chose not to adopt this procedure discouraged the practice[118]. The court will not exercise the power merely because the board has refused to call a meeting when asked to do so[119], although it was suggested that the power might be used where company machinery was immobilized[120].

In addition to this inherent power, certain statutory provisions have been enacted extending the court's power to convene company meetings. At one time companies legislation empowered the court to order a meeting on the application of any member when default was made in holding the annual general meeting[121]. This discretionary power[122] still exists but is exercised now by the Corporate Affairs Commission and the Board of Trade[123]. More important, however, are the provisions allowing the court to order a meeting to be called "if for any reason it is impracticable"

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114. Pennington, *op cit*, 536.
115. *Re Paris Skating Rink* (1877) 6 Ch D 731.
116. See for example *Exeter and Crediton Railway Co* v *Buller* (1847) LJ Ch 449.
117. (1843) 2 Hare 461, 67 ER 189.
118. Beck, S.M., "*The Shareholder's Derivative Action*" (1974) 52 Can Bar Rev 1159.
119. *MacDougall* v *Gardiner*((1875) LR 10 Ch App 606.
120. *MacDougall* v *Gardiner* (1875) LR 10 Ch App 606, 609.
121. Companies Act, 1928 (UK) s 112(3).
122. Paterson, W.E. and Ednie, H.H., *Australian Company Law*, (Sydney, Butterworths, 1962) section 136/13 citing *Re Thompson Graham Jewell Pty Ltd* (unreported decision of Lush J, Victorian Supreme Court, 13 August 1974) as an instance where the court exercised its discretion against calling such a meeting.
123. UCA s 136(4)(b); Companies Act, 1948 (UK) s 131(2).

to call a meeting in the normal manner. This provision, which originated from a minor amendment recommended by the Green Committee without discussion[124], is now found in virtually identical form in the Australian and Canadian as well as the British Companies Acts[125]. Again it is impossible to state clearly how frequently this principle is invoked, no search of court records being possible for this thesis. However, reference may be made to a number of reported cases where such an order was sought[126]. It is suggested that it is not necessary to prove that such a provision is frequently invoked before reaching a conclusion as to its utility inasmuch as it serves a function analogous to that of an emergency brake in an automobile. The presence of such a provision is indispensible if the power to call a meeting in the normal course of events is to be conditional. The section is designed to overcome technical difficulties in the way of holding a meeting but has also been invoked to overcome certain difficulties arising from failure of company members to co-operate. Both usages are considered below.

1. TO OVERCOME TECHNICAL DIFFICULTIES

If for any reason it is impracticable to call a meeting in the manner prescribed by the articles or the Act, the court may, of its own motion or on the application of any director or of any member who could vote at a meeting, order a meeting to be called in a manner prescribed by the court[127]. The court in making such an order has a discretion to

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124. Great Britain, Board of Trade, *Report of the Company Law Amendment Committee*, (1926) 54, hereinafter referred to as the *Greene Report*.
125. UCA s 142; Companies Act, 1948 (UK) s 135; Can Bus Corp Act s 138; Bus Corp Act (Ont) s 111.
126. *Re Noel Tedman Pty Ltd* [1967] QLR 591; *Re Beckers Pty Ltd* (1942) 59 WN (NSW) 206.
127. UCA s 142(1).

give ancillary directions and has express authority to direct that one member may constitute a meeting[128]. Further, the New South Wales Companies Act has recently been amended to provide for the purposes of the section that the personal representative of a deceased member shall be deemed to be a member of the company[129].

These provisions indicate the sort of difficulty to which the provision will be applied without controversy. In one case[130], an application was made by the executors of a married couple, the only shareholders and sole directors of two companies, after the couple had been killed in a traffic accident. The order was granted. There is express provision in the Australian Acts to allow the court to direct that one member shall constitute a quorum. The utility of such a provision is demonstrated by a Canadian case[131] where, in the absence of such a stipulation, the court held that it had no such power. The Canada Business Corporations Act[132] now contains a stipulation similar to that in the Australian Acts although the Ontario legislation does not[133].

Other difficulties which the section may overcome include difficulties in ensuring that all members receive the notice of meeting. Such problems were encountered by the Pall Mall Building Society whose records had been destroyed in the London blitz[134]. Problems of this kind may not make it logically impossible to convene and hold a meeting

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128. UCA s 142(1).
129. Companies Act, 1961 (NSW) s 142(3), new subsection added, Act No 1, 1976, s 3, sched 5 s 27.
130. *Re Noel Tedman Holdings Pty Ltd* [1967] QLR 591; see also *Re Beckers Pty Ltd* (1942) 59 WN (NSW) 206.
131. *Re Cowichan Leader Ltd* (1963) 42 DLR 2d 111.
132. Can Bus Corp Act s 138; see *Dickerson Report, op cit*, para 293.
133. Bus Corp Act (Ont) s 111.
134. *Re Pall Mall Building Society Ltd* [1947] WN 143; see also *Re Edinburgh Workmen's Houses Improvement Co Ltd* [1935] SC 56.

in the manner prescribed but the term used by the section is "impracticable". The test of the section's applicability is whether in the circumstances of a particular case a meeting may, as a practical matter, be called and held[135].

2. IN CONFLICT SITUATIONS

The argument that an order under this section could not be made where the application was opposed was advanced in *Omega Estates Pty Ltd* v *Ganke*[136]. The applicant in that case, who held nine-tenths of the shares in a three man company, sought to exercise his statutory power to remove the directors, the other two shareholders. He was prevented from doing so by the refusal of the respondents to call an annual general meeting. The argument was rejected and the order was granted, but questions still arise as to the circumstances in which an order will be granted in the face of opposition.

In the course of his judgment in that case, Else-Mitchell J held that the section could not be resorted to simply as a matter of convenience or on the excuse of manufactured difficulties: the section "does not authorize the court to over-rule the articles of association"[137]. The meaning of this last observation is unclear. However, it is suggested that the court will not set the articles aside merely because they prove inconvenient and will, in making an order, observe their provisions as nearly as possible[138].

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135. *Re El Sombrero Ltd* [1958] 1 Ch 900.
136. (1963) 80 WN (NSW) 1218.
137. (1963) 80 WN (NSW) 1218, 1223; see discussion above, 137.
138. See for example *Re Pall Mall Building Society Ltd* [1947] WN 143; *Re Morris Funeral Services Ltd* [1957] OWN 161.

Light is cast on the question of the use of the section in a situation where the application is opposed by several Canadian cases. In the first of these, *Re Morris Funeral Services Ltd*[139], the applicants were members of a small private company and held the majority of the share shares therein when shares held in a joint trust were discounted. In the circumstances which arose of a dispute among the company members, the trust shares were irrelevant because they could not be voted unless there was unanimity among the trustees, and this unanimity was lacking. The applicants desired to replace the managing director and sought an order which would reduce the necessary quorum for a general meeting, so that the trust shares, representing more than half the equity in the company, need not be represented at the meeting. The order, granted in the first instance, was set aside on appeal. It was held that the alleged difficulty, the fact that the trustees disagreed, was an artificial one created in large part by the applicants. It was further held that the section may not successfully be invoked in order to place one of two or more contending factions in control of the company[140].

The second case, *Re Routley's Holdings Ltd*[141], also concerned a small company. No annual general meeting had been held for five years. The applicants' first resort was to internal procedures. A meeting was called, but the company's officers, minority shareholders, refused to allow the applicants' proxies to attend. This was characterized by Landreville J as "an act of utter disregard of the interests of those who issued the proxies and a clear attempt to force minority rule on the majority". He held that the ill-will demonstrated by the officers made

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139. [1957] OWN 161.
140. [1957] OWN 161, 165.
141. [1959] OWN 89.

it impracticable to hold a genuine meeting and granted the order[142]. An appeal was brought on the ground that as one object of the application was to enable the directors to be supplanted it should have been refused. This suggestion was held to be an utter absurdity. In the course of the judgment McGillvray JA listed the grounds on which *Re Morris Funeral Services Ltd* could be distinguished. These were: first, that there was in the present case a breach of statutory duty, whereas the directors there had not failed to call an annual meeting; secondly, that the sole purpose there was to place a contending faction in control; thirdly, that the applicants there had not exhausted the other procedures open to them[143]; and finally and "perhaps the principal factor", the applicants there were seeking an advantage to which they were not entitled[144]. The applicants in *Re Routley's Holdings Ltd* may not have been legally entitled to the advantage of a court order made under the section, the power being discretionary and legal rights determined by the articles which the court was asked to set aside, but they were entitled to demand that a company meeting be held, and when the parties opposing the order refused to co-operate, the court had grounds on which to make an order despite the opposition. The applicants in *Re Routley's Holdings Ltd* had justice and equity on their side.

Not all of the factors pointed out by McGilvray JA carry equal weight or are essential when deciding whether the court may grant an order. An order will not be granted while there remains a practical possibility of some solution being found within the terms of the articles or statute.

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142. [1959] OWN 89.
143. It may be suggested *inter alia* that the trustees of the shares involved there might have sought directions from the court under the equivalent of the Trustees Act, 1925 (NSW) s 63.
144. *Re Routley's Holdings Ltd* [1960] OWN 160.

It is suggested that a breach of statutory duty is not necessary; thus an order might be made if, having heard of plans by the majority shareholder to replace them, directors called an annual general meeting but prevented it from being held by absenting themselves[145]. It is further suggested that the purpose of calling the meeting is irrelevant, save where the action contemplated is illegal or would clearly amount to oppression or a fraud on the minority. The essential factor, therefore, is whether in a situation where the applicant is entitled to refer a question to the general meeting, the parties opposing the order seek to take advantage of the fact that it is impracticable to hold the meeting in the normal manner or to ensure that such a meeting will be ineffective. In these circumstances it is fair and just for the court to make an order under the section despite the opposition. The essential element in *Re Routley's Holdings Ltd* was the attempt to force minority rule on the majority shareholders, just as the essential fact about *Re Morris Funeral Services Ltd* was that the applicants had not been deprived of any of their rights as shareholders[146].

In *Re Routley's Holdings Ltd* the court granted an order in circumstances where a meeting conducted as the parties opposing the order would have had it would have deprived the applicants of their right to proxy representation. If the court will exercise the power to make an order under this section whenever without such an order a meeting will be conducted so as to deprive the applicants of their rights as shareholders, then, in principle, minority shareholders should also be able to obtain an order. The applicant in *Re Routley's Holdings Ltd* was a majority shareholder and there is no reported case in which a minority shareholder has

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145. Getz, L., "*Court-Ordered Company Meetings*" (1969) 33 Conv (NS) 399, 404.
146. *Ibid*, 405, 404.

sought such an order, but Getz is of the view that the court would not refuse an order on this ground and therefore suggests that the section may "represent a significant weapon in the armoury available to shareholders to secure accountability for managerial conduct"[147], but this potential has yet to be realized.

3. STATUTORY POWER TO ORDER A MEETING IN OTHER CIRCUMSTANCES

Before leaving the topic of court-ordered meetings, a provision found uniquely in the new Ontario legislation should be noted. It gives the court power to order a meeting upon the application of a shareholder if it is satisfied that the purpose of the meeting is connected with the affairs of the corporation and not inconsistent with the act, and that the application is made in good faith and is *prima facie* in the interests of the corporation or its shareholders[148]. The applicant may be required to give security for costs, a stipulation that has been called unfair and unnecessary[149]. In the light of the fact that the court must be satisfied that the order is in the interests of the company, this requirement might well be abolished. Although no case has yet been reported in which this provision was invoked, its adoption in Australia is recommended on the basis that it circumvents the restriction on the court's inherent power to order a meeting.

There are no American provisions comparable with those discussed above enabling the court to order a company meeting to be held where the

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147. Getz, *op cit*, 406.
148. Bus Corp Act (Ont) s 110; see *Lawrence Report*, *op cit*, para 8.4.3.
149. Getz, *op cit*, 408.

normal procedures break down. Furthermore, this lack has not been deemed worthy of comment there. It is suggested that the reason is that it has never been doubted that a court could, and would, using its inherent powers, order a meeting to be held and compel the corporate officers to take any relevant action when the necessity arose[150].

E. THE AUTHORITY TO CANCEL OR POSTPONE A MEETING

Can a meeting once validly convened be cancelled or postponed before it meets? Who has the necessary power or authority? A meeting may, by a resolution passed by an ordinary majority, adjourn either indefinitely or to a specified time whether or not it has considered the business for which it was convened, but the decision to adjourn is made by those who attend the meeting. A decision to cancel or postpone a meeting may prevent those who would command a majority at the meeting from prevailing in a corporate dispute. It is necessary to limit such a power in the interests of controlling managerial autocracy.

1. THE AUSTRALIAN POSITION

There is no relevant statutory provision and little relevant Australian or British case law. It is, however, clear that a court may enjoin the holding of a meeting on the basis that the meeting was invalidly convened[151] or that it threatens to trespass on the legal rights of the

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150. 19 Am Jur 2d Corporations ss 707, 710 and 712; see also *Auer* v *Dressel* (1954) 118 NE 2d 590 (NY Ct Civ App).

151. See for example *Liego* v *Berner* [1976] 1 NSWLR 502, where such an order was sought but not granted because the case was not made out.

person who seeks the injunction[152]. The court has the power to cancel meetings or to postpone them until these issues have been resolved. This fact, however, does not threaten the autonomy of the general meeting.

The autonomy of the general meeting would, however, be threatened if the convening authority had the power to postpone or cancel it after the meeting has been called and before it has met. There is an English case[153] holding such purported cancellation ineffective. The judge held that before such a cancellation would be effective, express authority must be found in the articles. The convening authority did not derive such authority from the mere fact that it could fix the time and place for the meeting in the first place. The facts of the case showed that the convening authority had only become aware of the strength of the opposition after calling the meeting. The decision had the effect of enabling the opposition to remove from office the directors who had called the meeting.

There does not appear to be any other reported case from the British, Australian or Canadian jurisdictions in which the question was considered. It therefore appears that the board of directors will be unable, under the Table A articles, to cancel or postpone a meeting once validly called whether they themselves have called it or *a fortiori* if such a meeting has been called by requisitionists or by an individual under power entrusted to him.

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152. See for example *Cannon* v *Trask* (1875) LR 20 Eq 699.
153. *Smith* v *Paringa Mines Ltd* [1906] 2 Ch 193.

2. THE POSITION IN THE UNITED STATES OF AMERICA

As the fixed meeting is common, American concern with the problems of cancelling or postponing meetings is more active than that in Australia. A fixed meeting is one which takes place regularly at a date and sometimes at a place and time fixed by the corporation's charter or by laws. The fact that the corporation's constitutive documents fix a meeting makes several differences to the law governing meetings, especially as it affects the principle of notice[154]. The principal advantage is that management cannot avoid holding the meeting and cannot time it to take advantage of propitious circumstances. The principal drawback is the lack of flexibility: there will be circumstances in which it will be necessary to cancel or postpone the fixed meeting.

Several American states have laws which govern procedures for changing the fixed date or for changing the date of a specific meeting,where this becomes necessary or desirable[155]. The basic principle would seem to be that, as changing the date of the meeting alters the term of office of the incumbents, they will not be allowed to make such a change, more especially when the meeting is postponed so as to extend their term. Thus it has been held that even though the directors have general power to alter the by-laws, the decision in this one case must

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154. See below, 280.

155. *Gries* v *Eversharp Inc* (1949) 69 A 2d 922 (Del SC); *In re Tonopah United Water Co* (1927) 139 A 762 (Del Ch); and see also Kerr, J.H. and Wolf, H., "*Shareholders' Meetings under the Texas Business Corporations Act*" (1964-65) 43 Tex LR 713, 714-717.

be left to the shareholders[156]. It has also been argued that the shareholders should be protected from the "additional tactical advantage which incumbent managements might gain in proxy wars by manipulation of the meeting date"[157]. The statutory provisions limiting proxies to a period of eleven months are but one factor that may induce management to try for an advantage by moving the date of the meeting forward. However, in the only case so far reported in which this tactic was employed, the court held that such action was valid[158]. It is suggested, with respect, that the result achieved by the dissenting judgment in the case is preferable. It seems inequitable that the stratagem of precipitately advancing the annual meeting so as to fend off an anticipated proxy contest and to enable the officers responsible to retain office for an additional sixteen months should succeed.

Two recent American cases have involved attempts to postpone or cancel meetings where no set date has been fixed for the corporation's annual meeting. In one of these cases[159], the directors were empowered to pass a by-law setting such a date but had not done so. They called a meeting designated the annual general meeting for a specific date but five days before it was to be held they purported to postpone it indefinitely. The plaintiffs, shareholders representing an opposing faction, took the position that there was no authority to cancel the meeting. Despite the boycott by the defendant directors, two-thirds of the voting stock was represented at the meeting. It was held that the meeting was valid on

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156. *Penn-Texas Corp* v *Niles-Bement-Pond Co* (1955) 112 A 2d 302 (NJ SC).
157. Note, (1950) 63 Harv L Rev 701.
158. *Mansdorf* v *Unexcelled Inc* (1967) 281 NYS 2d 173 (SC).
159. *Silverman* v *Gibert* (1966) 185 So 373 (La Ct App).

the basis that the power to fix the time and place of the annual meeting cannot be construed as a power in the incumbent board to extend its term and office indefinitely.

The other case[160] concerned an attempt to cancel a special meeting properly called by the president of the company who was subsequently removed and replaced by the board. Both the board and the new appointee purported to cancel the special meeting. A declaration was sought that this action had been effective. The order sought was granted but an appeal was allowed on the basis that the by-law expressly granted the power to the president and as there was no provision for cancellation by the board their attempt was ineffective. The Appeal Court declined to decide whether the call could be cancelled by the individual who issued it but held that the board could not be allowed to achieve indirectly what it could not do directly. It declined to read a limitation into the by-law as it could be in the stockholders' interests to have such disputes presented to them. It is suggested that this authority would be accepted as persuasive should any similar question arise under article 44 of Table A in New South Wales, which, as stated above[161], authorizes individual directors to call extraordinary general meetings.

In conclusion, it may be said that the provisions for convocation of general meetings found in the Australian Companies Acts and the attached articles are generally satisfactory, and will function to prevent company management from retaining power by refusing to convene a general meeting.

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160. *Republic Corp* v *Carter* (1964) 253 NYS 2d 280 (SC).
161. See above, 130–131.

PART V THE GENERAL MEETING: NOTICE REQUIREMENTS

The statutory provisions relating to notice of shareholders' meetings embody and make more specific a rule of the common law applicable to corporations. Common law requirements as to notice varied according to whether the meeting involved was a meeting of the general body or of a select committee. When the requirements stipulated by the judges in one such case[1] are summarized, the rule may be stated in these terms: when corporate acts are to be done on a day not fixed by the charter, every member of the company must be summoned to that meeting by a notice given a reasonable time before the meeting and stating that a general meeting will be held on a specified date to transact specified business.

Judges in the eighteenth century applied the rule with very little comment on the reasoning or policy supporting it[2]. The one exception was not really decided on this point at all. In *Musgrave* v *Nevison*[3], the question was whether the jury's verdict could be set aside. The facts of the case were that when the mayor, the aldermen, and the councilmen of a municipal corporation had met informally, a resignation was announced and it was suggested that their host be elected then and there. Despite objections, the body corporate proceeded thereafter on the presumption that he had been duly elected. The court was of the opinion

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1. *R* v *Hill* (1825) 4 B & C 426, 107 ER 1118; see also *R* v *Shrewsbury* (1736) Lee temp Hard 147, 95 ER 94.
2. See *R* v *Liverpool Corporation* 2 Bur 723, 97 ER 533; *R* v *Doncaster Corporation* 2 Bur 728, 97 ER 541; *R* v *May*, *R* v *Little* 5 Bur 268, 98 ER 408; *R* v *Exeter Corporation* Show 258, 89 ER 558, 642; *R* v *Strangways* Hil 1 Geo I is the earliest authority cited.
3. (1724) 2 Ld Raymond 1558, 92 ER 384.

that the election was obtained by "surprize" and was consequently void. Although one councilman was absent, and this was considered by the court to be significant, it appears that his presence alone would not have been sufficient to validate the election. This inference is drawn from the fact that the court held that: "In cases of accidental election every member who had a right to vote ought to be present and assent". The appeal court held that as the jury's verdict was perverse it could be set aside, but in the result a settlement was arrived at.

Although the justice and wisdom of the opinion of the court of the first instance cannot be disputed, it may be asked in whose interest a ruling to this effect would be made. In that instance the ruling would have served the interest of the absent member, the dissenting minority and also those of the majority who in the circumstances might not have had time for sober reflection, but this will not be true in every case.

A case which took up and developed this point was that of *R* v *Theodorick*[4]. There, a general meeting duly summoned had assembled to accept a resignation. The select committee whose task it was elected a replacement on the same day without waiting for a special summons to be issued. The election was held valid on the basis that, as the charter did not stipulate that a special summons must be issued, a previous summons was only necessary for the purpose of preventing an election from taking place by surprise, that is, "by some of the electors without due means of attendance upon the occasion being equally afforded to all the others". The court further held that "due and equal means of attendance cannot be said to have been wanting, for any effective purpose, when

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4. (1807) 8 East 543, 103 ER 451.

all the electors have been actually present and have without objection on the part of any one of them, consented to proceed and have in fact proceeded to an election and have unanimously concurred in the object of such an election"[5]. The inclusion of the word "equal" in this statement may be significant. It might be possible to argue that someone who comes to a meeting unprepared does not have "equal means of attendance" with someone who has advance knowledge that certain business will arise.

One of the points which will be argued in this section of the thesis is that notice requirements should perform the function, at least in cases where unanimity is lacking, of ensuring that decisions can be considered at leisure[6]. However, the only judicial reference to such a concept that has been found was an observation in a Canadian case to the effect that the requirement of notice is not intended "to impose a time for reflection upon the unanimous decisions of the shareholders before effect can be given to such a decision", but is, rather, intended to afford every shareholder an opportunity to express his individual opinion[7].

It is suggested that unanimity may demonstrate that the decision is such a foregone conclusion that time for consideration is unnecessary[8].

The role that notice requirements play in protecting the right of the minority was recently pointed out in the judgment of Mahoney J in *Taylor* v *MacNamara*[9]. He held that:

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5. *R* v *Theodorick* (1807) 8 East 543, 103 ER 451, 452.
6. See *Nelson* v *Hubbard* (1892) 11 So 428 (Sup Ct, Ala).
7. *Re Excel Footwear Co* (1923) 3 DLR 213 per Mellish J at 214.
8. For further discussion see below, 312.
9. [1974] 1 NSWLR 165.

> The protection of personal rights is often achieved in the law, in whole or in part, by the requirement that an open and formal procedure be followed. It may be said that the relevant protection lies in the interstices of the procedure prescribed. The specification of a procedure for such a purpose subjects the steps taken to affect personal rights to the possibility of careful and subsequent scrutiny; and, in addition, by subjecting those who have the power to affect personal rights to the fulfilment of matters of procedure, the attention of those persons is more carefully directed to the precise nature of what they are doing."*10*

This approach is closely related to that taken to the natural justice requirement in administrative law: the common concept is that justice lies in the process*11*. Without such a viewpoint, an insistence on observing the formalities often becomes an empty gesture for which regret must be expressed*12*.

Notice requirements do protect the absent, and this function is often emphasised to the exclusion of any other*13*. Such an emphasis is particularly noticeable where partnership principles apply because the general rule here is that the parties are strictly bound by the terms of their original agreement and are liable for losses sustained by the partnership to the full extent of their property. Where, as in the deed of settlement associations, "partnership" agreements provided for a general meeting and majority rule, the absent partner's sole protection was that he knew by way of the notice what action was proposed. Because he had this knowledge he was presumed to consent to action being taken within the terms of the notice*14*.

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10. *Taylor* v *McNamara* [1974] 1 NSWLR 165, 172.
11. De Smith, S.A., *Judicial Review of Administrative Action*, 2nd ed (London, Stevens & Sons Ltd, 1968) 22-23.
12. See *Re North of Scotland and Shetland Steam Navigation Co Ltd* [1920] SC 94; *Jamieson* v *Trustees of the Hotel Renfrew Ltd* [1941] 4 DLR 470.
13. See *Benbow* v *Cook* (1894) 20 SE 453 (Sup Ct N Ca); *Doernbecher* v *Columbia City Lumber Co* (1892) 28 P 899 (Sup Ct Ore).
14. *Re the Vale of Neath and South Wales Brewery Joint Stock Company, ex parte Lawes* (1852) 1 De G M & G 42, 21 LJ Ch 688, 690.

American judgments more frequently discuss the policy basis of the common law rule requiring notice to be given, a rule which applies in the United States as well as in Australia, Britain and Canada. Thus there is American authority for the proposition that the notice requirement is intended strictly for the benefit of members of the corporate body and not for the benefit of the public generally or of those dealing with the corporation[15]. Notice requirements could, without such a ruling, be invoked in appropriate circumstances by anyone at all who wished to prevent the company taking a particular action. A supplier could try by invoking the notice requirements to prove that the board who had decided to terminate his contract had been improperly elected and was incapable of conducting the company's business for that reason. There is clearly no argument that would support such a result but there could be an argument for allowing members of the public or employees of the company the benefit of the notice requirement so that they might make representations on various proposals being considered by the company which will affect the community. However, there are grave philosophical problems in establishing that the company should have an obligation to receive such representations and any common law court would agree that notice requirements are intended strictly for the benefit of members of the body in question.

Perhaps the best statement of the rationale underlying the notice requirement is that found in *Hill* v *Atlantic and North Carolina Railroad Co*[16], where it was held that it was essential to the validity of acts

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15. *Nelson* v *Hubbard* (1892) 11 So 428 (Sup Ct Ala).
16. (1906) 55 SE 854 (Sup Ct N Ca).

done for the corporation by the body of stockholders that they should be assembled in their representative capacity, that is, with the intention of acting as a body in the name of the corporation. "The rule of law", it was further held, "is in accordance with a plain dictate of reason and justice. The corporation is entitled to the opinion and judgment of each of its members...upon any and all measures taken in the transaction of its business affairs and for the same reason is each stockholder whose interests may be vitally affected, entitled to be present and to a reasonable hearing and especially where anything is to be done likely to prejudice or impair his rights"[17]. The right to notice was there equated to the right to a fair judicial hearing.

Notice, in summary, is essential to the assembling of the shareholders in a deliberative body because all parties, the corporation and each individual member whether he belongs to the minority or the majority, are entitled to a decision as truly representative of the will of the majority as possible. Accordingly, each individual must have an opportunity to be present and may insist on his right to due warning giving a right to attend and to muster opposition where there is no general agreement. The remaining sections of this part of the thesis will canvass the intricacies of the law relating to notice with a view to determining whether it satisfactorily fulfils these functions.

A. PERSONS ENTITLED TO NOTICE

The Australian Uniform Companies Act requires a company to give notice

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17. *Hill* v *Atlantic and North Carolina Railroad Co* (1906) 55 SE 854 (Sup Ct N Ca).

of every general meeting to all members who have a right to attend and vote at general meetings unless the articles provide otherwise[18]. Inasmuch as the articles may otherwise provide, this requirement is directory, not mandatory, that is, it may be displaced and no statutory cause of action will arise. Company auditors, unlike shareholders, do have a statutory right to receive all notices of, and other communications relating to, any general meeting regardless of whether or not they will retire or be removed at that meeting[19]. The Stock Exchange Listing Requirements are also relevant. However, these were amended as of 1 July 1979 with a view to removing listing requirements duplicated by law or in the Listing Manual. There are now no Listing Requirements requiring listed companies to have articles of association on specified matters[20]. The former provisions have been replaced by a general requirement that the memorandum and articles contain provisions consistent with the Listing Requirements[21]. The relevant sections in the new Listing Requirements oblige the company to give notice of meeting to the Stock Exchange[22] and to preference shareholders[23]. These are the provisions under which an Australian company will be required to give notice of a general meeting.

The British provisions[24] parallel the Australian with the distinction that it is provided that notice of general meeting shall, unless otherwise provided, be given to every member of the company[25].

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18. UCA s 138(4).
19. UCA s 167(7).
20. See Introductory Note to Associated Australian Stock Exchange Listing Requirements signed by M. Kinsky and dated 1 July 1979.
21. Associated Australian Stock Exchange Listing Requirement s 1.1
22. Associated Australian Stock Exchange Listing Requirement 348, formerly 1 B 17, 3 A 15, 3 H 17.
23. Associated Australian Stock Exchange Listing Requirement 3.J.17.
24. Companies Act, 1948 (UK) s 134(a); Companies Act, 1967 (UK) s 14(7).
25. Companies Act, 1948 (UK) s 134(a).

The Canada Business Corporations Act contains provisions as to notice which are remarkably clear while, on the other hand, the Ontario legislation is very turgid. The federal legislation sets out in one mandatory provision that notice of the time and place of general meetings shall be sent to each shareholder entitled to vote, to each director and to the auditor[26]. Further provisions are made to deal with the situation where shares have been transferred but the transfer has not yet been registered[27], but there is no provision for notice to voteless shareholders. The provincial legislation in question provides that unless otherwise provided, notice shall be given to every person "who is entitled to notice of meetings and who appears on the records as a shareholder"[28]. It is not clear what the relationship between the two clauses is inteneed to be. Lavine states that the section "now makes it clear" that notice need only be given to persons who appear on the records as shareholders[29]. If this was the intention, it is submitted that it could have been more happily achieved. Provisions for the auditor's right to receive notice are contained in a different section[30]. The American Model Business Corporations Act provides that notice shall be given "to each shareholder of record entitled to vote at such meeting"[31]. The commentary to the section states that the longstanding rule is that notice be given to each person entitled to be present at a corporate meeting[32]. No heed is paid to the fact that the two phrases might encompass different groups despite the fact that provision is made

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26. Can Bus Corp Act s 129(1).
27. Can Bus Corp Act s 129(2).
28. Bus Corp Act (Ont) s 106(1)(a).
29. Lavine, S., *The Business Corporations Act: An Analysis*, (Toronto, Carswell Co, 1971) 198.
30. Bus Corp Act (Ont) s 171(12).
31. Mod Bus Corp Act Ann 2d s 29.
32. Mod Bus Corp Act Ann 2d s 29.02.

permitting companies to issue shares without voting rights[33].

1. ENFRANCHISED SHAREOWNERS OF RECORD

In all jurisdictions, enfranchised shareowners of record, that is, shareowners whose names appear in the register and whose shares carry voting rights are, *vis a vis* the company, entitled to attend meetings and to vote and are therefore entitled to notice whether or not they are beneficially interested in the shares in question[34]. There are statutory references to this right but its basis is usually to be found in the common law. Where the statutory provisions are directory only and not mandatory, there is nothing to displace the common law rule. In line with this contention it is suggested that Australian companies may extend but cannot further restrict the right to notice. Not only would any attempt at such restriction violate the common law rule, it would also violate a term which it is suggested must necessarily be implied into the contract by which the shareholder takes his shares. An express term of the contract is that the share shall carry voting rights; without an implied term to the effect that he will be given notice of meeting the right to vote might be rendered worthless.

An exception to this rule appears from case law. Where the member resides abroad or out of reach, the company is excused its obligation. The scope of this exception whose rationale is to avoid inconvenience to the company[35] is unclear, and it is suggested that the justification for

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33. Mod Bus Corp Act Ann 2d s 15.
34. See *Re Saunders Ltd* (1937) 49 WN (NSW) 220.
35. *Re Union Hill Silver Co* (1870) 22 LT 400; *Re Vale of Clywdd Coal Mining Co Ltd* (1912) 29 WN (NSW) 129.

it is much less apparent in today's world than it once was.

In the very early municipal corporations the corporation would be excused from giving notice of meeting to anyone who resided out of the borough. Residing out of the borough was grounds for withdrawal of membership, but before this could be done personal notice would have to be given to the member against whom the action was directed, regardless of residence outside the borough.

In one such case the proposal was to remove and replace W who held a certain office for life. W had fled from Britain to escape a criminal charge. It was held that the general proposition that notice was necessary in such cases must be understood as applying to cases where the party is within reach of the summons; "it cannot be necessary to send all over the globe to search for a man who has fled the country"[36].

In 1870 the rule was applied to joint stock companies in a decision[37] to the effect that anyone who could be reached by "ordinary English post" was within reach of notice but that persons residing abroad need not be served with notice. In the absence of specific provisions in the articles, this authority has been followed by almost all of the later cases without modification in the light of modern improvements in communications[38]. In the last reported case on the subject it was held that despite modern methods of communication this authority would be followed in the interests of commercial certainty[39].

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36. *R* v *Harris* (1831) 1 B & Ad 936, 109 ER 1034.
37. *Re Union Hill Silver Co* (1870) 22 LT 400.
38. *Re Vale of Clywdd Coal Mining Co Ltd* (1912) 29 WN (NSW) 129; *Re Newcastle United Football Club Co* [1932] WN 109; but see *Re Jenner Institute of Preventative Medicine* (1899) 15 TLR 399.
39. *Re Warden and Hotchkiss Ltd* [1945] Ch 270.

It has been held that persons living in other states of Australia must be served with notice of meetings held within Australia[40]. However, the Table A regulations excuse the company from giving notice when the registered address is outside the state and no address for service within the state has been given[41]. In the light of this article, the Stock Exchange Listing Requirement that documents be sent by airmail when addressed to members abroad[42] is of no relevance to notices of meeting[43].

2. NON-FRANCHISED SHAREHOLDERS OF RECORD

A shareholder whose name appears in the register but whose share does not confer voting rights or, as in the case of deferred preference shares, confers voting rights only when the dividends are in arrears, may or may not be entitled to receive notice of meeting. His entitlement will depend, in the first place, upon the relevant articles of association, but in this area there is a significant difference between the Australian and the British legislation as was pointed out above.

If the British statutory provisions apply, non-franchised shareholders of record will be entitled to receive notices of meeting. This does not mean, however, that they will necessarily be summoned to attend the meeting[44]. Such shareholders will receive a notice telling them that a meeting is to be held on the date in question to which certain proposals will

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40. *Re Merchants & Shippers Steamship Lines* (1917) 17 SR (NSW) 146.
41. UCA Fourth sched Table A reg 111(a).
42. Associated Australian Stock Exchange Listing Requirements 3.H.9.
43. See above, 271.
44. *Re Mackenzie* [1916] 2 Ch 450 as cited by Pennington, R.R., *Company Law*, 3rd ed (London, Butterworths, 1973) 538.

be submitted. The company, however, has no obligation to summon them to the meeting and is free to exclude them. Nevertheless, non-franchised shareholders are put in a better position to make representations to the company and, later, to find out quickly what decisions have been taken than if they were not put on notice.

Because the British provision is merely directory, a company could provide in its articles that notice need only be given to voting or enfranchised shareowners. For this reason the Jenkins Committee, noting that voting members have no need of a statutory right to notice in the light of the common law, recommended that a statutory right be given to non-franchised members of the company[45].

It is submitted that all members of the company, whether they have the right to vote or not, should be advised of decisions which are of sufficient gravity that it is proposed to make them in general meeting. Australian legislation should, at least, encourage this desirable practice by directing, as does the British legislation, that unless otherwise provided all members should be entitled to notice of meeting. In so far as listed companies are concerned, however, it may be noted that the failure of the legislation to make such a provision is remedied by the section of the Listing Requirements which requires that preference shareholders be given the same rights as ordinary shareholders to receive notices, reports and audited accounts and attend general meetings of the company[46].

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45. Great Britain, Board of Trade, *Report of the Company Law Committee* (1962) para 138, hereinafter referred to as the *Jenkins Report*.
46. Australian Associated Stock Exchange Listing Requirement 3.J. 17.

Adoption of the Jenkins Committee recommendations[47] would, however, be preferable. The only argument that could be advanced against the recommendation would be that it might lead to the invalidation of more meetings, improving the position of voteless members in a minor way at what could be vast expense to the company. Such an argument cannot stand in the light of the provision in the Uniform Companies Act that any defect, irregularity or deficiency of notice shall not invalidate any proceeding under the Act unless the court is of opinion that substantial injustice has been or may be caused thereby which cannot be remedied by any order of the court[48].

3. PERSONS BENEFICIALLY ENTITLED TO SHARES AND OTHERS

Persons who are only beneficially entitled to shares are not entitled to receive notice of meeting from the company under the companies legislation in force in Australia, Britain and Canada. This is also true of the United States so far as the provisions of the state corporations legislation are concerned. However, because of the prevalence of the practice of having a stockbroker hold the stock purchased for clients under his street-name, that is, as a nominee, those involved with the administration of the Securities Exchange Act 1934[49] have manifested concern for the effect of this practice on communication between the shareholder and the company. In 1975, Congress required the Securities Exchange Commission to investigate and report on the ramifications of

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47. *Jenkins Report, op cit,* para 138.
48. UCA s 366(1).
49. Aranow, E.R. and Einhorn, H.A., *Proxy Contests for Corporate Control,* 2nd ed (New York, Columbia University Press, 1968) 243, 247.

the practice for such communications[50]. Subsequently, new provisions have been adopted to facilitate transmission of proxy materials to beneficial shareholders through intermediaries holding in street or nominee name. Proxy rule 14a-3(d) requires an issuer to inquire of intermediaries prior to the meeting with respect to which it intends to solicit proxies whether the record holder represents others who are beneficial owners of the securities and to supply to those intermediaries sufficient copies of the proxy material to forward to his principals. Section 14b-1 imposes on broker-dealers acting as record holders the duty to forward the materials "promptly"[51].

Company officers are not, as such, entitled to notice of general meeting under the Australian Table A articles. Directors are under the articles obliged to hold shares[52] and as shareholders will receive notice of meeting, but where this article is excluded and the directors are not shareholders, they would not without special provision be entitled to such notice[53]. It is therefore suggested that provisions similar to those in the Canada Business Corporations Act[54] might appropriately be included in the body of the Australian Act.

B. CONTENTS OF THE NOTICE

The contents of notices of meeting are prescribed by the articles of

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50. CCH Securities Law Reporter para 23,391.
51. Castruccio, L.M. and Hentrich, J.J. "*Developments in Federal Securities Regulation - 1977*" (1973) 33 Bus Law 1645, 1692 citing Exchange Release No 13719 (5 July 1977).
52. UCA Fourth sched Table A reg 71.
53. See for American authority *Texlite Inc* v *H.H. Wineburg* (1963) 373 SW 2d 325 (Ct Civ App Tex).
54. Can Bus Corp Act s 129(1); and see above, 271.

association in Australia[55], but these provisions will reflect the requirements of the common law. In other jurisdictions these requirements are embodied in statute[56]. To enable the members of the company to attend the meeting, the notice must state the time and place of the meeting. To enable members to decide whether or not to attend the meeting, the notice must state what the business of the meeting will be. Each of these requirements is discussed below.

1. TIME AND PLACE OF MEETING

Regulation 45 of the Australian Table A articles stipulates that the notice must specify the place, day and hour of the meeting. The British regulations are to the same effect[57] but the provisions embodied in the Canadian federal legislation and the Ontario legislation merely stipulate that "time and place" shall be stated in the notice[58]. The American Model Business Corporations Act requires a notice to state the place, day and hour of the meeting[59]. There appears to be no practical difference among these varied provisions inasmuch as time will be interpreted to mean day and hour[60].

It was noted in the section of this thesis dealing with the convocation of meetings[61] that the older practice of having the date and place of meetings fixed by the charter or by-laws is still sometimes followed, especially in North America. Where this practice is not followed, those

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55. UCA Fourth sched Table A reg 45.
56. For example Can Bus Corp Act s 129(1); Bus Corp Act (Ont) s 106(1)(a).
57. Companies Act, 1948 (UK) First sched Table A reg 50.
58. Companies Act, 1948 (UK) First sched Table A reg 50.
59. Mod Bus Corp Act Ann 2d s 29.
60. Getz, L., "The Structure of Shareholder Democracy" in Zeigel, J.S., *Studies in Canadian Company Law*, (Toronto, Butterworth, 1967) 262.
61. See above, 228-229.

responsible for convening the meeting will have the power to determine where and when it will be held.

Where the charter or by-laws do fix a date for the meeting, the provision in the charter or by-laws which all members are deemed to know may constitute sufficient notice of the date of the meeting. However, unless the place and hour of the meeting are similarly stipulated, this notice will be insufficient to allow members to attend the meeting and written notice will still be required[62]. Written notice was even held to be necessary in one case where the charter designated the date and place of the meeting and the hour had been customary for twenty years. The charter stipulated that written notice should be given and the meeting was held invalid[63].

Even where the date, time and place of meeting are fixed by the charter, by-laws or articles, formal notice of meeting may still be required by the terms of these documents. Where formal notice is required, an informal reminder will not be sufficient. This was held in a case in which a meeting was adjourned to allow a poll to be taken, the time and place of resumption were specified in the motion for adjournment but the articles stipulated that notice must be given where an adjournment was for a period longer than ten days. The document that the company sent to its members purported to be a "reminder", not a notice, and it was held that the subsequent action was invalid[64].

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62. *Charter Gas Engine Co* v *Charter* (1892) 47 Ill App 36; *San Buenaventura Commercial Mining & Manufacturing Co* v *Vassault* (1875) 50 Cal 534.
63. *People ex rel Carus* v *Matthiessen* (1915) 109 NE 1056 (Ill SC); see also *Grant* v *Hartman Ranch Co* (1961) 14 Cal Rpt 531 (Dist Ct App).
64. *Robert Batcheller & Sons Ltd* v *Batcheller* [1945] Ch 169.

Although it is agreed that general meetings should be held at times and places convenient to the shareholders as a whole, a statutory provision to this effect has been judged inappropriate as being difficult to draft and to enforce[65]. One difficulty would appear to lie in defining what is meant by "the shareholders as a whole", the inconvenience of one shareholder cannot be regarded as determinative in the case of a company with hundreds of stockholders, but it could be determinative in a smaller company. Another difficulty would arise in ascertaining what the convenience of the larger number of the shareholders was and in proving that the directors had disregarded it.

Where an abuse can be substantiated, the courts will readily grant relief under the doctrine that the directors' powers must be exercised *bona fide* in the interests of the company as a whole. The difficulty will lie in substantiating the claim that the decision in question was such an abuse. This difficulty was overcome in two cases where, because of the provisions in the articles governing voting rights of newly transferred shares, the date fixed would mean that a large number of shareholders would not be able to vote their shares.[66]. In these cases the court prevented the meeting from being held until the holders of those newly transferred shares would be entitled to vote. In another case where the general meeting had habitually been held in London, the plaintiff sought unsuccessfully to prevent the directors from changing the place of the meeting to Liverpool, arguing that meeting in London suited the convenience of the majority of shareholders[67]. One question which has caused

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65. Great Britain, Board of Trade, *Report of the Committee on Company Law Amendment*, (1945) para 127, hereinafter referred to as the *Cohen Report*, see also Getz, *op cit*, 243.
66. *Cannon* v *Trask* (1875) LR 20 Eq 669; *Adams* v *Adhesives Proprietary I* (1932) 32 SR (NSW) 398.
67. *Martin* v *Walker* (1918) 145 LTJ 377.

some concern in the United States but which does not seem to have arisen in Australia[68] is whether a company must hold its meetings within the state. However, all but three American states have now enacted provisions allowing meetings to be held within or without the state[69]. Further, as the practice urged by Gilbert[70] and his cohorts of changing the meeting place from year to year has become common, the Model Business Corporations Act was amended in 1969 to permit the place to be selected in the manner specified in the by-laws[71]. It had previously required the charter or by-laws to specify the place of meeting. This Model Act does not, of course, bind anyone but it is representative of the climate of legal opinion as to the provisions which will best suit the commercial world.

As long as sufficient information is given in the notice to enable a shareholder to be present at a meeting, some slight uncertainty as to the hour at which the meeting will start will not invalidate the notice, but some indication should be given. Thus, where several different meetings were called to be held consecutively, the notice was not invalidated because the extension of one of them might have delayed the start of another[72].

2. PURPOSE OF THE MEETING

Under the Table A articles to the Australian Companies Acts and subject

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68. Under UCA s 344(a) and (b) a foreign company shall not be regarded as carrying on business within the state because it holds meetings there.

69. Mod Bus Corp Act Ann 2d s 29.03; see also Can Bus Corp Act s 126 and Bus Corp Act (Ont) s 105.

70. Gilbert, L.D., *Dividends and Democracy*, (Larchmont, New York, American Research Council, 1956) 205.

71. Mod Bus Corp Act Ann 2d s 29.02.

72. *Carruth* v *Imperial Chemical Industries Ltd* [1937] AC 707.

to the provisions of the Act relating to special resolutions and agreements for shorter notice, the notice of meeting is required in the case of special business to state the general nature of that business[73]. Special business is subsequently defined as being all business transacted at extraordinary general meetings and also all transacted at annual general meetings except the declaration of a dividend, the consideration of accounts and reports, the election of directors and questions of the appointment and remuneration of auditors[74]. The Canada Business Corporations Act embodies a definition of special business very similar to that found in the Australian Table A articles and stipulates that notice of a meeting at which special business is to be transacted shall state "the nature of that business in sufficient detail to permit the shareholder to form a reasoned judgment thereon" and the text of any special resolution[75]. But the Ontario provincial legislation, modelling itself more closely on the American provisions or perhaps on the common law relating to corporations, draws a clear distinction between annual and special meetings. It is stipulated there that "any shareholder shall have an opportunity to raise any matter relevant to the affairs and business of the corporation" at an annual meeting but that notice of other general meetings shall specify the general nature of the business to be transacted[76].

The Model Business Corporations Act requires the notice of a special meeting to stipulate the purpose or purposes for which the meeting is called[77] but makes no such provision in regard to the notice of an

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73. UCA Fourth sched Table A reg 45.
74. UCA Fourth sched Table A reg 46.
75. Can Bus Corp Act s 129(5) and (6).
76. Bus Corp Act (Ont) ss 107 and 108.
77. Mod Bus Corp Act Ann 2d s 29.

annual general meeting. The commentator points out that: "since the earliest days of corporate practice the annual meeting has been regarded as a forum for free expression of shareholder views whether or not sought by management". It is further stated that the Model Act "could not properly require that the notice of an annual meeting state the purposes for which the meeting is called in the sense of precluding consideration of other matters"[78]. In the light of the fact that there is case authority for the proposition that the business of an annual general meeting could validly be restricted by the by-laws of the corporation, it is unclear why such a restriction could not properly be imposed by statute.

The distinction between special and ordinary business thus drawn by the laws of all jurisdictions studied may be traced back to the common law rules applying to corporations. The rule was then that all members of the corporation were at least morally bound to be present on "charter days", that is, the day of the year nominated in the corporation's charter for the annual general meeting. The corporation was therefore empowered to exercise any or all of its powers on that day without special notice. Where the meeting was held on another day it might happen that not everyone could attend, so the notice was required to state the nature of the business that would be done to enable the members to judge whether a special effort to attend should be made[79]. As has been noted, the definition of special business has been extended in Australia to include all but the most routine business of the annual

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78. Mod Bus Corp Act Ann 2d s 29.02.
79. *R* v *Hill* (1826) 14 B & C 426, 441, 107 ER 1118; see also *Dolbear* v *Wilkinson* (1916) 156 P 488 (Cal SC).

general meeting. Even in the absence of such an extended definition it would seem that the courts will demand specific notice of certain matters, such as action regarding remuneration of directors[80], as being required by the duty of good faith. By analogy with the reasoning in *Adams* v *Adhesives Proprietary Ltd* [81], where requisitionists were held to be under a duty not to time their meeting so as to disenfranchise a large number of members, it is submitted that this duty of good faith would bind requisitionists as well as directors issuing notice of meeting.

No action may be taken with regard to an item of special business unless due notice has been given, alerting all members that such action is contemplated. Action going beyond the scope of the notice is invalid and void[82]. The single possible exception is where all business of an annual general meeting is deemed general in the absence of a restricting clause, so that a shareholder is entitled to raise any matter at the meeting and, if he can muster the votes, any action proposed by him may be authorized by the meeting. Where such a restriction does exist, it would seem that any question may be discussed but no action could be taken, because the standard articles have the effect of displacing the common law rule that any business may be transacted at an annual general meeting even if, which is not clear, this rule would apply to a business company.

Where, in addition to the clause stipulating the express purpose of the meeting, a requisition of meeting states that it will consider the

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80. *Hutton* v *West Cork Railway Co* (1883) 23 Ch D 654.
81. (1932) 32 SR (NSW) 398 as discussed above, 244.
82. *Kaye* v *Croydon Tramways Co* [1898] 1 Ch 358; *Re Vale of Neath & South Wales Brewery Joint Stock Co; ex parte Lawes* (1852) 1 De G M & G 421, 21 LJ Ch 688.

affairs of the company or contains some other general words, this general clause will, it has been held, be ineffective to expand the scope of the meeting's business[83]. It would follow that the inclusion of such words in a notice of meeting would have, similarly, no effect on the purpose of the meeting. It is therefore suggested that such clauses be omitted from notices of meeting for fear of giving members a false impression. It would, however, be regrettable if this recommendation were to influence company administrators in their capacity as meeting chairmen to use their powers to prevent shareholders from seeking information or expressing views at company meetings.

A notice may stipulate more than one purpose for the meeting[84]. What is more,

> "a shareholders' meeting is not cast in a strait-jacket by the terms of the original notice convening it. It is, however, limited and restricted to dealing with such business as has been notified to members a sufficient period ahead of the meeting itself."*85*

It appears from this statement that later additions may be made to the list of stipulated purposes. However, this privilege belongs to the convening authority alone in most cases. Thus, where the board of a company complies with a requisition, it, but not any other individual, may add to the stated purposes[86]. Where requisitionists exercise their default rights they may add to the objects of the meeting specified in the notice of meeting something not stated in the original requisition[87].

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83. *Fruit & Vegetable Growers Association Ltd* v *Kekewich* [1912] 2 Ch 52.
84. *Cleve* v *Financial Corporation* (1873) LR 16 Eq 363; see also *Kaye* v *Croydon Tramways Co* [1898] 1 Ch 358.
85. *Holmes* v *Life Funds of Australia Ltd* [1971] 1 NSWLR 860; see also *Cotter* v *National Union of Seamen* [1929] 2 Ch 58.
86. *Ball* v *Metal Industries Ltd* [1957] SC 315; but see *Cotter* v *National Union of Seamen* [1929] 2 Ch 58 for an exception in the case of president.
87. *Holmes* v *Life Funds of Australia Ltd* [1971] 1 NSWLR 860.

In the absence of statutory provision, the effect of which will be discussed in another part of this thesis, no shareholder or group of shareholders may require management to give notice of any additional purpose for a general meeting, but they may make a request with which management may, in its discretion, comply[88].

The proxy rules passed under the American Securities Exchange Act and adopted in Canada in the last ten years have some relevance to notice requirements. The American rules require the proxy form to identify clearly and impartially each matter or group of matters intended to be acted upon at the meeting[89]. Where such a requirement applies, managerial freedom to frame the notice of meeting required under state law becomes irrelevant inasmuch as the proxy rules effectively abolish any power to change the agenda of the meeting after the notice has been issued. The provision that discretionary authority may be conferred to enable the proxy-holder to deal with matters which he did not know were to be raised at the meeting, on the other hand, makes it impossible for the chairman to reject a motion advanced by a shareholder not involved in the solicitation of proxies on the argument that shareholders represented by proxy would be disenfranchised. This result appears highly desirable, inasmuch as the freedom as to the agenda of an annual general meeting, which has been traced back to the common law of corporations, was intended to benefit shareholders or members but may function, in the absence of these provisions, as a licence to management.

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88. *Grundt* v *Great Boulder Proprietary Gold Mines Ltd* [1948] Ch 145.
89. Code of Federal Regulations s 240.14a.4(a)(3).

The function of a purpose-notice requirement, as an American judge recently said, *obiter*, is to provide the shareholder with

> "sufficient opportunity to study the action contemplated at the meeting... . When the shareholder possesses knowledge of a special meeting, he can study the proposal, arrive at a position and either oppose or support it."[90]

This view is, perhaps, inconsistent with the idea that notice has no role to play in protecting the voter against over-persuasion which seems to have been held until recently, but it is hoped that it will be adopted and fostered. However, if a shareholder is to be given a real opportunity to study the proposal, he must be told not only that the proposal will be put forward but must also be given a resume of the relevant facts and arguments. (The duty of disclosure of the purpose of the meeting may be distinguished from the duty of disclosure about the purpose of the meeting[91]: the former has been discussed in this section, the latter will be considered below[92].)

3. SPECIAL REQUIREMENTS

As well as stating the time, place and purpose of the meeting, the notice of meeting may in particular circumstances have to comply with special requirements. For example, a public company in Australia is required to hold a statutory meeting shortly after incorporation; the notice calling such a meeting must specify the intention to hold it as a statutory meeting or the meeting will not fulfil the requirement[93].

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90. *Darvin* v *Belmont Industries Inc* (1972) 199 NW 2d 542 (Ct of App Mich).
91. Getz, *op cit*, 245.
92. See below, 300-310.
93. *Gardner* v *Iredale* [1912] 1 Ch 700.

Before a special resolution may be passed, notice must be given "specifying the intention to propose it as such[94] and where such an intention is not specified the resolution will be ineffective"[95]. However, it is not necessary to use any exact form of words in specifying such an intention: where the intention is manifest the action will be valid[96]. Similarly, where statutory authority is necessary to validate a contemplated act, it has been held that the notice of meeting must intimate that such statutory authority will be invoked[97].

Another special requirement is that a notice must state the authority under which it is issued. There is a question as to whether this must always be set out. It is clear that a notice of meeting will be invalid if it is issued without the necessary authority. A company secretary, for example, cannot issue a notice of meeting in the absence of a resolution by the board of directors or some direction from another authority empowered to convene the meeting[98]. In a recent case in which a question was raised as to the validity of an extraordinary general meeting called by the board subsequent to action by certain members designed to obtain a meeting, Wootten J held that a notice will not be invalidated by the failure to mention the decision of the board so long as the necessary

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94. UCA s 144(1).
95. *MacConnell* v *E. Prill & Co* [1916] 2 Ch 57; *Re North Victoria Deep Leads Gold Mines Ltd* (1934) 40 ALR 221; *Re North of Scotland and Orkney and Shetland Steam Navigation Co Ltd* [1920] SC 94.
96. *In re NSW Property Investment Co* (1889) 10 NSWLR (Eq) 214. *Vawdon* v *South Sydney Junior Rugby League Club* (unreported decision of Wootten J NSW Supreme Court, 29 March 1976); see also *Taylor* v *MacNamara* [1974] 1 NSWLR 164.
97. *Etheridge* v *Central Uruguay Northern Extension Rail Co* [1913] 1 Ch 425; *Imperial Bank of China, India and Japan* v *Bank of Hindustan, China and Japan* (1868) LR 6 Eq 91.
98. *R* v *Bowman; ex parte Willan* (1872) 3 VR (L) 258; *Re State of Wyoming Syndicate* [1901] 2 Ch 431; but see *Hooper* v *Kerr, Stuart & Co Ltd* (1900) 83 LTR 729.

decision had been made[99]. There is a Canadian case which seems to apply the same rule to requisitioned meetings[100] but this authority is not so clear. It held that it was desirable, but not essential, that the notice state the authority invoked and that the pre-conditions have been fulfilled. However, in that case the documents which accompanied the formal notice did make clear the necessary facts so that the issue was not clearly presented. There may be more difficulty in applying such a rule to a requisitioned meeting inasmuch as there is a presumption that where meetings are summoned by the board, regularity is observed[101] which does not apply in the special circumstances in question.

An evolution in the law requiring the notice of meeting to state the authority under which it is called may be clearly traced through the American cases. Courts in the nineteenth century held not only that the power to convene a meeting might only be exercised by those to whom it was entrusted[102], but also that the notice must state the authority invoked, or "no stockholder need regard it"[103].

The first relevant case in the twentieth century arose under by-laws which gave one officer the power to call meetings and another the duty to issue notices[104]. The latter refused to issue the notices, so the former proceeded to do so himself. It was held that where the result intended, notification of the meeting, was achieved, "courts ought not to upset the business done by a corporation merely because some official

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99. *Vawdon* v *South Sydney Junior Rugby League Club* (unreported decision of Wootten J, NSW Supreme Court, 29 March 1976) page 5 of transcript.
100. *Dalex Mines Ltd (NPL)* v *Schmidt* (1973) 38 DLR (3d) 17.
101. *Bubb* v *Wickham & Bullock Island Coal Co Ltd* (1911) 12 SR (NSW) 207.
102. *Congregational Society of Bethany* v *Sperry* (1834) 10 Conn 200.
103. *Johnstown* v *Jones* (1872) 23 NJ Eq 216.
104. *Whipple* v *Christie* (1913) 141 NW 1107 (Minn SC).

who had no discretionary duty to perform...wilfully failed in a mere clerical act"[105]. However, in a strongly worded and persuasive dissenting judgment, Brown J demanded to know why an alleged notice should be held good when its validity depended upon collateral facts which were not disclosed and which the recipient could not know.

A later case held that notices which were sent out not by the company secretary but by a minor official at the president's direction and which recited that the meeting was called by the directors when in fact it was called by the president were valid. This finding was justified on the ground that all stockholders had received actual and seasonable (sic) notice of the meeting and that therefore the notices substantially complied with the requirements of the by-laws[106].

In a 1963 case the validity of the meeting was challenged on the ground that the notice purported to be signed by the assistant secretary, N, whereas, in fact, N no longer held that post and had not signed the notice. It was held that the notice had achieved its purpose in that the shareholders had attended the meeting. Relief was denied. However, the court expressly found that the defect was not calculated or designed to secure some improper advantage. This finding might not have been relevant where the plaintiff had a right to receive notice of meeting but in the instant case the plaintiff was only a beneficial holder of the shares, not being on the record he lacked standing to protest[107].

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105. *Whipple* v *Christie* (1913) 141 NW 1107 (Minn SC).
106. *Boericke* v *Weise* (1945) 156 P 2d 781 (Dist Ct of Appeal, First Div, Cal).
107. *Andrews* v *Precision Apparatus Inc* (1963) 217 F Supp 679 (SD NY).

It would seem that any shareholder who received a notice of a company meeting that sufficiently identified the time, place and object of a meeting should take note of it whether or not it states the authority under which it is issued. But inasmuch as the likelihood of receiving an unauthorized notice is small and the authority may be questioned at the meeting, this does not appear likely to cause undue hardship.

C. SUFFICIENCY OF NOTICE

1. PERIOD OR LENGTH OF NOTICE

The statutory provisions stipulating the minimum period of notice are mandatory in all the principal jurisdictions studied[108]. The Australian Companies Acts stipulate that a meeting shall be called by notice in writing "of not less than fourteen days or such longer period as is provided in the articles"[109]. Where a special resolution is to be passed at the meeting, however, not less than twenty-one days' notice must be given[110]. In contrast, the British legislation provides that the articles must require at least twenty-one days' notice of an annual general meeting and at least fourteen days' notice of any other meeting. The British Act further stipulates that unless other provision is made by the articles, such notice will be sufficient[111]. Apart from mere draftsmanship, the chief difference is that the British legislation requires longer notice of an annual general meeting than of a meeting to pass a special resolution while the Australian legislation equates the

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108. UCA ss 138(2) and 144(1); Companies Act, 1948 (UK) s 133(1) and (2); Can Bus Corp Act s 129(1); Bus Corp Act (Ont) s 106(1)(a).
109. UCA s 138(2).
110. UCA s 144(1).
111. Companies Act, 1948 (UK) s 133(1) and (2).

annual general meeting to other meetings at which no special resolution is proposed.

This difference between the Australian and the British provisions appears to stem from the report of the Cohen Committee. The report noted that it was desirable to devise provisions which would make it difficult for directors to secure the hurried passage of controversial measures and as far as possible to encourage shareholders carefully to consider any proposals required to be put before them by the directors[112]. The Australian legislation has accepted the major stress of this statement while the Cohen Report went on to emphasise the proviso. Taking the view that the length of notice required must not delay important transactions unduly, the Committee recommended a longer period of notice for annual meetings for two reasons. The first of these was the importance of the business transacted there, the second that this requirement would cause little inconvenience inasmuch as the necessity of such a meeting made it a foreseeable event while business of other meetings might well be more urgent[113]. While it is clearly a matter on which conflicting views may be held, it is respectfully suggested that the view adopted in Australia is preferable. Business transacted at an annual general meeting is of a recurring nature and it is likely to prove less harmful to choose directors who hold office for a limited period without full consideration than it would be to pass, for example, a resolution to wind up the company without such consideration. The purpose served by provisions fixing a period of notice was explained by Chitty J in a case concerning a provision which stipulated not only a minimum but also a maximum period of

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112. Cohen Report, op cit, para 124.
113. Idem, para 125.

notice. The minimum period was stipulated, he held, to give reasonable time for deliberation and to prevent undue haste and surprise as well as to allow the shareholders time to make arrangements to attend the meeting. The maximum period was stipulated lest the matter should be forgotten or be deemed to have been dropped, and to bring about a decision while the matter was comparatively fresh in the minds of the members[114]. Maximum periods of notice are not usually stipulated today except in North America. Where they were so stipulated in the articles of an Australian company, it was held that an informality which consisted of giving a slightly longer period of notice than strictly necessary would not invalidate the resolutions passed, as nobody could be prejudiced by such an informality[115].

All of the North American statutes which have been selected for purposes of comparison specify both a minimum and a maximum period of notice. In stipulating the minimum period, the Ontario Act differentiates between a company that offers its shares to the public and one that does not. This distinction may be explained by reference to the time it may take a dissident group to organize opposition. Where shares are offered to the public, communication with the other shareholders with a view to organizing opposition can take much longer and it would be appropriate to extend the necessary period of notice beyond the fourteen days currently stipulated for. When the proxy rules apply, and particularly when shareholder proposals are concerned, questions of timing can become vitally important. This has given rise to much discussion[116], but the question

114. *Re Railway Sleepers Supply Co* (1885) 29 Ch D 204, 206.
115. *Re Vale of Clwydd Coal Mining Co Ltd* (1912) 29 WN (NSW) 189.
116. Code of Federal Regulations s 240-14 a - 6(a)(2); s 240-14a-8(c), (d); see discussion in Aranow and Einhorn, *op cit*, 141, 142 and 281, 282.

will not be further canvassed here. Although the distinction between public and close companies would seem to be well founded, it has not yet been adopted elsewhere. None of these statutes draws any distinction between an annual general meeting or a meeting at which a special resolution is to be passed and any other meeting[117]. It is suggested that in this regard the Australian legislation is preferable but that the distinction between the private and the public company drawn in the Ontario Act should be adopted here.

In Australia the articles may stipulate a longer period of notice than that required by statute, but they do not usually do so[118], and the Australian Stock Exchange Listing Requirements, the only other external influence relevant, also adopt the statutory period[119]. It is, therefore, important that the statutory periods be of sufficient length. Gower states that the provisions adopted in 1948 constituted a great improvement but that the period provided will still be woefully short if the opposition has to start from scratch. He further states that the intention behind the provisions is often defeated by the use of proxies lodged long before the meeting[120]. However, it is difficult to lay down strict guidelines to govern the appropriate period of notice as this will vary according to the nature of the company and the standard of the mail service[121]. When a period of notice is stipulated, the stipulation must be interpreted. It has been observed that: "Probably no question

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117. Bus Corp Act (Ont) s 106(1)(a); Can Bus Corp Act s 129(1); Mod Bus Corp Act Ann 2d s 29.

118. *Cohen Report, op cit,* para 126.

119. Associated Australian Stock Exchanges Listing Requirements, formerly 1.B.17, 3.A.15, 3.H.17, now 3.A.

120. Gower, L.C.B., *Principles of Modern Company Law*, 3rd ed (London, Stevens & Sons, 1969) 477-478.

121. See *John Morley Building Co* v *Barras* [1891] 2 Ch 386, where the court held with respect to a meeting of subscribers that, in the absence of specific provision, only reasonable notice was necessary. Factors taken into account are interesting.

has more vexed the minds of judges in former times than the question as to the proper mode of computing the time"[122]. It is suggested that one reason for this concern has been the fact that the question is purely one of logic or construction involving no policy considerations and thus one with which the judicial mind could freely toy. However that may be, the rule is now well settled, where the relevant provision uses the expression "at least" or stipulates for clear days, then neither the day of service nor the day of the meeting may be counted[123]. Further, express provisions may be made in drafting the article[124].

Although the statutory provisions concerned are mandatory, shareholders may, by express agreement, accept a shorter period of notice. In the case of an annual general meeting, such agreement must be unanimous, while in any other case ninety-five per cent approval is sufficient under both the Australian and the British provisions[125]. Although provisions stipulating a minimum period of notice are designed to protect the shareholders, the matter was once deemed to be one of internal management. Thus it has been held that although insufficiency of notice would be decisive as between the company, its shareholders and directors, it does not affect the rights of creditors[126]. In another case the court refused to make an order based on this insufficiency but recessed to allow the irregularity to be corrected[127]. However, the effect of these decisions may have been displaced by the statutory provisions just cited.

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122. *Re Railway Sleepers Supply Co* (1885) 25 Ch D 204.
123. *Re Railway Sleepers Supply Co* (1885) 25 Ch D 204; *Mount Oxide Mines Ltd* v *Goula* (1915) 15 SR (NSW) 290; *Re Hector Whaling Ltd* [1936] Ch 208; *Ashton* v *Powers* (1912) 67 DLR 222, 51 OLR 309; but see *Neil M'Leod & Sons Ltd Petitioners* [1967] SC 16 and *Re Pavilion Newcastle-upon-Tyne Ltd* [1911] WN 235.
124. UCA Fourth sched Table A reg 45.
125. UCA ss 138(3) and 144(2); Companies Act, 1948 (UK) s 133(3); *Cohen Report, op cit*, para 126.
126. *Re Millers Dale and Ashwood Dale Lime Co* (1885) 31 Ch D 211.
127. *Mount Oxide Mines Ltd* v *Goula* (1915) 15 SR (NSW) 290.

2. SERVICE OF NOTICE

The Canada Business Corporations Act stipulates that notice of meeting "shall be sent" to the shareholders[128]. The provisions in each of the other statutes examined are more complex. The Ontario legislation stipulates in mandatory terms that notice shall be given by sending it by prepaid mail to the latest address of the member shown on the corporation records[129]. The Model Business Corporations Act provides that it shall be delivered either personally or by mail to each shareholder. If mailed, such notice is deemed to be delivered when a prepaid letter is deposited in the mail[130].

The Australian and British provisions, unlike their North American counterparts, are not set out in the body of the legislation. Instead, the stipulation appears in the legislation that notice be served on those entitled to it "in the manner in which notices are required to be served by Table A"[131]. The only putative distinction between the Australian and British provisions arises when the question is posed whether the Table A articles referred to are those currently in force or those in force when the company was first incorporated. The British legislation states that for this purpose Table A means that table currently in force[132]. It is suggested that, if the question arose, it would be held that the Australian provision had the same effect. The basis of this suggestion is the fact that the Table A articles in force when the company is registered would apply in the absence of articles

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128. Can Bus Corp Act s 129(1).
129. Bus Corp Act (Ont) s 106(1)(a).
130. Mod Bus Corp Act Ann 2d s 29.
131. UCA s 138(4).
132. Companies Act, 1948 (UK) s 134(a).

excluding or modifying them by force of section 30(2) of the Companies Act. Unless the New South Wales provision as to notice is equivalent in meaning to the British Act, the wording used is redundant[133].

The relevant articles of the Australian Act are regulations 108 and 109[134]. These articles provide that a notice may be given by the company to any member personally or by post at his registered address, or the address within the state supplied by him for the purpose. Special provisions apply to notices sent by mail. Service of the notice is deemed to be effected by properly addressing, prepaying and posting a letter containing the notice and such letter is presumed to have arrived the day after it was posted[135]. Where a share is held jointly, notice to the first named joint holder is sufficient. It is clear that even where these regulations apply, the member may not actually receive the notice, but the company itself cannot be blamed where the mail fails to go through[136]. However, the articles can make other provisions which would make a travesty of the notice requirement. In theory, the articles might provide that notice be given by affixing it to a notice board at the registered office[137], and it was once common to provide that notice should be given by publication in a newspaper which might or might not come to the member's attention. It is suggested that the present provisions of the Table A articles might appropriately be made obligatory.

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133. See *Hawkesbury Development Corporation Ltd* v *Landmark Finance Pty Ltd* (1969) 92 WN (NSW) 199, 221 for discussion of the analogous question of whether Third Schedule powers accrued to companies incorporated before 1961.
134. Companies Act, 1948 (UK) First sched Table A regs 131 and 132.
135. See *Gresham House Estate Co* v *Rossa Grande Gold Mining Co* [1870] WN 119.
136. *Alexander* v *Simpson* (1889) 43 Ch D 139.
137. Gower, *op cit*, 478.

Inasmuch as they are generally followed, this would in practice amount to only a small change, but in theory the move is desirable as the possibility outlined should be excluded.

Where there is no prescribed mode for service of notice, a situation which cannot arise under the present legislation, it is necessary to prove not only that notice was sent but also that each individual member received it[138]. Of more relevance now is the question of the effect of failure to follow the prescribed mode for service. In general it is clear that non-compliance with the prescribed mode will be fatal to the validity of the meeting. This is because the articles which prescribe the mode are deemed to have contractual force as pre-conditions for the meeting's validity. Thus, where notice was required to be given by publication and was instead given by circular, the meeting was invalid[139].

The severity of such rulings has been relaxed on occasion. Thus, where notice which was to be sent by post was in fact given personally it was held that, as the object of ensuring that every shareholder received notice had been achieved, the service was sufficient[140]. It should be noted, although it is suggested that the distinction makes no difference, that in the cases in question the mode of service was stipulated not by the articles but by court order.

In a relatively recent New South Wales case, the articles of a Leagues Club provided for service either in person or by mail to a registered

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138. *Charlton* v *Barkly Reef Gold Mining Co* (1877) 3 VLR (L) 101; see also *Bank of Little Rock* v *McCarthy* (1897) 18 SW 759 (Ark SC); *Stow* v *Wyse* (1828) 7 Conn 214.
139. *Solomon* v *Collingwood Quartz Mining Co* (1867) 4 WW & A'B 128.
140. *Re International Harvester Co of Australia Pty Ltd* [1953] VLR 669 citing *Re Anglo-Saxon Tarter Refineries Ltd* [1924] WN 222; see also *State Bank of Wilbur* v *Wilbur Mission Church* (1954) 265 P 2d 821.

address within the state, providing that, if there was no such address, a notice posted on the notice board would be sufficient. The directors purported to give notice by posting a notice on the board, by making periodic announcements on the public address system, and by publication in the Club journal. It was held that such notice was insufficient and, inasmuch as the court was not satisfied that a substantial number of members had actual notice of the meeting, the court refused to make an order under section 366 waiving the irregularity[141].

It is clear that it is the member's responsibility to ensure that the company has his latest address for service. When he has not notified the company of a change of address, a letter sent to the registered address will constitute valid notice despite the fact that previous notices sent to that address have been returned. The company may not effectively serve notice on a member by giving it to anyone else even if it is known that that person is in contact with the member[142].

D. SUFFICIENCY OF DISCLOSURE

1. GENERAL LAW REQUIREMENTS IN AUSTRALIA AND BRITAIN

Despite a recommendation from the Jenkins Committee[143], neither the

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141. *Mansfield* v *NSW Leagues Club Bowling Club Ltd* (1963) 80 WN (NSW) 1407.
142. *Home State Bank of Manhattan* v *Swartz* (1926) 252 P 396 (Mon SC).
143. *Jenkins Report, op cit,* para 466-468 noting that section 207(1)(a) is no more than declaratory of the general law but urging the utility of such a provision.

British nor the Australian legislation yet contains any general provision declaratory of the duty of disclosure placed on the board of directors in relation to matters discussed at meetings. That notice must be given specifying the purpose of the meeting, in all but a few cases, has already been shown.

When a purpose is stated, the question arises whether the information disclosed is sufficient. It is suggested that it should not, for example, be sufficient to disclose that a resolution to authorize the sale of the company's major undertaking will be proposed without also disclosing the proposed price or price range, the reasons for the sale and the proposals for disposition of the proceeds and for the company's future to the extent to which these are relevant. The question for consideration in this section is whether the law contains provisions designed to ensure that the information disclosed is sufficient and whether these are adequate.

Frequently the purpose of the meeting will be stated formally in the notice of meeting while argumentative material will be set out in accompanying documents. However, these documents are read with the formal notice[144] and, it is submitted, should not escape scrutiny when the question arises whether sufficient disclosure has been made.

There is a multitude of cases in which the decision has rested on the finding that in the particular circumstances, sufficient disclosure has not been made. Not all of these have been scrutinized, and of those

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144. *Tiessen* v *Henderson* [1899] 1 Ch 861, accompanying documents are to be read with the notice but not so as to extend its scope to include additional unrelated matters: *Vawdon* v *South Sydney Junior Rugby League Club* (unreported decision of Wootten J, NSW Supreme Court, 29 March 1976).

which have been scrutinized there are many in which the court confined itself strictly to a consideration of the facts. No purpose would therefore be served by analysing these cases. However, there are other cases in which some general remarks have been made.

One of the less well known authorities on this question is the High Court decision in the case of *Ryan* v *Edna May Junction Gold Mining Co NL*[145]. The question was whether the rights in the winding up of the company were to be determined under the general provisions in the articles or under a special proviso which could apply in the circumstances but which had not been invoked in the notice. It was held by Isaacs J that the shareholders "are not to be put upon conjecture as to what might be intended. They cannot, of course, require meticulously precise notices. All that is needed in the absence of definite provision is a fair and reasonable intimation of what is actually proposed to be done"[146]. The reason for the requirement as explained by Barton J is the possibility or presumption that the shareholders who stay away do so because they are satisfied that the proposal is advantageous[147]. In the instant case it was held that to wind up the company under the special proviso would disadvantage certain shareholders who might have desired to attend the meeting to oppose this step and therefore, in the absence of notice that the special proviso was being invoked, the winding up was to be governed by the general provisions.

Notice, it has been held, ought to put the shareholder in a position to judge for himself whether he would consent to the proposal put forward

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145. (1916) 21 CLR 487.
146. (1916) 21 CLR 487, 500.
147. (1916) 21 CLR 487, 494 citing *Clinch* v *Financial Corporation* (1867-68) LR 5 Eq 450, 481.

for his approval[148], but it must not be forgotten that the notice is preliminary to a meeting where arguments pro and con which are expected to influence the member's decision will be put[149]. Thus it is suggested that what the notice should do is to give the members the essential facts, leaving persuasion for the meeting.

Whether or not a notice does put the shareholder in possession of the necessary facts is a question which must in each case be answered on the facts[150]. Thus the general rule that the notice need not give the specific terms of the proposed resolution but need only specify the general nature of the business to be considered[151] is subject to modification where the directors stand to gain a benefit which remains hidden under the terms of the notice[152]. It has been held that in reading the notice and accompanying documents to determine whether there has been sufficient disclosure, the court should not be overly critical[153]. The test for construction of notices has been variously expressed to be what an ordinary man[154], a man of ordinary prudence[155], or a person of common sense[156] would understand.

No matter how specific the notice, it would appear that it will not have the effect of rendering it impossible to amend the resolution proposed[157]

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148. *Pacific Coast Coal Mines Ltd* v *Arbuthnot* [1917] AC 607.
149. *Attorney-General* v *Scott* (1745) 1 Ves Sen 413, 27 ER 1113, as discussed below, 326-328.
150. *Normandy* v *Ind Coope & Co Ltd* [1908] 1 Ch 84.
151. *Betts & Co Ltd* v *MacNaghten* [1910] 1 Ch 84; *Colhoun* v *Green* [1919] VLR 196.
152. *Kaye* v *Croydon Tramways Co* [1898] 1 Ch 358; *Colhoun* v *Green* [1919] VLR 196; *Normandy* v *Ind Coope & Co Ltd* [1908] 1 Ch 84, but contrast with the last case cited *Young* v *South African & Australian Exploration & Development Syndicate* [1896] 2 Ch 268.
153. *Henderson* v *Bank of Australasia* (1890) 45 Ch D 330.
154. *Choppington Collieries Ltd* v *Johnson* [1944] 1 All ER 762; *Henderson* v *Bank of Australasia* (1890) 45 Ch D 330.
155. *Tiessen* v *Henderson* [1899] 1 Ch 861.
156. *Inglewood Mining Venture Ltd* v *Price* (1872) 6 SALR 20.
157. *Betts & Co Ltd* v *MacNaghten* [1910] 1 Ch 430; *Henderson* v *Bank of Australasia* (1890) 45 Ch D 330.

so long as such amendment does not amount to an attempt to obtain a resolution on a totally different subject, but this matter will be considered further elsewhere.

Two decisions whose merits might well be reconsidered have laid it down that an explanation which does not reveal that there are two sides to a question[158] or which conveys an incorrect view of the situation[159] does not amount to an insufficient disclosure so as to invalidate the notice inasmuch as the members are not barred from putting their own views to the meeting. In view of the widespread use of the proxy, this would seem to be an inadequate remedy and it is suggested that to put only one side of the question to the shareholders is not to put them in a position to make an intelligent decision.

Where bad faith can be substantiated, no court will hesitate to declare that insufficient notice invalidates the subsequent resolutions. "Tricky" notices, that is, notices designed to deceive, being worded so that although no outright lies are told, the shareholder who glances at it quickly will be misled, are not tolerated by the courts[160].

Where the general meeting is called upon to pass a resolution ratifying an invalid act of the board of directors, the standard of disclosure demanded is higher than that imposed in other cases. The board is required to state why the general meeting is being asked to pass the resolution in question, but they are not even in this situation obliged to put the opposing arguments to the shareholders. It is submitted that

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158. *Matabeleland Co Ltd* v *British South Africa Co* (1893) 10 TLR 77.
159. *Peters American Delicacy Co* v *Heath* (1939) 61 CLR 457.
160. *Kaye* v *Croydon Tramways Co* [1898] 1 Ch 358; *Garvie* v *Axmith* (1962) 31 DLR 2d 65.

the duty to disclose should and must extend beyond the duty to state one's own views in good faith. Some duty to take care in informing the shareholders should be insisted on so that inaccuracies and omissions are discouraged.

The Canada Business Corporations Act does make an attempt to impose such a duty. It contains a provision such as that recommended by the Jenkins Committee to the effect that notice of a meeting at which special business is to be transacted shall state the nature of the business "in sufficient detail to permit the shareholder to form a reasoned judgment thereon"[161]. It also provides that the text of any special resolution shall be set out. The first clause expresses the general law[162], but the second clause may go further. It is not clear whether under such a provision amendments would be allowed to be made at the meeting. If the clause does have the effect of preventing amendments from being made, it would seem to be far from desirable.

It is, of course, clear that an appeal to the members to trust the judgment of the board is no substitute for a sufficient disclosure of facts. While it is true that in a going concern the member will have confidence in the executive, he is entitled to know whether there is anything to shake his confidence[163]. However, a Canadian court which considered the

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161. Can Bus Corp Act s 129(6).
162. Getz, *op cit*, 245.
163. *Normandy* v *Ind Coope & Co Ltd* [1908] 1 Ch 84, 101 per Kekewich J, adopting a view which is, it is submitted, preferable to that he expresses in *Young* v *South African & Australian Exploration & Development Syndicate* [1896] 2 Ch 268.

validity of a resolution passed after just such an appeal supplies direct authority for the proposition[164].

The Ontario Business Corporations Act contains no provision requiring sufficient disclosure as a component of notice of meeting, but both it and the federal legislation contain provisions requiring disclosure in connection with the solicitation of proxies[165]. These provisions are modelled on those first passed in the United States and reference is made to the next section where these will be discussed.

As proxy solicitation is mandatory when membership exceeds a minimum number of fifteen, the Canadian provisions achieve wide coverage. The relationship between these provisions and those of the general law relevant in Australia, Britain and Canada before enactment of the new legislation was stressed by one Canadian judge who seemed to take the view that the duty of disclosure had not been extended[166]. It cannot, however, be denied that such statutory provisions make the duty of disclosure more specific and, it is submitted, these provisions also import a duty of care to supplement the duty of good faith in this matter.

Before turning to examine the provisions of the proxy rules, an inherent problem in enforcing sufficient disclosure under the general law should be noted. Where the would-be recipients of the information are so thoroughly misled as not to know that something is being concealed, there will be no one to complain. It appears that the only person who will have standing to complain will be someone who is entitled to receive such

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164. *Rudkin* v *British Columbia Automobile Association* (1969) 70 WWR 649 (BC).
165. Bus Corp Act (Ont) s 118; Can Bus Corp Act s 144.
166. *Charlebois* v *Bienvenue* (1967) 64 DLR 2d 683, 692.

information, but an ingenious argument to the effect that a recipient who inquired further and acquired the information which should have been imparted could not complain, has been advanced and rejected. A member of a company has a right not merely to receive sufficient information himself but also to ensure that his fellow members are not misled by those whose duty it is to inform them[167].

2. DISCLOSURE REQUIREMENTS IN THE UNITED STATES OF AMERICA

There is no provision in the Model Business Corporations Act relevant to the duty of directors to make any sufficient disclosure of information preparatory to a corporate meeting. Nor is there much recent case authority concerning the duty to disclose in the notice of meeting. Since the 1930's, the principal thrust of the law in this area has been based on the requirement of disclosure in connection with the solicitation of proxies. Rule 14 A - 9, which prohibits solicitation by means of false and misleading statements in the proxy statement or form or in the notice of meeting or other communication, has been described as the most important of all the proxy rules for this reason[168].

It is, however, clear that even where the proxy rules do not apply, American law is not powerless to prevent an abuse of corporate procedure occurring through failure to disclose. Thus it was held that a notice whose purpose was "to lull the petitioner into a false sense of security and to discourage him from attending the meeting so that the hidden and

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167. *Kaye* v *Croydon Tramways Co* [1898] 1 Ch 358; *Garvie* v *Axmith* (1962) 31 DLR 2d 65.

168. Aranow and Einhorn, *op cit*, 146, see also 146-159.

secret purpose and scheme of the respondent might be carried out without opposition" invalidated the meeting[169]. In so far as the proxy rules do not apply, the American position is identical to the Anglo-Australian: the shareholders must be given information sufficient to allow them to exercise an intelligent judgment but need not be given details[170].

Under the general law in force before the proxy regulations became operative, a proxy solicitor was held to be under no duty to reveal tactical plans even when these plans included such a major step as amending the by-laws[171]. The proxy regulations changed this, and both management and non-management are now required to give information on these matters and a number of others specified in the rules.

The body of case law on what constitutes sufficient disclosure under these rules, what will amount to a false and misleading statement and what the effect of such a statement will be, is enormous and no attempt has been made to canvass it all. The principle involved would seem to be the same as that at stake where disclosure in the notice of meeting is concerned. A person who solicits proxies is obliged to make a full and fair disclosure of those facts that a stockholder might reasonably need in order to make an intelligent decision but not to include in the proxy statement every single detail that might be relevant. Thus material facts should be selected from the mass of relevant material[172]. Nevertheless, lawyers in other jurisdictions frequently express dismay

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169. *In re Faehndrich's Petition* (1956) 151 NYS 2d 261 (NY SC).
170. *Gruber* v *Chesapeake & Ohio Railway Co* (1957) 158 F Supp 593 (ND Ohio); *Jones* v *Commonwealth Edison Co* (1938) 18 NE 2d 113 (App Ct Ill).
171. *Gow* v *Consolidated Copper Mines Corp* (1933) 165 A 136 (Ch Del).
172. *Richland* v *Crandall* (1969) 262 F Supp 538 (SD NY).

at the mass of information which proxy statements sometimes contain. It is, indeed, possible that a new way to avoid sufficient disclosure has been found, a method that consists of burying the stockholder in a mass of minimally relevant material. In one case in which corporate management provided the shareholders with a mass of bare facts, an American court held the statement invalid as being false and misleading even though it was conceded that a sophisticated analyst with knowledge of the corporate world might ultimately be able to make significant deductions from the material. It was held that: "Conclusory statements and bare facts without a disclosure of the key issues involved will not satisfy the requirements"[173].

The United States Supreme Court has held that there is an individual right of action to enforce the requirements of the proxy rules which require the directors of a company who solicit proxies to make a sufficient disclosure of information deemed material[174]. Further, the damage which is suffered where sufficient disclosure is not made results not from the deceit practised on the complainant alone but from the deceit practised on the stockholders as a group[175]. Each stockholder, it has been held, has a right to insist that neither he nor his fellows be deceived when acting in a body in casting their votes[176].

Before a right of action will arise, it must be established that the omission or misstatement was material. This does not mean that it must be established that a different result would have ensued, but only that

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173. *Robinson* v *Penn Central Co* (1971) 336 F Supp 655 (ED Penn).
174. *J.I. Case* v *Borak* (1963) 377 US 426.
175. *J.I. Case* v *Borak* (1963) 377 US 426, 432.
176. *Gerstle* v *Gamble-Skogmo Inc* (1969) 298 F Supp 66, 96 (ED NY); on the question of damages (1971) 332 F Supp 644 (ED NY).

it must be shown that there was a likelihood that some stockholder might have voted differently[177].

The aim of disclosure provisions whether embodied in the proxy rules or elsewhere must be to ensure that corporate management does not purport to fulfil the fiduciary duty to inform their members by issuing a statement in which they "omit a fact or two here, disperse others through the ...statement, make a slightly misleading statement there and rest on the assumption that the drafter's task has been adequately performed if he can avoid blatant fraud and still keep the stockholder from discovering what shell the pea is under"[178]. It is submitted that the Australian provisions, whether they relate to notice of meeting or to proxy statements, a difference relevant only inasmuch as it affects the coverage of the disclosure provisions, should be amended to make the "pea" harder to hide.

E. EFFECT OF IRREGULARITY ON VALIDITY OF NOTICE

Prima facie the effect of an irregularity in the notice of meeting is to invalidate the meeting and any resolutions which are passed subsequent to that notice. However, both courts and draftsmen have, understandably, proved reluctant to see an elaborate structure invalidated for what might be a minor and technical defect. The courts have protected the validity of company meetings by applying a presumption of regularity[179]

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177. *Dunn* v *Decca Records* (1954) 120 F Supp 1 (SD NY); *Goldfield Corp* v *General Host Corp* (1971) 318 NYS 2d 378 (Sup Ct Apl Div).
178. *Gould* v *American Steamship Co* (1970) 319 F Supp 795, 810 (D Del).
179. *Bubb* v *Wickham & Bullock Island Co Ltd* (1911) 12 SR (NSW) 20; *Papillon* v *Brunton* (1860) 29 LJ Exch 265.

and a doctrine of waiver, as well as by developing an internal management rule[180]. There is nothing objectionable in the first two responses if one accepts that it is no function of the principle of notice to ensure the shareholder ample time for consideration but, it is submitted, in one of its applications the internal management rule is objectionable. Outsiders are not privy to the internal workings of the company and have no way of knowing whether due notice has been given or not. The rule in *Turquand's* case[181], designed to protect the outsider in such cases, is therefore unexceptionable. However, the internal management rule should have no application in questions between the company and its shareholders. The draftsman's response to the prospect of having a meeting invalidated by an irregular notice has taken the form of providing against an accidental omission and, more recently, the statutory provision for regularization, section 366, has been framed. Of these various responses, only the application of the doctrine of waiver and the provisions against accidental omissions have peculiar relevance to notices of meeting.

1. ACCIDENTAL OMISSIONS

The provision now found in the Australian Companies Acts to the effect that accidental omissions to give a notice of meeting to any member or

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180. *Grant* v *UK Switchback Railways Co* (1888) 40 Ch D 135; *Bentley-Stevens* v *Jones* [1974] 2 All ER 654 which last case, however, concerns a directors' meeting; see *Taylor* v *McNamara* [1974] 1 NSWLR 165 where Mahoney J queries the applicability of the internal management rule.

181. *Turquand's* case (1856) 6 E & B 327, 119 ER 886; see K.E. Lindgren's Ph D thesis as extracted in "*The Power of a Constitutional Organ of a Registered Company to Bind the Company by its Contractual Acts*" (1977) 8 Syd L Rev 333.

the non-receipt of a notice of meeting by any member shall not invalidate the proceedings[182] first found official sanction in 1928[183], when it first appeared in the Table A articles to the British Act. The British provision is still to be found in the Table A articles[184] and not in the body of the Act, but inasmuch as this article serves the interests of company managements who will not therefore be tempted to exclude it, it is suggested that this distinction is irrelevant[185].

So long as this provision is not unduly extended, it is unexceptionable and, indeed, in serving the interests of regularity serves the interests of the company's members as well as its management. The word "accidental" must, however, be strictly construed to avoid the section being abused. It is, therefore, reassuring to find that it has been held that deliberate omission to give notice whether under a mistake of fact or of law or of mixed fact and law is not an accidental omission[186]. Further, it is to be hoped that the holding of Street J on the effect of the provision as embodied in an article will hold true also of the statutory provision. It cannot validly be construed so as in effect to dispense with notice to an appreciable or large number of shareholders[187]. There is no comparable provision in any North American jurisdiction.

2. WAIVER

Canadian federal legislation contains a statutory provision embodying

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183. UCA s 138(4).
184. Companies Act, 1948 (UK) First sched Table A reg 51.
185. See *Re West Canadian Collieries Ltd* [1963] 1 All ER 26.
186 *Re Compaction Systems Pty Ltd and the Companies Act* [1976] 2 NSWLR 477, 478.
187. *Holmes* v *Life Funds of Australia* [1971] 1 NSWLR 860.

the doctrine of waiver[188], but in all other jurisdictions the doctrine depends strictly on case authority. Waiver, it has been held, may be expressed either orally or in the form of document[189], or it may be implied where the member voluntarily attends and participates in the meeting without protesting against the irregularity[190] or under certain other circumstances[191] as, for example, where a member attends the meeting to oppose the proposal but afterwards lets several months go by without taking further action[192]. However, despite some bald statements to the effect that physical presence constitutes waiver[193], it is clearly established that mere physical presence while an unauthorized minority seeks to take action in the name of the company cannot deprive a member of the right to object to lack of notice[194].

One recent American case drew an interesting distinction between waiver of time and place and waiver of notice of purpose. It was suggested that inasmuch as the notice of time and place of meeting was intended to make it possible for the member to attend, presence at the meeting was sufficient waiver of a notice designed merely to achieve this purpose, but

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188. Can Bus Corp Act s 130.

189. *Re Express Engineering Works* [1920] 1 Ch 466; *In re British Sugar Refining Company* (1857) 3 K & J 408, 69 ER 1168; *J.W. Butler Paper Co* v *Cleveland* (1906) 77 NE 99 (Sup Ct Ill).

190. *Re Joyce Bros Pty Ltd* (1935) 55 WN (NSW) 192; *Re Oxted Motor Co* [1921] 3 KB 32; *Transport Ltd* v *Schonberg* (1905) 21 TLR 305; *Walsh* v *Stephens* (1873) 3 QSCR 18. See also *Camp* v *Shannon* (1961) 348 SW 2d 517 (Tex SC); *Caldwell* v *Kingsbury* (1970) 451 SW 2d 247 (Tex Ct Civ Aps); *Hiles* v *C.A. Hiles* (1905) 120 Ill App 617.

191. *Harvey* v *Adelaide and Hindmarsh Tramway Co Ltd* (1881) 15 SASLR 136; see also *Andrews* v *Precision Apparatus Inc* (1963) 217 F Supp 679 (SD NY): *Weinburg* v *Union Street Railway Co* (1897) (Ch NJ). Plaintiffs in the latter case sought to prevent passage of certain resolutions by injunction; see also *Matter of 74 & 76 Tremont Ave Corp* (1958) 173 NYS 2d 154 (Spec Term) where the possibility of the officer responsible for issuing the notice insisting on an irregularity was considered.

192. *Harvey* v *Adelaide and Hindmarsh Tramway Co Ltd* (1881) 15 SASLR 136.

193. *Re Express Engineering Works Ltd* [1920] 1 Ch 466; *Beggs* v *Myton Coal & Irrigation Co* (1919) 179 P 984 (Utah SC).

194. *Harvey* v *Adelaide and Hindmarsh Tramway Co Ltd* (1881) 15 SASLR 136; *Dolbear* v *Wilkinson* (1916) 156 P 488 (Cal SC).

that when the notice was required to specify the object of the meeting the member is entitled to insist upon the full period of notice and mere presence would not then constitute waiver[195]. Inasmuch as an Australian company's notice will usually serve both functions, the distinction will not often be of functional importance. However, the distinction is logical and should be adopted where relevant.

The theoretical basis of the doctrine of waiver of notice is the idea that as notice requirements are designed for the protection of the shareholders and for no other purpose, the shareholders individually can waive these requirements. Although the idea that a person should be able to waive provisions designed for his protection has been challenged in certain areas recently, to allow a shareholder to waive notice requirements is acceptable where such waiver is express. The fact that the right is held in common by what may be a very large number of people and that any one of these may bring an action to invalidate the proceedings unless he personally has waived the irregularity imports an extra safeguard against abuse of waiver. It becomes increasingly unlikely that notice will be dispensed with in a case where any contention as to the proposed measure exists.

Where waiver is to be implied the doctrine is much more dangerous. It is submitted that waiver should not be implied unless the shareholders are made aware that they are waiving provisions designed for their protection. In particular, it is felt that they should be given an opportunity to insist on the full period of notice, a period that may be useful should they desire to consider the matter at length. A Canadian

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195. Darvin v *Belmont Industries Inc* (1972) 199 NW 2d 542 (Ct of Aps Mich).

case in which the judge found it necessary to decide that the notice provisions were not designed to impose a time for reflection before he could hold that notice had been waived should be noted[196]. It is submitted that the law should be altered to make it clear that notice provisions are designed to impose a time for reflection on the shareholders or at least to encourage them to reflect on the wisdom of the proposal and that accordingly implied waiver should not be recognized.

Both the Australian and the British statutes contain express statutory provisions noted above that govern agreements to shorten the period of notice. In the face of these provisions it has been held that waiver of this particular irregularity will not be implied. However, where express consent was obtained after the meeting from all members, the court declined to interfere[197]. The statutory provisions in question thus operate to exclude implied but not express waiver of notice where the irregularity affects the period of notice and effectively answer the objections stated above.

Notice, it has been held, is indispensable unless waived, and the fact that no member is actually injured or deprived of a substantial right by lack of notice is immaterial[198]: the requirement, especially when contained in a statute, is sacramental[199]. As each member has an individual right to due notice, the fact that all but one of them has waived the requirement is irrelevant. Further, the fact that that member had actual notice of the meeting and intended to attend is immaterial[200]. However,

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196. *Re Excel Footwear Co, ex parte Nova Scotia Trust Co* [1923] 3 DLR 212.
197. *Re Pearce, Duff & Co Ltd* [1960] 3 All ER 722.
198. *People ex rel Carus* v *Matthiessen* (1915) 109 NE 1056 (Sup Ct Ill).
199. *Jones* v *Shreveport Lodge No 122 BPOE* (1952) 60 So 2d 889 (Sup Ct La).
200. *In re the Election of Directors of FDR-Woodrow Wilson Democrats* (1968) 293 NYS 2d 463 (Spec Term); see also *Nelson* v *Hubbard* (1892) 11 So 428 (Sup Ct Ala).

where all the shareholders have waived notice the corporation is also estopped from pleading irregularity due to lack of notice[201]. When notice of meeting is waived or deemed to have been waived because the purpose of the requirement has been fulfilled[202], the meeting and all proceedings of the meeting will be as valid as if full notice had been given[203].

F. ADJOURNED MEETINGS

It is unnecessary to give notice of adjourned meetings unless such notice is specifically required by the company's articles[204]. This follows from the fact that an adjournment is considered to be but a continuation of the original meeting. All the members who were present at the original meeting know where and when the meeting will continue and it is assumed that those members absent from the original meeting were absent because they were not interested and thus will have no desire to attend the resumed meeting. This assumption may be made too readily in some cases but inasmuch as the process of issuing notices may cost a considerable amount and the number of cases in which shareholders having unavoidably missed the original meeting will want to attend the continuation will be slight, it is not justifiable to require that notice of adjournment be sent out in most circumstances.

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201. *Kearnseyville Creamery Co* v *American Creamery Co* (1927) 137 SE 217 (Sup Ct Aps W Va).
202. *Benbow* v *Cook* (1894) 20 SE 453 (Sup Ct N Ca); *J.W. Butler Paper Co* v *Cleveland* (1906) 77 NE 99 (Sup Ct Ill); *Nelson* v *Hubbard* (1892) 11 So 428 (Sup Ct Ala).
203. *Benbow* v *Cook* (1894) 20 So 453 (Sup Ct N Ca).
204. *James* v *Rymill* [1932] SASR 365; *Robert Batcheller & Sons Ltd* v *Batcheller* [1945] Ch 169.

Where the time and place at which the meeting is to be continued are not announced at the original meeting, it is suggested that the company will be under a duty to provide such details by means of a notice. Further, where an adjournment is prolonged, some reminder such as that required under Canada's federal legislation may seem desirable[205].

G. SUMMARY

Notice requirements are capable of serving two functions, of ensuring first that each shareholder or member is informed as to when and where a company meeting is to be held and, secondly, that each knows what questions will be put before the meeting and has the basic data necessary for an intelligent decision on each question. Under Anglo-Australian company law these functions are in fact performed almost exclusively by the notice of meeting while under American law the proxy statement is made to serve the second function to a much greater extent. In consequence, the American provisions de-emphasise provisions designed to make the notice serve this function[206]. It is submitted that, inasmuch as notice requirements achieve wider coverage, the Australian approach is preferable but that it would be desirable to emphasise yet further the informational aspect by adopting disclosure provisions similar to those enforced under the American proxy rules and by promoting a consciousness of this function of the notice.

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205. Can Bus Corp Act s 129(3) and (4).
206. Cary, W.L., *Cases and Materials on Corporations*, 4th ed (New York, The Foundation Press Inc, 1969); Gower, L.C.B.,"*Some Contrasts between British and American Corporation Law*" (1956) 69 Harv L Rev 1369, 1391.

PART VI THE PROXY SYSTEM

The proxy system is of central importance to the attempts to revive corporate democracy in the United States of America. This is in part attributable to the fact that the use of proxies in listed companies is federally regulated, while corporation law in general is a matter of state jurisdiction, but there are other reasons too. The details of the proxy system in force in Australia have not been subjected to the same scrutiny and discussion.

Nevertheless, it is true in Australia, as in the United States of America, that the right to vote by proxy gives many shareholders of modern companies their only chance of being represented at the general meeting. The device is also significant because it constitutes a separation of ownership and control, albeit for a relatively short time. Managements can, and have been known to, use the device to entrench themselves more firmly in the seat of power.

It is true that management's normal role in activating the machinery of the general meeting, as discussed in the parts of this thesis dealing with convocation and notice requirements, would give management some influence over the decisions reached by the general meeting whether or not the proxy device was utilized. Nevertheless, it is the role of proxy holder which involves members of management in the corporate decision-making process most directly. Furthermore, the proxy system has the potential virtually to replace the company meeting as the method of corporate decision-making. It is, therefore, appropriate that the final section of this thesis should be devoted to an examination of the proxy system.

Not surprisingly, the live issues arising from proxy voting have changed over the years in Australia and Britain as well as in North America. Development in the United States has proceeded a step further than it has in either Australia or Britain, while the latter two countries have developed this law in step with each other. For the most part, as will be seen, the principles laid down in British decisions in this field, as in the other areas considered in this thesis, apply equally in Australia. Thus it is relevant to note that the first case to consider the use of proxies under modern company principles was decided by the English Court of Appeal in 1883. The point in issue in *Harben* v *Phillips*[1] was the necessity to comply with stipulated formalities in filling out the proxy form. In the course of deciding this point, the court had to come to grips with the broader issue of the source of the power to vote by proxy. It held that such a right did not exist independently of the contract constituted by the articles of association. A statutory right to vote by proxy has since been provided. Another significant English decision was handed down in 1907 when it was held in *Peel* v *London and Northwestern Railway Co*[2] that corporate funds could be used to send out proxy forms to the shareholders and to encourage them to return completed forms enabling management nominees to vote in their place. A recent Australian case which involved a consideration of proxy issues, *Re Marra Developments Ltd*[3], was decided by Wootten J of the New South Wales Supreme Court in 1976. Marra Developments, a large public company, whose share structure consisted of ordinary shares and redeemable preference shares, had been going through

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1. (1883) 23 Ch D 14.
2. [1907] Ch D 5.
3. (1976) 1 ACLR 470.

a period of financial difficulty which had led to major policy differences between members of the board of directors and certain shareholders. The dissident shareholders requisitioned an extraordinary general meeting and in connection with that meeting issued a summons for orders requiring the company to take certain steps in regard to the form of the notice of meeting and the form of the instrument of proxy. The issues which arose for consideration included the validity of nominating the chairman of the meeting as alternative proxy holder, the use of a two-way proxy, and the degree of discretion to be left to the proxy holder. The main points at stake in the case were, however, the clarity of identification of the issues put before the meeting and the definition of the test of disclosure.

The issues which arose in *Re Marra Developments Ltd* had not previously been considered in any reported case in Australia or Britain, but they had been considered in the United States. American concern with proxy issues may be traced back to the classic work of Berle and Means, *The Modern Corporation and Private Property*. In the course of discussing company control, these authors emphasised the role of the proxy machinery in entrenching management[4] and stated that "the proxy machine has...become one of the principal instruments not by which a stockholder exercises power over the management of the enterprise, but by which his power is separated from him"[5]. Within a space of three years after the publication of Berle and Means' book, Congress had passed a law which, for the purpose of furthering "fair corporate suffrage"[6], set

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4. Berle, A.A. and Means, G.C., *The Modern Corporation and Private Property*, (New York, The Macmillan Company, 1932) 86-88.
5. *Ibid*, 139.
6. HR Rep 1383, 73d Cong 2d Sess as quoted by Dean, A.H., "*Won Compliance with Proxy Regulations*" (1939) 24 Cornell LQ 483, 485.

up a Commission with power to make rules and regulations which must be observed by any person who chose to solicit proxies. The Commission in question has stated that the purpose of its rules is to prevent the dissemination of half truths, untruths and misleading information in the course of proxy solicitation[7], but its rules are not limited exclusively to matters of disclosure[8]. The question on which academic attention has focussed has been the possibility of using the proxy rules to open channels of communication and participation for the shareholders so that they may take a greater part in the affairs of their corporation. Thus, in the 1950's and the early 1970's. attention focussed on the definition of proper subject in the context of the shareholder proposal rule while at the present moment the issue is whether shareholders should be given a right to nominate candidates for directorships through the corporate proxy statement. One question which has not been considered in Australia, Britain or the United States but which has arisen in Canada is whether company managements should be required by statute to solicit proxies from their shareholders. An attempt will be made below to deal with all of these issues except disclosure. Disclosure requirements are dealt with under the heading of notice of meeting because Anglo-Australian courts, unlike their American counterparts, have traditionally grappled with the problems which arise in that light[9].

The writer would wish at this point to be able to assess the practical significance in the Australian context of the statutory provision for proxy voting rights. Unfortunately, Australian companies are not

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7. CCH Federal Securities Law Reports para 24.081.
8. Cohen, M.F., *"The SEC and Proxy Contests"* (1960) 20 Fed B J 91, 97.
9. Conard, A.F., *Corporations in Perspective*, (Mineola, Foundation Press Inc, 1976) 43, 45.

routinely required to report details of the exercise of such rights. Studies, such as those undertaken by Wheelwright[10] and Lawriwsky[11] of control patterns in Australian companies, have concerned themselves exclusively with share ownership data. As it has not been considered feasible to undertake original research on this question for the purposes of this thesis, all that can be said is that all companies listed on Australian Stock Exchanges have undertaken, in response to the listing requirements of the Associated Stock Exchanges[12] at the pain of being delisted, to solicit proxies from their shareholders when they issue notices of general meeting.

Because British laws in this regard closely parallel the Australian, statistics on the use of proxies there might bear some relationship to the situation that can be expected to pertain here. Midgley has published the results of an enquiry in which he was assisted by forty-five large British companies who replied to a questionnaire issued in 1969 covering the period 1960/61 to 1969/70 and seeking, *inter alia*, information on the use of proxies. It appeared that the individual company's procedure relating to proxy forms made a marked difference to the use of the device. In the most favourable circumstances, where the company provided reply paid cards or forms, up to twenty per cent of the shareholders might appoint a proxy, while when shareholders were left to their own initiative, "barely a handful", it was reported, submitted proxies. The percentage of votes represented by proxies rarely exceeded thirty per

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10. Wheelwright, E.L., *Ownership and Control of Australian Companies*, (Sydney, Law Book Co, 1957); Wheelwright, E.L. and Miskelly, J., *Anatomy of Australian Manufacturing Industry*, (Sydney, Law Book Co, 1967).

11. Lawriwsky, M., *Ownership and Control of Australian Corporations*, (Transcontinental Corporations Research Project, University of Sydney, 1978).

12. Formerly Associated Australian Stock Exchanges Listing Requirement 3.H.1, now 3.K.4.

cent of the possible votes and the level of opposition so recorded was minute[13]. Midgley generally concluded that the machinery of corporate democracy, including both proxy and other rights, was under-utilized[14], but inasmuch as a substantial shareholding is defined by law in some jurisdictions to be a holding of not less than one-tenth or ten per cent of all the shares of a class[15], it is suggested that a voting device by which votes representing more than ten per cent of the total possible votes were cast in forty-five per cent of the companies surveyed is not negligible.

In the United States the Securities and Exchange Commission produces an Annual Report in which statistics are given on all dealings which it has with proxy materials. The only figure not given here is the number of shareholders who return completed proxy forms. For the year 1976 it is reported that 6,898 proxy statements were filed. They related to 6,616 meetings and it is stated that 6,807 were filed with management groups

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13. Midgley, K., *"How Much Control Do Shareholders Exercise?"* (1974) 114 Lloyds Bank Rev 24, 31 sets out the following statistics:

Table 3 *Shareholders' use of proxy forms*

	Percentage of companies falling within each category	
	1969	1960-69
Percentage of proxy forms returned	%	%
Less than 16%	92	82
16 to 20%	8	14
Above 20%	Nil	4
Percentage of total possible votes in favour of resolutions		
Less than 11%	55	39
11 to 30%	35	50
Above 30%	10	11
Percentage of total possible votes against resolutions		
Less than 0.06%	83	70
0.06 to 0.2%	14	18
0.2 to 0.4%	3	6
Above 0.4%	Nil	6

14. *Ibid*, 34, 37.
15. Companies Act (Amendment) Act (NSW) No 61, 1971 s 3(d). Similar provisions are found in the Victorian Companies Act but not in the acts of other states.

while 9 were from non-management groups or individuals. It is suggested that the 9 is a misprint for 92. A total of 477 shareholder proposals submitted by 121 stockholders was included in the proxy materials of 242 companies while Commission staff agreed that 268 proposals submitted by 91 shareholders could be omitted by 122 companies. 18 proxy contests for the election of directors were fought, 15 of which involved control. In 2 of the 3 contests for representation alone, the minority secured such representation, while of the 15 contests for control, management retained control in 4 cases, negotiated settlements were arrived at in another 4 cases, in 2 cases management lost control and 5 contests were yet to be resolved when the year ended[16]. The number of proxy contests is equivalent to the number twenty years before[17], and inasmuch as there are now more companies subject to these provisions, it seems unlikely that such contests will ever be numerically significant. However, American commentators stress that the importance and effect of the proxy contest is not reflected by statistics, and point out that the possibility of facing such a contest will affect management attitudes and that the requirements of routine solicitations where no contest arises are even more significant in that they force management to account annually for their stewardship[18].

As yet no serious consideration has been given to proposals to adopt American-style proxy provisions in Australia. In the course of advising the Commonwealth Attorney-General on the desirable features of the

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16. 42 SEC Ann Rept, House Doc No 95 - 21, 95th Cong, 1st Sess (1976) 61.
17. Cohen, *op cit*, 108 reports 18 proxy contests were held in 1955, 20 in 1956, 20 in 1957, 34 in 1958 and 19 in 1959, although in every year but 1958 only 11 contests involved control.
18. *Ibid*, 109.

Corporations and Securities Industry Bill, an American advisor did recommend that the Commission which would be set up should have power to regulate the use and solicitation of proxies[19], but this suggestion was not adopted, apparently because the matter was considered one of internal management more appropriately dealt with by the National Companies Bill. However, that Bill as drafted merely proposed to adopt the provisions presently found in the Uniform Companies Act[20]. In a submission to the Senate Sub-committee on the Corporations and Securities Industry Bill, Baxt and Samuel noted that "there appears to be great resistance in this country to regulation along these lines" but stated that "the present English and Australian law in relation to proxy contests is quite unacceptable. The position is unduly weighted in favour of management"[21]. Mention might also be made of Hamilton's paper on the subject of proxy regulation in Australia delivered to the Australian University Law Schools Association Conference in 1978[22]. This thesis is unique in entering into a detailed discussion of the law as it exists presently and as it may be changed.

A. BASIS OF THE RIGHT TO VOTE BY PROXY

The statutory right to vote by proxy now conferred by the Australian and British legislation is of recent origin. The common law denied any right to vote by proxy and in these jurisdictions before 1948 proxy voting only existed under the authorization of the company articles.

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19. Senate Select Committee, *Report on the Corporations and Securities Industry Bill*, 1975 Official Hansard Report 362, hereinafter cited as *Sen Sel Comm Report*.
20. National Companies Draft Bill 1975 s 124.
21. *Sen Sel Comm Report, op cit*, 2746.
22. Hamilton, R., *Proxy Regulation in Australia*, (delivered at the AULSA Conference, Perth, 1978).

Before turning to a detailed study of the current law governing proxies, the historical background merits some attention for the light it can shed on the policy considerations related to the use of proxies.

1. ABSENCE OF COMMON LAW RIGHT

The common law rule denying a right to vote by proxy derived from an early rule concerning the rights of members in quasi public organizations, such as religious and municipal corporations, in which membership rights were accorded on a personal basis, not measured in regard to the member's financial interest in the body[23]. Two cases which exemplify the application of the rule to such corporations may be considered. In 1607 a dispute concerning a lease granted by a religious corporation was decided on the basis that the Dean had no power to act through a representative when the chapter convened to confirm the lease[24]. The common law on this point was held to agree with the canon law. In the light of the practice in the House of Lords which allowed a peer to give a proxy to a fellow member but not to an outsider, the fact that the Dean had chosen as his representative a stranger to the chapter was given some weight as an argument for invalidating his proxy[25].

The second case, *Attorney-General* v *Scott*, which was decided in 1749, considered the question of an election to a living which under a decree of the Lord Chancellor was entrusted to a body of twenty-five trustees. The number of trustees having been depleted, a deadlock arose. One faction in the dispute purported to meet to elect a candidate but among

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23. Getz, L., "*The Alberta Proxy Legislation*" (1970) 8 Alta L Rev 18, 19.
24. *Dean* v *Chapter of Fernes* (1607) Davis 42, 80 ER 529.
25. (1607) Davis 42, 47, 80 ER 529, 534.

other disqualifying factors was the fact that some of the faction were present only by proxy. The Lord Chancellor expressed the opinion, *obiter*, that although a proxy might be authorized to perform a merely ministerial act, the power to elect, which constituted a personal trust, could not be exercised by proxy. He further held that "the law presumes ...persons who meet to elect to act reasonably and that the reasons and arguments offered by one would influence the others and therefore the not giving an opportunity to meet avoids the election"[26]. It followed that the delegation in question was the more deplorable because it was accompanied by explicit instructions as to how to vote, since the trustee who gave such instructions had made his decision without hearing his fellows[27]. It is not suggested that this case has any direct relevance to the use of proxies in modern companies, indeed, the fact that the power to vote was there an incident of a trusteeship would in itself constitute sufficient ground for distinguishing the authority; however, the presumption stated is of interest.

In corporations where membership rights are regarded as personal privileges, the other members might expect a vote to be a reflection of the member's interest in the welfare of the general body influenced by that member's personal experience, and this would justify an objection to having this vote cast by an outsider. These objections lose their force when membership rights, as in the modern registered company with a share capital, are linked not to the member personally but to his financial interest in the company. The objection that a vote is meant to be influenced by the intelligence conveyed by the discussion that takes place at a meeting has no peculiar relevance to such corporations

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26. *Attorney-General* v *Scott* (1745) 1 Ves Sen 413, 417, 27 ER 1113.
27. (1745) 1 Ves Sen 413, 418, 27 ER 1113.

and is an argument that might equally be used against the recognition of proxy rights under the modern companies legislation. This point will be reverted to later.

2. RIGHTS CONFERRED BY THE ARTICLES

Many cases have affirmed the fact that the common law rule is applicable to joint stock companies[28], but it was equally well established under Anglo-Australian law, even before 1948, that the articles of association could confer a right on the shareholder to vote by proxy[29].

Provisions enabling the proprietors of a joint stock company to grant proxy rights were contained in the Joint Stock Companies Act, 1844 and the Companies Clauses Consolidation Act, 1845[30]. From 1856, when the modern division of the company constitution into articles and memorandum was introduced, until the enactment of the Companies Act, 1948, provision for the exercise of proxy rights was made in the articles scheduled to the Acts but no relevant provisions occurred in the body of any British or Australian Companies Act[31]. Whether it would have been open to the company to make provision for proxy representation in the absence of provisions in the articles attached to the companies acts clearly indicating that the legislature had no objection to such rights, is not a question which ever arose under Anglo-Australian law. There is, however, a New South Wales partnership case[32] in which certain purported

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28. *Harben* v *Phillips* (1882) 23 Ch D 14.
29. *Harben* v *Phillips* (1882) 23 Ch D 14; *Cousins* v *International Brick Co Ltd* (1931) 1 Ch D 86, 93 per Luxmoore J, 100 per Hanworth MR.
30. Joint Stock Companies Act (1844) 7 & 8 Vic c 110 s 26; Companies Clauses Consolidation Act (1845) 8 & 9 Vic c 16 s 76.
31. Joint Stock Companies Act (1856) 19 & 20 Vic c 42 First sched Table B regs 42 and 43; Joint Stock Companies Act (1862) 25 & 26 Vic c 89 First sched Table A regs 49-51; Companies Consolidation Act (1908) 8 Edw VII c 69 First sched Table A regs 60-67; Companies Act (1929) 19 & 20 Geo V c 23 First sched Table A regs 54-62.
32. *Sheldon* v *Phillips* (1894) 15 NSWLR (Eq) 98.

proxies were disallowed despite the presence of a clause in the partnership agreement allowing partners to vote by proxy. The basis of the decision was the lack of specificity in the document and procedure adopted. But in the course of his judgment Owen CJ in Eq remarked that the use of proxies in the partnership context was unprecedented and, noting that meetings of partners were more comparable to directors' meetings than shareholders' meetings because business was in fact transacted at the said partnership meeting, he held that, as directors were forbidden to vote by proxy, so great particularity should be required before a partner's right to do so was recognized[33]. There is American authority, considered below, suggesting that the courts will be slow to recognize proxy rights in the absence of permissive legislation and it is suggested that the same view could well have been taken in Australia.

Company law texts written before 1948 all mention the existence of provisions for proxy rights existing in the Table A articles but few of them give any indication how widespread the use of the provisions was. Steibel, however, states that "the articles almost always do contain such a provision"[34], while Topham goes further and explains the general practice by reference to the extreme inconvenience that would be occasioned members especially those living at a distance if they were obliged to attend every meeting personally[35]. An Australian writer further stated that it was common practice for directors' circulars to suggest that the chairman be appointed as proxy holder and to enclose a

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33. *Sheldon* v *Phillips* (1894) 15 NSWLR (Eq) 98, 104.
34. Steibel, A., *Company Law and Precedents*, 3rd ed (London, Sweet & Maxwell, 1926) vol 1, 245.
35. *Palmer's Company Law*, 17th ed (London, Stevens & Sons Ltd, 1942) 158.

printed and stamped proxy form together with a prepaid return envelope[36].

3. THE STATUTORY RIGHT

The statutory provision conferring the right to vote by proxy presently in force in Australia under the Uniform Companies Act, section 141, is closely related to that introduced into the English Companies Act in 1948[37] as a result of the Cohen Committee's recommendation[38]. No basis for the recommendation is given in the report but it is suggested that it rested on a general feeling that this was a right to which shareholders were entitled.

Both Tasmania and Victoria had adopted provisions granting shareholders a statutory right to vote by proxy before 1960[39], but New South Wales did not do so before the coming into force of the Uniform Companies Act[40].

Despite the close similarity of the British and the Australian provisions, there are some significant differences. The British provision, unlike that in the Uniform Companies Act, does not confer the right to vote by proxy upon members of companies not having a share capital. On the other hand, the Australian section qualifies the grant of statutory rights by stating that a member of a proprietary company shall not be entitled to exercise it unless provision is made in the articles or the leave of the court is obtained[41]. The British Act limits the rights of

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36. Sidey, R.L., *Companies, Formation, Management and Winding Up*, 4th ed (Sydney, Law Book Co, 1936) 262.
37. Companies Act, 1948 (UK) s 136.
38. Great Britain, Board of Trade, *Report of the Committee on Company Law Amendment*, Cmd 6659 (1945) para 133, hereinafter referred to as the *Cohen Report*.
39. Companies Act 1958 (Vic) s 117(5); Companies Act 1959 (Tas) s 103(6).
40. UCA s 141.
41. UCA s 141(2).

members of proprietary companies only by stipulating that such a shareholder may not appoint more than one proxy holder[42].

4. REGISTERED CLUBS IN NEW SOUTH WALES A SPECIAL CASE?

The New South Wales Registered Clubs Act, 1976, lays down certain provisions which will apply to any club organized for social, political, sporting or other purposes that seeks registration so as to be able to sell liquor on the premises. The relevance of this Act for the purposes of company law lies in the fact that such club must either be incorporated under the Companies Act or registered as a co-operative[43]. In 1978 the Registered Clubs Act was amended to provide that no person was to vote as a proxy at any meeting of the club or of a committee of the club or at any election of the club[44]. This provision would seem to conflict with the provisions of section 141(1)(a) of the Companies Act, which gives members of companies not having a share capital the right to appoint another member as his proxy. The conflict is resolved by virtue of section 30(3) of the Registered Clubs Act which provides that a rule referred to in sub-section 1 or 2 shall have effect notwithstanding the provisions of any other law. This does not quite dispose of the difficulty, however, as a club's elections will be affected directly by the question of whether the club's registration is current and valid. If registration has been obtained, section 30 would apply and use of proxies would be prohibited, but, if not, it appears that the Companies Act itself would apply and there would be a statutory right to vote by proxy. This situation is less than satisfactory but

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42. Companies Act, 1948 (UK) s 136(1)(a).
43. Registered Clubs Act, 1976 (NSW) s 10(1)(b).
44. Registered Clubs (Amendment) Act No 68, 1978, sched 3.

the more interesting question for our purposes is the rationale behind this change regarding the use of proxies.

The explanation for this revision of the proxy rules as they affect registered clubs may be found in the Report of Mr Justice Moffitt on *Allegations of Organized Crime in Clubs*[45]. It was found that certain abuses had occurred in such clubs as South Sydney Juniors, of which, in Moffitt J's opinion, there would have been little likelihood if the clubs had been more under member control[46]. Some registered clubs were found to be particularly vulnerable to being taken over wholly or partly by outsiders and it was reported that there was little to prevent a board, once there, from remaining in office by rigged elections, rigged proxies or miscounting the votes[47]. Although it was not part of the inquiry to examine club structures, it was recommended that procedures be made available to prevent the exploitation of clubs whose members were unable to protect themselves because of ballot rigging, the use of proxies or corrupt or standover methods[48].

During the course of debate on the amendment in the legislature, it was stated that because of the abuse of proxy voting in clubs over the past few years the Government is of the opinion that proxy voting should be abolished and that the club industry supported that opinion. The Honourable L.A. Solomons[49] commented that the Minister's explanation might have been a little trite. The requirement for proxies, he pointed out,

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45. New South Wales Royal Commission on Allegations of Organized Crime in Clubs, Report of the Hon Mr Justice Moffit, 1974.
46. *Ibid*, paras 159A and 193A.
47. *Ibid*, para 310.
48. *Ibid*, para 319.
49. NSW Parliamentary Debates, 45th Parl 2d Sess Thursday 16 March 1978, 13222.

arises in clubs with large memberships where, without proxies, not enough members would have a say in the management of the club. However, this objection was not pressed and no reply was elicited from the government.

The proxy solution is not the only, and perhaps not the most effective, way to make sure that members who cannot attend the meeting are not prevented from voting in club elections. With proxy voting prohibited, the possibilities of postal balloting or of setting up a polling booth at which members will vote over a prolonged period disassociated from the general meeting remain. However, the prohibition of proxy voting will not, by itself, eliminate any possibility of electoral abuse.

This amendment, as a provision restricting the appointment of non-members as proxy holders in companies without a share capital, is not peculiarly Australian. In fact it appears that in enacting a provision which would require such companies to allow non-members to exercise such a power in the first place Australia was unique. The British Companies Act does not grant any statutory right to vote by proxy to members of companies without share capitals[50]. This is also true of the North American enactments where, indeed, separate acts to govern business corporations are usually enacted[51]. The fact, therefore, that there are several American cases[52] standing for the proposition that the right of a proxy holder to choose a representative cannot be restricted

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50. Companies Act, 1948 (UK) s 136(1)(a).
51. See for example Corporations Act, RSO 1970 c 89 s 130(1)(c).
52. *State ex rel Syphyers* v *McCune* (1957) 101 SE 2d 834 (W Va SC); see also *In re Lighthall Manufacturing Co* (1888) 47 Hun 258 (NY SC); *People's Homes Savings Bank* v *Superior Court of San Francisco* (1894) 38 P 452 (Cal SC) as cited by Axe, L.H., *"Corporate Proxies"* (1942) 41 Mich L Rev 38, 51.

by the company's requirement that the proxy holder be a member of the company creats no contrast with the Australian provisions. The new Registered Clubs Act amendment has the effect of moving New South Wales closer to the British position, but it is suggested that it is anomalous to prohibit the use of proxies in such companies if they acquire the authority to serve liquor and to stipulate that similar companies that do not seek or acquire such authority must recognize such rights.

Although the abolition of proxy voting in registered clubs has been effected in New South Wales, there is no move to extend the provision to business companies. The grounds on which a distinction between these two kinds of organization is drawn include the differing nature of membership in the clubs from membership in a business organization. The government was motivated to effect this amendment by a desire to put the onus squarely on members of clubs to be present at meetings and to exercise the right to vote in person[53].

5. THE RIGHT TO VOTE BY PROXY IN NORTH AMERICA

Both Canada and the United States of America share the common law heritage which derives from British colonial background. This heritage is less influential in the field of company law, called corporation law in the United States, than in most other areas of the law. This is because of the recent origin of the joint stock company: the body of British law in this area for the most part post-dates the American Declaration of Independence and has only had persuasive influence over American decisions in rare instances. However, the common law rule against proxy

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53. NSW Parliamentary Debates, 45th Parl 2d Sess Wednesday 15 March 1978, 13091.

voting, originating, as has been seen, in an earlier period, is an exception to this general proposition.

American law in this area, therefore, started from the proposition that proxy voting was forbidden in shareholder meetings as in "all primary assemblies"[54]. Certain of the early American cases held that an express grant of statutory authority was necessary before a right to vote by proxy could be claimed, regardless of the existence of any contractual right under the corporate constitution. The argument was that the inherent corporate power to make by-laws did not encompass the power to make by-laws conferring the right to vote by proxy as such by-laws were not "essential nor even *apparently necessary* to carry into effect the objects for which corporations are generally created"[55]. A right to vote by proxy might serve the members' convenience but would not, it was held, promote the company's interest or the public good; indeed, such a right might work against these interests inasmuch as "if one member may appear and vote by proxy, then all may and so the welfare and interest of the company and of the public be utterly neglected"[56]. However, even at this stage the disapproval of proxy voting was by no means universal[57].

Today, state corporation laws in all jurisdictions stipulate that a shareholder may vote either in person or by proxy[58]. In addition, the

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54. *Taylor* v *Griswold* (1834) 14 NJLR 222, 226-227; see also *Robbins* v *Beatty* (1954) 67 NW 2d 12 (Iowa SC); *Dal Trans Service Co* v *Fifth Avenue Coachlines Inc* (1961) 220 NYS 2d 549 (NY SC) apl gr 11 NY 2d 679, 180 NE 2d 997.
55. *Taylor* v *Griswold* (1834) 14 NJLR 222, 228.
56. *Ibid*, 229.
57. Axe, *op cit*, 42-46 citing *State ex rel Kilbourne* v *Tudor* (1812) 5 Day 329 (Conn SC); *McKee* v *Home Savings and Trust Co* (1904) 98 NW 609 (Iowa SC); see also *Rossing* v *State Bank of Bode* (1917) 165 NW 254 (Iowa SC).
58. Mod Bus Corp Act Ann 2d ed s 33 para 3, for summary of distinctions between state provisions

Securities and Exchange Commission, acting under the authority of the Securities Exchange Act section 14a, enacted in 1934, has promulgated a code of regulations to govern the process of proxy solicitation. This system of regulation was introduced because the widespread use of proxy voting, under state corporation laws which contained few if any disclosure requirements, was seen to be resulting in the abuse of managerial responsibility[59]. Some of the provisions of the Securities and Exchange Commission's code will be considered below, but inasmuch as certain features of it are closely comparable with Anglo-Australian provisions considered elsewhere in this thesis, such as, for example, notice requirements, no comprehensive treatment of this regime is attempted here.

The Securities and Exchange Commission rules do not make the solicitation of proxies mandatory. However, those companies to which the rules apply[60] are required to furnish certain information to their stockholders whether or not they solicit proxies. Furthermore, it is a listing requirement of the Stock Exchange that proxies should be solicited[61].

In Canada, following the recommendations of the Kimber Report[62], which was submitted to the Ontario legislature in 1965, many Canadian

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59. Aranow, E.R. and Einhorn, H.A., *Proxy Contests for Corporate Control*, 2nd ed (New York, Columbia University Press, 1968) 89.
60. By section 12(g) of the Securities Exchange Act, 1934 as amended in 1964, companies with total assets exceeding $1 million and a class of equity securities held of record by 500 or more persons are required to register those securities with the Commission even if their securities are not traded on an Exchange. Upon registration, the reporting and other disclosure requirements of the Act will apply to these companies: US Congress, *Securities and Exchange Commission Annual Report 1976*, 61; see also Aranow and Einhorn, *op cit*, 95.
61. Conard, *op cit*, 63-65.
62. Ontario, *Report of the Attorney-General's Committee on Securities Legislation*, March 1965, hereinafter referred to as the *Kimber Report*.

jurisdictions have adopted provisions[63] embodying a comprehensive set of requirements governing proxy voting which are to a large extent modelled on the American Securities and Exchange Commission rules[64]. In all of these provinces except British Columbia[65], a statutory right to vote by proxy is granted to shareholders in all companies limited by shares, regardless of size. In the discussion which follows, reference will be made exclusively to the legislation adopted in Ontario and by the federal parliament. These enactments have been chosen because together they are representative of the form this legislation has taken.

6. JUSTIFICATION OF PROXY RIGHTS

The history of proxy voting rights has been canvassed with a view to discovering not only the present basis of such rights but also the arguments which have been advanced for and against the recognition of such rights. Against this background the writer will now attempt to answer the question: Should proxy voting rights be abolished?

In answering this question it is necessary to draw a distinction between business companies, that is, companies organized to seek profit which are typically limited by shares, and non-profit organizations formed to further social, political or other aims, which are usually limited by guarantee. In New South Wales, as has been seen, proxy voting in one

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63. Can Bus Corp Act ss 141-148; Bus Corp Act (Ont) ss 115-121; Companies Act, RSA 1970 (Alta) c 60 ss 137-144; Companies Act, SBC 1973 (BC) c 18 ss 173-180; Companies Act RSM 1970 (Man) c 160 ss 97-103.
64. Iaccobucci, F., Pilkington, M.L. and Pritchard, J.R.S., *Canadian Business Corporations*, (Agincourt, Canada Law Book Ltd, 1977) 182.
65. Companies Act, SBC 1973 (BC) c 18 s 173; see Getz, *op cit*, 24, n 60.

type of social "company", the registered club, is now forbidden. It is suggested that the use of proxies should be forbidden in all companies in which membership is based not on the financial contribution which the member has made to the company but on personal acceptance of the member as an individual.

If it is accepted that a distinction should be drawn between various types of company with share capitals on the basis of size[66], the distinction is relevant to the question of the right to use proxies. The use of proxies in a domestic company may threaten to disrupt the personal relationship among members which is the distinguishing feature of such companies. On the other hand, in a large "endocratic" company such as those listed on a Stock Exchange, there is no close personal relationship between the members, and the number of the shareholders and their geographical dispersion clearly make it impossible to convene a meeting at which each shareholder will be present in person. In such circumstances some device to allow absentee voting is necessary. It is suggested that the proxy device is preferable to such devices as postal voting in that it allows a greater degree of flexibility and in particular in that it does not totally displace the meeting as a place where negotiations may take place and questions may be raised. Where the proxy device is used, management continues to come face to face with at least a handful of shareholders, but where postal balloting is used such a meeting is even less important.

In the smaller proprietary company, the decision as to whether or not proxy rights should be allowed is more complicated. There may be a fairly large personal facet to membership of such a company and thus

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66. See above, Part I.

the argument that other shareholders are entitled to demand that the shareholder exercise his personal judgment is not automatically displaced. Further, it is clearly a physical possibility to convene a meeting with all shareholders in attendance. However, where the shareholders themselves decide that they wish to make provision for proxy voting, there are no grounds on which to dispute that decision. The common law has traditionally taken the view that a man is free to neglect his own property, and as shares are regarded purely and simply as property it cannot be argued that, as a principle of law, a member in such a company has undertaken a personal responsibility to the company. There is a growing tendency to leave the administrative details of such a company to be settled by contractual negotiation among the members and this principle should continue to be applied to the field of proxy rights.

B. PROXY VOTING IN AUSTRALIA

1. GOVERNING PROVISIONS

Before examining the practical aspects of the proxy system in effect in New South Wales, it would be as well to define the relevance of company articles and stock exchange requirements in controlling the exercise of a statutory right. When the right to vote by proxy was founded on the contract contained in the articles there could be no doubt that the company had the power to make the right to vote by proxy subject to conditions[67]. Stipulations as to the form which the proxy should take

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67. *Harben* v *Phillips* (1882) 23 Ch D 14.

and the time at which it should be lodged were standard while other restrictions were not uncommon. All these restrictions could effectively increase the voting power available to management[68], for example, where it was stipulated that the proxy holder should be a member of the company the shareowner might be forced to appoint a member of management as his proxy holder because he knew no other members. Has the fact that there is a statutory right to vote by proxy affected the company's power to impose conditions on that right?

Where the statute specifically provides that, for example, a proxy holder may be a non-member, it is apparent that the articles cannot negate this stipulation, but in other cases the company may have power to demand compliance with specific regulations. Discussing the requirement that proxies be lodged before the meeting, where the requirement in the articles was not in direct conflict with the statute, it was held that non-compliance with that requirement would invalidate the vote but the point was *obiter* only[69]. There is direct statutory authority[70] allowing the company to impose such a condition within certain limits. Nevertheless, the decision suggests that the company does have power to make regulations controlling the exercise of the statutory right. A 1969 decision settles the point definitively. The statutory right, it was held, "is, of course, subject to regulation by the terms of the company's articles, but the regulatory effect of the articles cannot be permitted to frustrate the statutory right of a shareholder"[71].

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68. Getz, *op cit*, 19-26.
69. *Armstrong* v *Landmark Corporation Ltd* (1966) 85 WN (Pt 1) (NSW) 328, 329.
70. UCA s 139(1)(c).
71. *Industrial Equity Ltd* v *New Redhead Estate and Coal Co Ltd* [1969] 1 NSWLR 563.

In *Coachcraft Ltd* v *S.V.P. Fruit Co Ltd*[72], the question arose as to whether the company articles invalidated certain proxies. The plaintiff argued, *inter alia*, that section 141(1) would operate to prevent such an invalidation. The facts were that the articles in question limited the number of shares which could be held by any member. In an attempt to circumvent this limitation, the plaintiff, who had purchased shares far in excess of the stipulated number, made it a condition of the contract of sale that the vendor execute a power of attorney in respect of the shares. The chairman of an extraordinary general meeting refused to allow these powers of attorney to be used to vote the shares. The court held that the relevant article contained an implication that a shareholder could not by the granting of such an authority achieve indirectly as against the company what he could not achieve directly. In response to the argument founded on section 141 it was held that the section conferred a statutory right on every member of a company to attend and vote by proxy, which right may be regulated but not frustrated by a company's articles, but that this left open the question of whether the member had validly appointed a proxy. It was further held that in the circumstances, the shareholders had failed to exercise their entitlement to appoint proxies[73].

Some light is cast on the problem of the company's right to make regulations affecting the exercise of the statutory right by two Canadian cases[74] decided under a statute which expressly empowered the directors to make such regulations. In these circumstances it was held that regulations enacted by the general meeting would be invalid but it was

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72. (1978) 3 ACLR 658.
73. (1978) 3 ACLR 658, 677.
74. *Kelly* v *Electrical Construction Co* (1907) 16 OLR 232; *Colonial Assurance Co* v *Smith* (1912) 4 DLR 13.

suggested that in the absence of express stipulation the general meeting would have had the power in question. The general meeting is empowered by the statute to adopt articles or regulations governing the internal workings of the company and as the use of proxies falls within this area, it must therefore be regarded as capable of regulation by the company.

The right to regulate is not equivalent to a right to prohibit, and it cannot be doubted that our courts would be quick to invalidate regulations which infringed the statutory right to vote by proxy. It is not necessary to discuss the American authorities for this proposition[75].

A question may arise when considering any regulation contained in the company's articles as to whether the clause imposes a requirement and is mandatory or merely indicates the preferred procedure and is directory. This question does not arise exclusively in circumstances where there is a statutory right to vote by proxy. Two cases in which the question was considered in regard to a contractual right to vote by proxy may be referred to. In *Harben* v *Phillips* the court held that the article in question was imperative, that a special power was conferred and so the accompanying conditions must be duly observed[76]; the decision, however, was determined by construction of the article in question. On the other hand, in *Isaacs* v *Chapman*[77] the article was held to be merely directory although the wording of the article in question was mandatory. The

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75. See *Clark* v *Wild* (1911) 81 A 536 (Ver SC); *Brooks* v *State ex rel Richards* (1911) 79 A 790 (Del SC); *State ex rel Lally* v *Cadigan* (1918) 174 P 965 (Wash SC) as cited by Axe, *op cit*, 49-50.
76. *Harben* v *Phillips* (1882) 23 Ch D 14, 22 per Chitty J, 32 per Cotton LJ: "Where parties have a right depending on the contract between them and other parties, there, in my opinion, all the requisitions of the contract as to the exercise of the right must be followed."
77. (1919) 32 TLR 183.

court was assisted in reaching this decision by the fact that the long-established usage in the company contravened the direction in the article[78]. It is suggested that the courts would be more ready to hold that an article regulating the exercise of a statutory right was merely directory than they were to come to the same conclusion regarding an article regulating the exercise of mere contractual right, and that any regulation that threatened to interfere unduly with this right would therefore be read as merely directory.

Before leaving this topic, the relevance of the Stock Exchange Listing Requirements should be explained. Any company that seeks or obtains listing on an Australian stock exchange gives an undertaking in the course of the application that it will comply with the listing requirements. If it fails to comply, the stock exchange obtains a contractual right to suspend and in the last resort to delist shares[79]. Inasmuch as the directors of listed companies do not like the stigma of having their securities suspended and that such suspension will adversely affect the transfer ability and therefore the value of the company's securities, this sanction has been found effective. The listing requirements applicable to proxies take two forms, that is, they both require the company's articles to contain certain stipulations and require that the company issue proxy forms with the annual report. Where the company fails to comply with these requirements, the individual shareholder does not, for that reason, acquire a cause of action against the company. The shareholder is not privy to the contract between the company and the stock exchange. Nevertheless, in a recent

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78. See also *Bombay Trading Corp* v *Dorabji Cursetji Shroff* [1905] AC 213.
79. This was explained to the Senate Select Committee on the Corporations and Securities Industry, *Sen Sel Comm Report, op cit,* 154-157.

New South Wales case in which shareholders complained that management was failing to comply with the articles governing the use of proxies, the court referred to the Stock Exchange Listing Requirements as an aid in construing those articles[80].

2. THE PROXY MACHINERY EXAMINED

The proxy machinery of an Australian company must be framed to accord with the Companies Act and public listed companies can be expected to meet the requirements of the Stock Exchange Listing Requirements. Within this framework, details will be determined by the company's articles. The writer now proposes to examine the details of this machinery and for the purposes of this examination it will be assumed that the Table A articles contained in the Fourth Schedule of the Uniform Companies Act apply.

(a) Statement of Proxy Rights

An Australian public company is required to include in every notice calling a meeting of the company a statement outlining the proxy rights which are conferred by the statute[81]; moreover, this statement must be accorded reasonable prominence. If default is made in complying with this provision, every officer of the company shall be guilty of an offence against the Act, but no penalty is provided for this offence. The Stock Exchange Listing Requirements go further and require public companies to send out proxy forms with the notices of meeting[82].

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80. *Re Marra Developments Ltd* (1976) 1 ACLR 470.
81. UCA s 141(3).
82. Associated Australian Stock Exchanges Listing Requirement formerly s 3.H.1, now 3.K.4.

Companies which comply with this requirement are engaging in the solicitation of proxies and this topic will be discussed below[83]. For the moment it should be sufficient to note that the Australian statutory requirement, while parallel to the British requirement[84], is elementary compared with the requirements imposed by Canadian statutes.

(b) Eligibility of Proxy Holder

If a shareholder decides that he would like to appoint someone to hold his proxy at a meeting of his company, he must select an eligible person. Such a person, as any candidate for legal power, must be both sane and adult and must be under no other disqualification. This granted, the only concern of the law is with the relationship between the prospective proxy holder and the company. The shareholder is free to choose as proxy holder a person who is his relative, friend, or a person who is a stranger to him.

The question of whether the proxy holder must be a member of the company in his own right was the point at issue in several cases[85], but is now answered by statute. Non-members may, under the terms of the Australian Companies Acts, act as proxy holders at meetings of companies having a share capital. At meetings of companies not having a share capital non-members may not act as proxy holders unless so authorized by a provision in the company's articles. The stipulation as to companies not having a share capital was added to the Companies Acts by an

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83. See below, 370-377.
84. Companies Act, 1948 (UK) s 136(2).
85. *In re Madras Irrigation and Canal Co* (1881) WN 120; followed by *Re Central Bahia Rail Co* (1902) 18 TLR 603; distinguished by *Re General Mortgage Society (Great Britain) Ltd* [1942] Ch 274.

amendment in 1971[86].

The amendment has been explained as resulting from difficulties experienced by incorporated clubs. Access of non-members to club premises was restricted by the liquor laws and the members of these clubs resented the presence of non-members at club meetings[87]. The right to vote by proxy in such clubs has recently been abolished in New South Wales and it has been suggested by the writer that the right to vote by proxy at meetings of all companies without share capitals be abolished[88]. If this is done, the restriction in question will be otiose and can be written out of the statute.

No question has ever arisen as to whether a shareholder may appoint as his proxy holder an officer of the company. Indeed, officers such as the company secretary and the chairman of the board of directors are frequently nominated as proxy holder in the proxy forms circulated by the company[89]. It would be extremely unrealistic to expect the courts to sustain an objection to the practice at this point of time, but it may be desirable to consider amending the statute to outlaw such a practice. Company officers will often have an interest in the decision that is to be taken at the meeting for which the proxies are given and inasmuch as the proxy holder retains under the law as it stands a discretion as to whether to use the proxy or not and how to cast these votes, it might be better if some disinterested party could be found to undertake the task. The fact that company proxy materials commonly nominate such officials may be explained by motives of convenience. It

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86. Companies Act (Amendment) Act, 1971 (NSW) no 61 s 17(f); Vic Act No 8185 s 43(1)(h).

87. CCH Corporate Affairs Reporter s 9320.

88. See above, 331-334.

89. See for example *Re John O'Brien Consolidated Industries Pty Ltd* (1975) 1 ACLR 311; *Re Marra Developments Ltd* (1976) 1 ACLR 470.

is known in advance that these officials will be at the meeting whereas there may be doubts as to the attendance of any other individual, but this difficulty is far from being insuperable.

One way in which this difficulty may be overcome is by appointing a public official whose duty will be to accept and exercise proxy votes at any company meeting held within the jurisdiction[90]. This suggestion would also serve to a large extent to obviate any difficulty in ensuring the independence of the nominee. However, before such a suggestion is adopted, it is necessary to consider whether or not the intention of the shareholders returning such proxies is not in fact to give the company management a blanket endorsement. This question is discussed below under the sub-heading "Unmarked Proxies".

(c) The Proxy Form

Once the shareholder has decided that he will exercise his right to appoint a proxy and has chosen his proxy holder, he must embody his decision in a document so framed that the company will honour it.

It is usually possible to obtain a printed proxy form from the company's secretary, but use of such a form is not mandatory. The shareholder may prepare his own form and in so doing is not bound by any statutory requirements as to the content or language of the proxy form. The Table A articles provide a model proxy form which exhibits below the signature a statement that affords the member an opportunity to instruct the proxy holder to vote for or against a resolution with a note stipulating that

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90. Similar suggestions have been made in France: see De Hogton, C.(ed), *The Company: Law, Structure and Reform in Eleven Countries*, (London, PEP, 1970) 187. The practice in Germany is that the executive body of the corporation does not solicit proxies or act as proxy holder, rather, proxies are commonly entrusted to the banks: see Grossfield, B., "Management and Control of Marketable Share Companies" in *International Encyclopedia of Comparative Law*, vol XIII c 4, 98-99.

unless otherwise instructed the proxy holder may vote as he thinks fit[91]. It is not clear why this statement appears below the signature in the model. One explanation may be that such a feature is optional and would be expected to appear above the signature if adopted. However, there is another possible explanation, to wit, that such an instruction is not considered an integral part of the authorization and that even where the option is exercised nothing would prevent the company from honouring a vote cast by proxy in contravention of the instruction. The limitation on authority would be considered a matter strictly between the shareowner and the proxy holder. It is suggested that the model form be altered to include the "two-way" feature above the signature.

The Stock Exchange Listing Requirements are relevant in that section 1.B.23 provides that the articles of all companies subject to the requirement must provide that "shareholders shall be given an opportunity to vote by proxy for or against any resolution submitted to a meeting of the company". This may be construed to mean that the proxy holder must be allowed to vote yea or nay but seems clearly to have been intended to mean that the shareholder must be given an opportunity to instruct his proxy holder that he must vote for or against the resolution. The ambiguity does not exist in section 3.H.1, now section 3.K.4, which requires companies to send out proxy forms which enable shareholders to vote for or against any resolution. When called upon to interpret an article which had adopted the wording of section 1.B.23, Wootten J recommended that the article be amended to remove the ambiguity but required that shareholders be given an opportunity to issue instructions to their proxy holders by the use of a proxy form which contained a "two-way" feature[92].

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91. UCA Fourth sched Table A reg 60.
92. *Re Marra Developments Ltd* (1976) 1 ACLR 470, 476.

The articles appended to the British Companies Act contain two model proxy forms, one a two-way form offering the opportunity outlined above[93], the other merely appointing a proxy holder stipulating no limits as to his authority on its face[94]. In both the British and the Australian articles, the model forms are introduced by the direction that "the instrument is to be in the following form or a form as near thereto as circumstances admit". It follows that the use of such a form is not mandatory.

The Canadian federal legislation, like the Ontario provincial enactment, draws a distinction when laying down requirements as to the form of proxy between a proxy that has been solicited and one that represents an exercise of the shareholder's initiative. In the latter case there is no necessity to use a prescribed form, while in the former use of such a form is mandatory[95].

In drawing a distinction as to the required proxy form between solicited and unsolicited proxies, the Canadian legislation follows the example set by the United States of America. The state statutes do not require any particular words to create a valid proxy instrument as long as the language used clearly indicates the creation of an agency relationship by which the proxy holder is empowered to exercise the voting rights of the stock held on record by the proxy giver[96]. However, if the solicitation of proxies is subject to the Securities and Exchange Commission proxy rules, then the proxy form must meet a number of requirements[97].

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93. Companies Act, 1948 (UK) First sched Table A reg 71.
94. *Ibid*, reg 70.
95. Compare Can Bus Corp Act s 142 with s 143; see also Aranow and Einhorn, *op cit*, 416.
96. Aranow and Einhorn, *op cit*, 160, 161; Mod Bus Corp Act Ann 2d s 33 third para, para 4.04 citing *Atterbury* v *Consolidated Copper Mines Corp* (1941) 20 A 2d 743 (Del Ch); *Smith* v *San Francisco & NP Railway* (1897) 47 P 582 (Cal SC); *Gentry-Futch* v *Gentry* (1925) 106 So 473 (Fla SC).
97. CFR s 240.14a-4; see also Aranow and Einhorn, *op cit*, 160-178.

Australian Stock Exchange requirements stipulate that proxy forms circulated by the company are to be blank "so far as the person primarily to be appointed is concerned"[98], but the practice of nominating an alternative or substitute proxy holder is commonly followed. Where the shareholder signs and returns such a form without filling in the blank left for the name of the primary appointee, the proxy will be valid. The practice of circulating proxy forms with the names of alternative proxy holders filled in is recognized as conferring an advantage on the incumbent management but the listing requirement has been hailed as a welcome fetter on the previous practice of sending out proxies made out primarily in favour of the directors[99]. In taking cognizance of this practice the courts are beginning to come to grips with the problem of proxy solicitation and the reader is referred to Section C below for a further treatment of it, but it may be noted in passing that the Securities and Exchange Commission proxy rules do not forbid the prepared form from nominating the proxy holder.

(d) Execution of the Proxy

The body of the Companies Acts lays down no requirements as to the manner of execution of the proxy form but the Table A articles provide that "the instrument appointing a proxy shall be in writing (in the common or usual form) under the hand of the appointor or of his attorney

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98. Formerly Associated Australian Stock Exchanges Listing Requirement s 3.H.1, now 3.K.4.

99. *Re Marra Developments Ltd* (1976) 1 ACLR 470, 476; see also *Garvie* v *Axmith* (1962) 61 DLR 2d 65 in which Spence J held that circulating proxy forms with the names of appointees already filled in, without supplying blank forms in addition, was not good corporate practice but that it was not sufficient to invalidate the votes of a large number of shareholders who had given such proxies.

duly authorized in writing"[100]. Provision is also made for an execution procedure where the appointee is a corporation.

The prime objective recognized by the courts and aimed at by the articles of association in laying down requirements as to execution of the proxy form is to ensure the production of acceptable evidence that the shareowner has expressed an intention to register his vote by the agency of a particular representative. Where the shareholder can be deemed to have so evidenced his intention, a court concerned with a statutory right to vote by proxy would be unlikely to hold that formal requirements as to execution need be observed. Thus, although proxies were once invalidated because of faulty compliance with attestation requirements[101], such requirements, while not unthinkable, are not common today and are not included in the Table A articles. It might well be that if such a requirement were to be imposed it would be held to be an infringement on the statutory right[102]. Cases in which the American courts have taken a relaxed approach to formal execution requirements include cases in which it has been held that a proxy signed by means of a rubber stamp[103] was valid as well as cases holding that a shareholder may authorize a third party to sign his name to a proxy[104]. Australian courts may be expected to adopt a similar attitude when such questions arise. As proof of this, it is established

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100. UCA Fourth sched Table A reg 59.
101. *In re Parrott, ex parte Cullen* [1891] 2 QB 131; *Harben* v *Phillips* (1882) 23 Ch D 14.
102. See above, 330-331.
103. *Schott* v *Climax Molybdenum Co* (1959) 154 A 2d 22 (Del Ch) as cited by Aranow and Einhorn, *op cit*, 424.
104. *Standard Power & Light Corp* v *Investment Associates Inc* (1947) 51 A 2d 572, 580 (Del SC) as cited *idem* but on the general point see, *contra*, *Schilling* v *Car Lighting & Power Co* (1922) 289 F 488 (SD NY) as cited *idem* 417, where it is noted that the holding was criticized by Axe, *op cit*, 56.

law that the fact that a blank was left in the proxy form will not invalidate it. The proxy holder will be deemed to have authority to fill up such a blank[105], a liberty that would invalidate a more formal document.

(e) Lodging the Proxy Form

There is no statutory requirement that proxy instruments should be pre-lodged, but it is left open to the company to require pre-lodgment subject to the provision that any requirement that they be lodged with the company more than forty-eight hours before the meeting will be void[106]. That such a requirement is administratively convenient in that it allows the company to make provision for controlling admission to the meeting and to balloting as well as giving the company, through its officers, time to determine the validity of the instrument, is obvious.

Aranow and Einhorn, however, report that as soon as proxies are filed it becomes possible for management to ascertain the strength of the opposition and that management may then undertake last-minute efforts to secure additional votes in support of its proposals[107]. The suggested solution to such difficulties is an agreement between contesting factions specifying that all proxies will be filed at the same time and that after such initial filing no further proxies will be accepted[108]. In the United States, proxies are not generally required

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105. *In re Lancaster, ex parte Lancaster* (1877) 5 Ch D 911.
106. UCA s 139(1)(c).
107. Aranow and Einhorn, *op cit*, 309.
108. *Ibid*, 311.

to be filed before the commencement of the meeting[109], and Aranow and Einhorn express the opinion that such a requirement would be unfair and unreasonable to the insurgents except under special circumstances inasmuch as it would threaten to effectively disenfranchise a number of stockholders as well as shortening the time available to the insurgents to conduct their solicitation[110].

Nevertheless, it is considered that the provisions contained in the Australian articles are unobjectionable so long as their enforcement is even-handed. Some method of ensuring that management is not voting proxies lodged after the deadline is, of course, necessary, but such an assurance is commonly found in the involvement of an independent firm of auditors in company meeting procedures. While such a provision does serve to put a time limit on efforts to contact absent shareholders and obtain their proxies, by the same token it prevents such a deterioration of the company meetings as is described by Gilbert in his account of the Sparks-Withington proxy contest which was prolonged for hours while last-minute efforts to obtain more proxies continued[111]. It may be noted that provisions requiring pre-lodgment of proxies have been enforced as mandatory by the New South Wales Supreme Court[112].

Articles such as regulation 61 of Table A, which specifies that proxy instruments must be deposited with the company not less than forty-eight hours before the meeting, frequently contain stipulations allowing fresh proxies to be lodged before an adjourned meeting reconvenes. In the

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109. The British and Canadian provisions parallel the Australian: see Companies Act, 1948 (UK) s 136(3); Can Bus Corp Act s 142(5); Bus Corp Act (Ont) s 116(5).

110. Aranow and Einhorn, *op cit*, 310-311.

111. Gilbert, L.D., *Dividends and Democracy*, (Larchmont, American Research Council, 1956) 175-180.

112. *Armstrong* v *Landmark Corporation Ltd* (1966) 85 WN (Pt 1) (NSW) 328, 329 as discussed above, 340.

absence of such provisions, proxies intended for use at an adjourned meeting must be deposited in time for use at the original meeting[113]. Where such provisions do exist, the question may arise whether the continued meeting was in fact adjourned[114], but these questions are outside the scope of this paper.

(f) Inspection of Proxy Instruments

Proxy instruments are routinely inspected by the executive officers of the meeting. Indeed, it has been noted above that one reason why pre-lodgment is required is to facilitate such inspection. The purpose of such inspection is to take reasonable precautions to ensure that those who vote are entitled to do so. This inspection is in the ordinary course carried out by the secretary or the auditor of the company during the period of time immediately preceding the meeting at the direction of the chairman of the board of directors given in his capacity as the chairman of the general meeting. Doubtful instruments are referred to the chairman of the general meeting for his decision as to their validity or otherwise[115].

Although these procedures are logical necessities and are commonly followed, there are no statutory directions requiring that they be followed nor are there any relevant provisions in the Table A articles or the Stock Exchange Listing Requirements. If there is a duty to ensure that such procedures are followed, it is a duty which is imported from the common law. Every meeting needs to have a chairman, a person

113. *McLaren* v *Thomson* [1917] 2 Ch 261.
114. *Jackson* v *Hamlyn* [1953] 1 Ch 577.
115. See for example *Armstrong* v *Landmark Corporation Ltd* (1966) 85 WN (Pt 1) (NSW) 238; see also Horsley, M.G., *Meetings, Procedure, Law and Practice*, (Sydney, Butterworths, 1978) 152, 170.

whose basic function is to superintend all aspects of the meeting, exercise control as needed and generally enable those present to fulfil the function and purpose of the meeting in an orderly and lawful fashion[116]. Company articles recognize this necessity and provide for the election or appointment of a person to discharge these duties. Because the meeting will function more smoothly if advance preparations are made, the provision found in the Table A articles to the effect that the chairman of the board of directors should preside at the general meeting[117] is commonly adopted. The chairman, however, must look to common law and traditional usage for guidance as to the extent and scope of his rights and duties. It was originally intended to undertake in the course of this thesis an extensive examination of chairman's duties. This intention has been abandoned due, not to disinterest, but to limitations of time and space. For the purposes of this section of the paper it is sufficient to reiterate that an official of the company at the instigation of the chairman will check the proxy documents to ensure that they satisfy the various requirements laid down by the statute and the company articles[118].

Inasmuch as usage supplies the lack of specific provisions demanding that these functions be carried out, it may be necessary to remedy this defect in the relevant provisions. In any event, action should be taken to allow for an independent check on these procedures. Aranow and Einhorn state that in the United States it is customary for management to recognize that the opposition is entitled to have representatives and scrutineers present during the count of proxies[119].

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116. *Colorado Constructions Pty Ltd* v *Platus* [1966] 2 NSWR 598 as cited by Horsley, *op cit*, 149.
117. UCA Fourth sched Table A reg 32.
118. Horsley, *op cit*, 127.
119. Aranow and Einhorn, *op cit*, 372.

This right was recently claimed by a shareholder and director in a New South Wales company. It was held that each shareholder of the company is entitled to have the articles faithfully observed in relation, in particular, to the regulation of the right to cast votes at meetings. Further, it was held that it fell properly within the province of any director of a company to interest himself in the question of whether those rights are being recognized or are being repudiated and that, accordingly, an individual director has the right to inspect such documents as may cast light upon this question[120]. In other words, it was held that the directors' common law right to inspect the company's documents[121] extended to the inspection of proxies. However, Street J refused to order the defendant company to allow the dissident shareholder-director to be present while the management check of proxies was being carried out as this, he felt, would impose an unreasonable burden on the auditors. Further, he held that it would be unreasonable to expect the management checking procedure to be completed early enough to allow the plaintiff to exercise his right of inspection before the meeting and accordingly he ordered the defendant company to make the proxies available for inspection after the conclusion of the annual general meeting[122]. In these circumstances the right of inspection appears to be virtually useless.

If a right of inspection is to be meaningful, it must be open to the shareholder or director who claims it to object to management decisions as to the validity or otherwise of certain proxies. However, under the

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120. *Armstrong* v *Landmark Corporation Ltd* (1966) 85 WN (Pt 1) (NSW) 238.
121. See *Conway* v *Petronius Clothing Co* [1978] 1 WLR 72; *Edman* v *Ross* (1922) 22 SR (NSW) 351.
122. *Armstrong* v *Landmark Corporation Ltd* (1966) 85 WN (Pt 1) (NSW) 238.

provision in the Table A articles to the effect that no objection shall be raised to the qualification of any voter except at the meeting[123], such an objection will not be entertained if made after the meeting itself[124]. It does not appear from the judgment discussed above whether or not such a regulation did appear in the articles of the company concerned, but equally Street J did not refer to any possible action to be taken as a result of the inspection. In a later case, however, it was recognized that if those opposing the incumbent management were denied an opportunity to see the proxies before the meeting, it must be open to them to challenge the validity of the votes cast at that meeting in subsequent judicial proceedings despite the existence of such an article[125]. As the policy informing the article in question, that of making the decision of the meeting conclusive, is to be supported, it would be preferable to allow the claimant to inspect the instruments of proxy before the meeting is adjourned. In fact, it is the writer's opinion that the best course would be to allow a member who claims this right to be present during the management's inspection and it is suggested that legislation providing for such a right should be introduced in Australia even though this has not been done elsewhere.

(g) Joint Authority

A shareholder in a company having a share capital may appoint two proxy holders but no more[126]. If more than one proxy holder is appointed it will be necessary for the shareowner to indicate how the responsibility is to be distributed. There are several ways in which this

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123. UCA Fourth sched Table A reg 41.
124. *Marx* v *Estates & General Ltd* [1976] 1 WLR 380; see also *Molloy* v *Bemis Bro Bag Company* (1959) 74 F Supp 783 (N Hamps).
125. *Industrial Equity Ltd* v *New Redhead Estate and Coal Co* [1969] 1 NSWLR 565.
126. UCA s 141(1)(b).

may be done: the authority may be given jointly requiring the nominees to act together; the authority might be given in the first place to one while the second nominee is to act only in the alternative of the first failing to do so; finally, two persons can be appointed, each independently, to exercise a specified proportion of the shareholder's voting rights. By an amendment to the Australian legislation enacted in 1971, it is stipulated that the appointment of two proxy holders will be of no effect unless each is appointed to represent a specified proportion of voting rights[127]. This clearly means that a requirement that proxy holders act co-operatively will invalidate the proxy, but it is still permissible to nominate proxy holders in the alternative and, as has been mentioned, proxy forms issued under the Stock Exchange Listing Requirements, while leaving the name of the first proxy holder blank, commonly nominate the chairman to act in an alternative capacity.

The sort of problem which this amendment aimed to avoid is demonstrated by the American cases. Appointment of persons to shared responsibilities will inevitably cause difficulties when they fail to agree. Legal problems arise when three or more persons are appointed but not where only two are named. In the latter case there is an unresolvable deadlock while in the former there will be a question as to the ability of the majority to act in the absence of unanimity[128]. One of the situations in which three or more persons are involved arises where a proxy is given to the board of directors as such. In one such case of this kind it was held that the normal agency presumption of joint authority did not apply, as the intention was to empower the board as an entity to cast

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127. Companies Act (Amendment) Act, 1971 (NSW) no 61 s 17(f)(ii).
128. *Keogh* v *Kittleman* (1968) 447 P 2d 77 (Wash SC); *Callister* v *Graham Paige Corp* (1956) 146 F Supp 399 (D Del); *People ex rel Courtney* v *Botts* (1941) 34 NE 2d 403 (Ill SC).

the vote, and therefore the majority could exercise the power[129].

In Ontario the terms of the statute deny a shareholder the right to appoint more than one proxy holder[130], while the Canadian federal provisions allow proxy holders to be appointed in the alternative but not to joint or concurrent office[131]. It should be noted that because of the provisions regarding proxy holder's powers[132], the practice in Australia will tend to rule out concurrent appointments.

(h) Powers Conferred on the Proxy Holder

To enable the proxy holder effectively to represent his principal, the shareholder, recognition of his right to speak and vote at the meeting is essential. The Australian Uniform Companies Act in endowing the shareholder with proxy rights stipulates that he may appoint a representative "to attend and vote" at the meeting[133]. The right of the proxy holder to attend corporate meetings is never questioned. The statute also stipulates that the proxy holder shall have the same rights as the member to speak at the meeting[134], and again this right is not questioned. However, the statute limits the proxy holder's right to vote at the meeting by providing that, unless the articles otherwise provide, a proxy shall not be entitled to vote except on a poll[135].

In other words, a proxy holder's right to vote on a show of hands is not supported by statute. The articles may, however, stipulate that proxy holders shall have this power[136]. Australian Stock Exchange

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129. *Keogh* v *Kittleman* (1968) 447 P 2d 77 (Wash SC).
130. Bus Corp Act (Ont) s 116(1).
131. Can Bus Corp Act s 142(1).
132. See below.
133. UCA s 141(1).
134. *Idem*.
135. *Idem*.
136. *Idem*, see also Companies Act, 1948 (UK) s 136(1)(c).

Listing Requirements formerly required subject companies to provide that, where one proxy only is appointed, he shall be entitled to vote on a show of hands[137]. However, this requirement has been omitted from the Listing Requirements that came into force on 1 July 1979. It is submitted that this is to be regretted, as the statute does not embody this provision.

The explanation of the original limitation and its conditional relaxation is to be found in the fact that to allow proxy voting on a show of hands threatens to complicate a simple procedure. Voting by show of hands is intended to be a simplified procedure by which per capita voting is used to decide issues on which there is substantial agreement. If, under a provision which allows a shareholder to appoint two proxy holders, such proxy holders were allowed to vote by this method, either a shareholder effectively doubles his vote or it is necessary to identify all the individuals so voting to determine whether a hand represents more or less than one per capita vote. The complications which would arise, though obvious, are exemplified in a decision of the New South Wales Supreme Court denying proxy holders the right in question[138]. Where but one proxy holder is appointed these complications do not arise. This fact may explain why the North American legislation makes no reference to this problem.

The Australian legislation provides that the instrument appointing a proxy shall be deemed to confer authority to demand or join in demanding a poll[139]. In circumstances where voting is, in the first

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137. Associated Australian Stock Exchanges Listing Requirement s 1.B.21.
138. *Clifton* v *Mount Morgan Ltd* (1940) 40 SR (NSW) 355.
139. UCA s 139(2).

place, by show of hands, such a provision is necessary because the courts have laid it down that the proxy holder does not have an implicit right so to vote[140]. Such a ruling, when combined with the fact that the proxy holder could not vote on a show of hands, was obviously capable of producing injustice. However, it should be noted that even absent the statutory provision in question, the courts were not entirely powerless to prevent the injustice. In one such case, where the proxies held by the chairman were necessary to constitute the quorum, the instructions attached to the proxies were such that if a poll were taken, the resolution, which was supported unanimously on a show of hands, would not have been carried[141]. The article gave the chairman a right to demand a poll but he neglected to do so. It was held that, in the circumstances, the chairman was under an obligation to ensure that a poll was taken. The resolution was accordingly invalidated by the court. While the facts of this case are such that it could be easily distinguished, the spirit of the decision is one which should be honoured. A study of comparative material shows that the legislative provisions in Britain and Canada, as in Australia, contemplate that votes should be taken in the first place by show of hands and that it is therefore necessary to provide for a right to demand a poll vote. In providing such a right, these statutes clearly stipulate that a proxy holder has an equal right with those shareholders present in person[142]. In addition, the Ontario legislation stipulates that a poll must be held where "proxies requiring that the

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140. *McCurdy* v *Corrie* (1913) 32 NZLR 769; *Queen* v *Government Stock Investment Co* (1878) 3 QBD 443; *Re Rhodesian Manufacturing Co* [1927] SASR 210.

141. *Second Consolidated Trust Ltd* v *Ceylon Amalgamated Tea Ltd* [1943] 2 All ER 567.

142. Companies Act, 1948 (UK) First sched Table A reg 58(b) and (c); Can Bus Corp Act s 135; Bus Corp Act (Ont) s 121.

shares represented thereby be voted against what would otherwise be the decision of the meeting" total more than five per cent of all the votes that may be cast at the meeting[143]. Such a provision could appropriately be written into the Australian legislation.

The situation in the United States is very different. Aranow and Einhorn state that per capita voting should be permitted only on those organizational matters which are mere formalities and that a stock vote is the only proper method for voting on all questions in regard to the management of the corporation or its business policies[144]. In such circumstances, no concern has been manifested for the problem of enabling the proxy holder to demand a stock vote.

(i) Duration of the Proxy Holder's Authority

Statute may limit the duration of the authority conferred by a proxy, but if no such limitation is expressed by statute, the instrument itself will determine the duration. In Australia, neither the statute nor the Table A articles, nor, indeed, the Stock Exchange Listing Requirements, specifically require that the duration of the proxy be limited. The model form provided by the proxy does state that the nominee is to vote at a meeting to be held on a specified day[145], but it seems unlikely that such a provision in a model form would be effective to invalidate a proxy instrument which did not include such a clause. Even if the provision were held to have such an effect, it could be circumvented by means of a power of attorney. This is an authority which one person confers on another to act in his name, the scope of the powers and

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143. Bus Corp Act (Ont) s 121.
144. Aranow and Einhorn, *op cit*, 361.
145. UCA Fourth sched Table A reg 60.

authority involved depending on the donor's intentions. Powers of attorney may and frequently do empower the nominee either to attend and vote as a proxy holder, or to appoint another person to be a proxy holder, for the principal[146]. There is an instance in the decided cases of a power of attorney nominating any person who might be a partner in a particular firm during its continuance which was honoured twenty-one years after its execution[147]. It may be noted that a power of attorney may be granted for an indefinite term and unless limited by its terms will endure during the lifetime of the parties or until revoked[148], and that consequently such an instrument may effect a separation of ownership and control which will not be reviewed by its donor.

The situation in Australia, where voting powers may, it appears, be delegated to another for an indefinite period of time, may be contrasted with the situation in North America, where provisions limiting the duration of a proxy are common. The American Model Business Corporations Act contains a stipulation that, without an express provision to the contrary, a proxy will only be valid for eleven months[149]. The Securities and Exchange Commission's proxy rules[150] stipulate that no proxy shall confer authority to vote at more than one annual meeting, and the Commission can, it has been said, be expected to prevent the use of a proxy for a special meeting at more than one meeting[151]. The Canadian

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146. Horsley, *op cit*, 125-127; see also *Coachcraft Ltd* v *S.V.P. Fruit Co Ltd* [1978] VR 706.
147. *Bombay Burmah Trading Co* v *Dorabji Cursetji Shroff* [1905] AC 213.
148. Horsley, *op cit*, 177.
149. Mod Bus Corp Act Ann 2d s 33 third para; see also *Molloy* v *Bemis Bro Bag Co* (1959) 174 F Supp 783 (N Hamps); *Stein* v *Capital Outdoor Advertising Inc* (1968) 159 SE 2d 351 (N Ca SC).
150. CFR s 240.14a-4(d).
151. Aranow and Einhorn, *op cit*, 164.

provisions parallel the Securities and Exchange Commission rules and provide that a proxy is valid only at the meeting in respect of which it is given[152]. It appears that where such provisions apply, a power of attorney to vote stock and exercise other rights in respect of the stock will, like the simpler proxy, not entitle its possessor to vote outside the stipulated period[153].

The current usage in Australia is to solicit new proxies for every meeting using the model form provided in the Table A articles, but it is suggested that it would be advisable to forbid the use of proxies that are not limited in duration so as to ensure that the shareowner will take thought as to company policy and affairs from time to time.

(j) Revocation of the Proxy

Regardless of whether the proxy was conferred for a limited or an indefinite period, that proxy may be effectively revoked by the action of the shareowner conferring it. It may be that such a revocation will give the proxy holder a right of action against the shareowner, but this question will be considered later. It does not affect the operation of the proxy machinery with which we are concerned here, in that the company itself will not be concerned with the rights and wrongs of such a claim. Where a vote is cast at a company meeting under a proxy which has not been effectively revoked, the company will assert its right to rely upon that vote. Such a right arises under agency principles, when the proxy holder has apparent authority to cast that vote and the

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152. Can Bus Corp Act s 142(3); Bus Corp Act (Ont) s 120(d)(ii).
153. See *Chapman* v *Bates* (1900) 47 A 638 (NJ Ct of Errors & Appeals); *Roberts* v *Whitson* (1945) 188 SW 2d 875 (Texas Ct of Civ Apps); *Burleson* v *Hayutin* (1954) 273 P 2d 124 (Colo SC).

company is not privy to transactions which may have occurred between the shareowner and the proxy holder to change that position[154]. Moreover, the right is usually asserted in the company articles by a regulation in the form of article 67, Table A. It thus becomes important to determine how and when a proxy will be effectively revoked.

(k) Manner of Revocation

A proxy can be expressly and formally revoked so that the company cannot rely on the ostensible authority it confers by written notice to the company at its registered office before the commencement of the meeting[155], or as otherwise provided by the articles. It has also been held in the United States[156] and would, it is submitted, be similarly held in Australia, that a proxy is revoked when a subsequent proxy in respect of the same holding is lodged as required by the articles so as to be valid at the meeting to which both relate. There are, of course, technical problems as to deciding which proxy is of later origin and whether the proxies do relate to the same holding[157], but the principle is clear: the former is superseded by execution of a later authority.

A slightly more difficult problem is whether the presence of the shareowner at the meeting or his exercise of the powers delegated under the proxy revokes that proxy. The decision of the Court of Appeal in the case of *Cousins* v *International Brick Co Ltd*[158] is the leading authority. At first instance it was held that the company, when faced with the

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154. See Treitel, G.H., *Law of Contract*, 4th ed (London, Stevens & Sons, 1975) 488-491.
155. UCA Fourth sched Table A reg 62.
156. *Burleson* v *Hayutin* (1954) 273 P 2d 124 (Colo SC).
157. *Schott* v *Climax Molybdenum Co* (1956) 154 A 2d 221 (Ch Del).
158. [1931] 2 Ch 90.

choice must, in the absence of any special contract, accept the votes cast by the shareowner in preference to those cast by the proxy holder[159]. This decision was upheld on appeal, but Lord Hanworth MR suggested that the articles might be so drawn as to provide that the giving of a proxy amounted to a renunciation of the right to vote in person[160]. Only Romer LJ, however, referred to the question of whether the shareholder's action amounted to a revocation of the proxy and he held that what the shareholder was doing was not to revoke the proxy but to forestall any necessity for its exercise[161]. The authority of the Court of Appeal's decision on this question has been accepted in the Australian case of *Ansett* v *Butler Air Transport (No 2)*[162] referred to below[163].

In his decision in *Ansett's* case, Ayers J held that the distinction between revoking the proxy and preventing its use drawn by Romer LJ was central to the decision in *Cousins* v *International Brick Co Ltd*. It is suggested, however, that the real key to the decision of the Court of Appeal lies in the fact that the proxy holder, as agent, could not be allowed to assert his rights in competition with the shareowner. In the Australian case, the shareowners attended the general meeting and voted on a show of hands but refrained from voting their own shares when the ballot was held. The court found that this manifested an intention objectively apparent to the chairman of the meeting that the proxies continued in effect and found that the proxies had not been revoked by the exercise of certain rights by the shareholders, but declined to base its

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159. *Cousins* v *International Brick Co Ltd* [1931] 2 Ch 90, 95.
160. [1931] 2 Ch 90, 101.
161. [1931] 2 Ch 90, 103.
162. (1958) 75 WN (NSW) 306, 311.
163. See below, 383.

decision on the fact that the shareholders' intention was determinative[164]. The judge pointed out that the case could have been decided on the narrower basis that, in the circumstances in point, the proxy holder, being himself a member of the company, had an independent right to attend the meeting and had no right to vote, in the right of the proxy, on show of hands. Thus, the shareowner had not exercised in person any of the rights he had conferred under the proxy[165].

Aranow and Einhorn point out that a dissident shareholder or group may give a proxy to his lawyer or accountant solely for the purpose of allowing them to attend the meeting[166]. Management's professional advisors will attend the meeting and the dissident may wish to take steps to counteract this advantage. If the mere presence of the shareholder nullifies a proxy given for this purpose, the law will be assisting management in maintaining this advantage. Despite the expression elsewhere of contrary views[167], those authors accept the authority[168] which provides that the mere presence of a stockholder at a meeting will not revoke a proxy in the absence of a contrary intention.

A proxy will be effectively revoked so far as the company is concerned only when the intent to do so is formally conveyed to the company either by formal written notice of revocation or by execution and lodgment of a new proxy. But it is concluded that when faced with a choice, the company has no lawful alternative but to accept the vote of the shareholder.

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164. See further, Herron, B.J., *'Proxy Voting at Company Meetings'* (1958) 32 ALJ 249, 254.
165. *Ansett* v *Butler Air Transport (No 2)* (1958) 75 WN (NSW) 306, 311.
166. Aranow and Einhorn, *op cit*, 330.
167. 5 Fletcher Cyc of Corps s 2062 (rev vol 1967) as cited *idem*.
168. *In re Manacher* v *Central Coal Co* (1954) 133 NYS 2d 265 (SC), affirmed 131 NYS 914, accord *In re Nugent* v *Mooney* (1956) 155 NYS 2d 615 (SC) as cited *idem*.

C. REGULATION OF PROXY SOLICITATION

It has been stated above[169] that companies which comply with the Stock Exchange Listing Requirements and send out proxy forms to their members are engaging in the solicitation of proxies. Anglo-Australian courts have found the distinction between a proxy given at the initiative of the shareholder and proxies solicited by the proxy agent relevant to their decisions concerning the duty and discretion of proxy holders and the revelation of proxies. Nevertheless, due to the fact of statutory provisions utilizing the concept, they have not found it necessary to define exactly what does and does not constitute proxy solicitation. This need has, however, been felt in North America, where the statutes do employ the concept.

1. SOLICITATION DEFINED

"To solicit" is defined by the Oxford English Dictionary as meaning to entreat or petition a person to do something, to ask earnestly or persistently[170]. The term "proxy solicitation" as used by Aranow and Einhorn means "the process of systematically contacting shareholders and urging them to execute and return proxy cards which authorize named persons to cast the shareholders' votes"[171]. What follows is an examination of the elaborations of this definition in the American Securities and Exchange Commission's proxy rules, which, in this respect, have been copied almost

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169. See above, 322.
170. Oxford English Dictionary (1970) vol X 395 (2).
171. Eisenberg, M.A., *"Access to the Corporate Proxy Machinery"* (1970) 83 Harv L Rev 1489, 1491.

verbatim by the Canadian draftsmen[172].

A proxy solicitation is defined by regulation to include any request to execute or not to execute or to revoke a proxy, or the furnishing of a form of proxy or other communication to shareowners under circumstances reasonably calculated to result in the procurement, withholding or revocation of a proxy[173]. Soliciting material may be either written or oral[174], and it has been determined judicially that preliminary communications will be caught if the requirements of a two-fold test are met[175]. The test is whether the sender ultimately intended to solicit proxies and whether the communication was made under circumstances reasonably calculated to result in the procurement, withholding or revocation of a proxy. Both questions are determined objectively[176].

Certain acts are specifically stated not to constitute solicitation. These are the furnishing of a proxy form in response to an unsolicited request, the mailing by management under the requirements of the proxy rules of proxy material prepared by non-management groups, and other merely ministerial acts performed on behalf of a person soliciting a proxy. Finally, certain acts are specifically exempted from the requirements of the proxy rules[177]. These include limited solicitations of not more than ten people conducted by non-management committees. This exemption is designed to allow a dissident to approach a limited number of shareholders quietly to see whether they will join in mounting a campaign to oppose management. At this early stage it is still possible that the decision not to go ahead will be made and it is deemed unfair under these circumstances to apply the proxy regulations and thus alert management to

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172. Getz, *op cit*, 26.
173. CFR s 240.14a-1.
174. Aranow and Einhorn, *op cit*, 100-101.
175. *SEC* v *Oakin* (1943) 132 F 2d 784 (2d Cir).
176. Aranow and Einhorn, *op cit*, 101-104.
177. CFR s 240.14a-2.

the need to forestall such opposition. The second exemption applies to communications between the beneficial owner of a share and his nominee: a beneficial owner who writes to his nominee and requests the nominee to execute a proxy allowing the beneficial owner to attend the meeting will not have to comply with the proxy rules. In such a case the proxy device is being used not to separate but to unite voting power with ownership interest and there is deemed to be no necessity for regulation. Rules governing proxy solicitations are designed to ensure that individuals who seek to further their own plans for the company by persuading others to give, or to withhold from the solicitor's opponents, the authority to vote as their representatives will not define their own authority too broadly or conceal their interests in the matter.

2. MANAGEMENT SOLICITATIONS

(a) As Treated by Anglo-Australian Courts

Although managements in Australia, as in Britain, are not required by statute to solicit proxies from shareholders, and although the courts are only beginning to come to grips with some of the problems that such solicitations present, it would be false to conclude that such a practice is new. Managements probably began soliciting proxies from shareholders in the days of the chartered trading corporation[178]. Courts in the nineteenth century were called upon to decide whether the expenditure of corporate funds on machinery designed to procure proxies in management's favour was valid, and in deciding this question they were compelled to decide whether such solicitation was within management's

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178. Cooke, C.A., *Corporation Trust and Company*, (Manchester, Manchester University Press, 1950) 74 states that the right to vote by proxy was granted by statute to the Mines Adventurers and Northumberland Fishery Soc 9 Anec c 24 (1710).

power.

In the earliest case the court held that it was within the power of the company executive to print and send out blank forms of proxy but that the use of corporate funds to pay stamp duty and return postage on the completed forms was invalid in that it would practically give the directors power to determine as they chose any question that arose at such a meeting[179]. However, on this point that case was overruled by *Peel* v *London and Northwestern Railway Co*[180]. Vaughan Williams LJ held there that the power to issue proxy forms was incidental to, and consequential upon, the board's statutory authority to convene a meeting. He further held that it was the duty of management to inform the shareholders and to advocate what appeared to be the best corporate policy and, further, that they might suggest that the best way to ensure that such a policy was adopted was to appoint their nominees as proxy holders. Fletcher Moulton LJ agreed on this point and held further that the directors would be under a duty to carry out such a solicitation if they thought that there was a danger that the corporation would take a step that might injure it. The company's interest in obtaining a quorum for the meeting justified the payment of all expenses involved in obtaining proxies.

Buckley LJ's judgment in *Peel's* case is, however, that most frequently cited. He held that

> "as a general principle it cannot be *ultra vires* to use the company's funds *bona fide* and reasonably for the purpose of obtaining the best expression of the voice of the corporation in general meeting"*181*

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179. *Studdert* v *Grosvenor* (1886) 33 Ch D 528, 539.
180. [1907] 1 Ch 5.
181. [1907] 1 Ch 5, 18.

The use of the term "reasonably" here is worth noting in that it implies that there may be some limits to the funds that can be used but this limit has not been explored by Anglo-Australian jurisprudence. Buckley LJ further held that it was the duty of the directors to inform and attempt to guide the shareholders' decisions on questions of policy. The distinction between questions of policy and questions of personnel was important inasmuch as he held that the directors could not legitimately use corporate funds to solicit proxies where their only aim was to retain office. This distinction was picked up by the American cases. However, difficulties were to manifest themselves when an attempt was made to apply it. Before turning our attention to the American treatment of these problems, this paper is concerned to show how Anglo-Australian courts have treated management proxy solicitations in more recent times.

Although the board of directors is not required to solicit proxies from their shareholders by statute, they may be required to do so by the courts in certain circumstances, as when court approval is requisite before a scheme of arrangement can be put into effect. In *In re Dorman Long & Co*[182], Maugham J was called upon to decide a dispute arising under just these circumstances. In the course of his judgment the learned judge commented upon the advantageous position which management occupied *vis a vis* opposition and held that the court ought to bear these considerations in mind when it has before it a case where the whole matter is really determined by the proxies which have been given before the meeting begins[183]. Before going on to consider whether the explanatory circular which had been sent out was objectionable, the

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182. [1934] Ch 635.
183. [1934] Ch 635, 658.

judge dealt with two other matters. He held, first, that the court's power to summon a meeting might involve a power to settle a form of proxy to be sent out at the expense of the company but that in this case the court had not directed that no other proxy form could be used at the meeting[184]. He also held that the directors who, pursuant to the order of the court, get proxies for or against the scheme have no option as to whether or not they will use them as the persons who give them are entitled to assume that the proxies will be used[185]. This last point is potentially of wide significance as the question will arise where management or, indeed, anyone else solicits proxies in other circumstances whether they will be under a duty to exercise them[186].

In *Re Marra Developments Ltd*[187], referred to in the introduction, an Australian court has recently considered a number of contentions arising out of a management solicitation of proxies in the context of a corporate dispute. Wootten J was concerned to see that the issues in dispute were carefully evaluated and, as the proxy contest was "likely to be decisive", found occasion to review the proxy requirements laid down in conformity with the Stock Exchange Listing Requirements by the company's articles. He canvassed the question of whether a proxy which named the chairman of the board of directors as an alternate was proper. It was impossible, he held, to rule that the use of such a form was improper but the advantages it conferred on management would be borne in mind in considering what terms, if any, to impose on his order. In the end he required management to send out a "two-way" proxy form and

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184. *In re Dorman Long & Co Ltd* [1934] Ch 635, 662.
185. [1934] Ch 635, 664.
186. See below, 378-380.
187. (1976) 1 ACLR 470.

in addition required the proxy form to include a note to the effect that unless instructed how to vote, the proxy holder may vote or refrain from voting as he thinks fit.

One aspect of management proxy solicitation that is covered by statute is the partial solicitation. In the course of his judgment in *Peel's* case, Fletcher Moulton LJ conditioned his decision on the fact that the shareholders had been treated impartially[188]. This prerequisite was lost sight of in the later decision of *Wilson* v *London Midland and Scottish Railway Co*[189]. In that case, management sent stamped proxy forms only to those shareholders whose holdings were substantial. It was held that this fact did not invalidate the proxies or the use of corporate funds in their solicitation but that the action would have been open to challenge if it could be proved that the basis of selection was an expectation that those shareholders would support management policy. The court was influenced by considerations of administrative convenience and the desirability of limiting expense. These factors are, it is suggested, insufficient to justify the exclusion of the smaller shareholder from equal representation, especially in view of the fact that his interests are those most likely to be overlooked. Such a partial solicitation at company expense is now specifically forbidden in Australia by a penal provision of the Uniform Companies Act[190], and this is deemed right and necessary by the writer.

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188. *Peel* v *London and Northwestern Railway Co* [1907] 1 Ch 5, 17.
189. [1940] Ch 169.
190. UCA s 141(4).

(b) In North America

Management solicitation of proxies is mandatory under the new Canadian legislation which applies to all but the smallest companies[191]. These provisions were introduced on the recommendation of the Kimber Committee whose report stated that:

> "If proxies are not solicited the shareholder will, in large part, have no adequate voice in the affairs of the company. The management of most large or well established public companies does, in fact, solicit proxies for annual or special meetings of shareholders. The Committee recommends that the solicitation of proxies by the management of all public companies be made mandatory."*192*

In the United States such solicitation is not mandatory even under the Securities and Exchange Commission's proxy rules, but where these rules apply if management chooses not to solicit proxies they are still required to furnish prescribed information to their shareholders. All solicitations, whether voluntary or mandatory, are regulated by the provisions found in the Canadian and Ontarian statutes as by those promulgated by the Securities and Exchange Commission.

The use of corporate funds to pay for management solicitations is an issue that has aroused renewed interest in the United States recently, and will be examined below under the heading of "Access to the Corporate Proxy System". In the interim, it may be stated that to date American courts[193] have accepted the principles laid down in the British decision

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191. Can Bus Corp Act s 143; Bus Corp Act (Ont) s 1.
192. *Kimber Report, op cit,* para 6.24.
193. *Hall* v *Translux Daylight Picture Screen Corp* (1934) 171 A 226 (Del Ch); *Steinberg* v *Adams* (1950) 90 F Supp 604 (SD NY); *Rosenfeld* v *Fairchild Engine and Airplane Corp* (1955) 128 NE 2d 291 (NY CA), 116 NYS 2d 840, 132 NYS 2d 273; *Braude* v *Havenner* (1974) 113 Cal Rptr 386 (CA).

in *Peel's* case[194] and have striven to apply Buckley LJ's distinction between questions of policy and questions of personnel. Difficulties have arisen, however, because it is not always easy to separate the two questions. For example, where two different slates of directors offer themselves for election advocating policies which vary slightly in their details, is the ensuing contest to be considered one as to policy or as to personnel?[195]

A recent American decision which is worth remark concerned a management practice in an incorporated association of automobile owners whose activities included member services and lobbying[196]. The membership application in use had appended to it a blank form of proxy which applicants were requested to fill out prior to approval of their membership. The propriety of this practice was challenged. It was held that a person could validly execute a proxy form in anticipation of acquiring membership status but certain of the proxies in question were invalidated because it had been suggested to the applicants that execution of the proxies was a precondition for membership. While management may solicit proxies needed to conduct ordinary corporate business, they may only invite and must not require members to execute such an authorization. This holding would, the writer predicts, be followed in Australia.

3. NON-MANAGEMENT PROXY SOLICITATIONS

There are no statutory provisions in either the Australian or the British Companies Acts governing proxy solicitations by non-management

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194. *Peel* v *London and Northwestern Railway Co* [1907] 1 Ch 5.
195. *Hall* v *Translux Daylight Picture Screen Corp* (1934) 171 A 226, 228 (Del Ch): "A question of policy which concerns very intimately the future of the corporation business may turn upon the particular personnel of the directors and officers."
196. *Braude* v *Havenner* (1974) 113 Cal Rptr 386 (CA).

groups. In addition, there is scant case authority on problems arising out of such solicitations. One decision, however, which may be referred to is that of Maugham J in the case of *In re Dorman Long & Co*[197], which was mentioned above. In that case, management attempts to have the scheme of arrangement approved were opposed. Maugham J commented on the difficulties faced by a non-management group[198] or class of objectors, difficulties which include lack of prior warning, isolation, lack of funds and lack of information. The fact that the proxies which this group had obtained were not in the form prescribed by the court was not, he held, a ground for denying them the right to exercise the votes so obtained. In addition, he saw grave objections to holding that a proxy which was lodged too late would be bad, but found it unnecessary to decide this point[199].

In North America there are, of course, no provisions requiring a non-management group to undertake a proxy solicitation, but once such a solicitation is undertaken voluntarily it is subject to the same regulations as those that govern a management solicitation.

D. THE PROXY HOLDER IN RELATION TO THE SHAREOWNER

The proxy holder occupies the position of agent to the shareholder's principal and the rules of agency law are applicable. However, inasmuch as this particular type of agency relationship has some distinctive features, it is proposed to discuss the relationship under the headings of Duty, Lack of Right and Discretion of the proxy holder. In each

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197. [1934] 1 Ch 635.
198. [1934] 1 Ch 635, 658.
199. [1934] 1 Ch 635, 662.

case it will be seen that the relationship is affected whether or not the proxy has been solicited by the proxy holder.

1. THE DUTY OF THE PROXY HOLDER

The creation of an agency does not, without more, impose an obligation on the agent to exercise his powers. This is because it may be desirable to provide against the contingency that an agent will be needed. The agent will only have a duty to exercise his powers when he has contracted to do so and then his duty will be limited by the terms of the contract. The proxy holder is not, without more, under a duty to exercise his powers. This was implicit in the judgment in *Clifton* v *Mount Morgan Ltd*[200], where the question for decision was whether the shareholders present at the meeting who failed to indicate on their ballot papers that they were voting in the dual capacity of shareowner and proxy holder had effectively voted in both capacities. Roper J at first instance held that "no presumption that a shareholder is exercising his proxy votes can arise unless he gives some clear indication that he is doing so"[201]. On appeal this decision was reversed, and it was held by a majority of two to one that, in the circumstances, votes had been cast in both capacities. The disagreement was as to whether the proxy holder must affirm or deny his intention to vote as such once he has lodged the proxy forms[202]. All the judges in the appeal court obviously contemplated that the proxy holder was free to form an intention not to cast the votes given him by proxy.

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200. (1940) 40 SR (NSW) 31.
201. (1940) 40 SR (NSW) 31, 35.
202. (1940) 40 SR (NSW) 31, 54 per Davidson J, *contra* at 43 per Jordan CJ (dissenting on this point).

Direct authority on this point is found in *Oliver* v *Dagleish*[203] , where the court considered the position of a certain individual, an opponent of management, who held a large number of proxies which he had solicited. The proxies were in such a form as to allow the shareowner to direct the proxy holder to vote either for or against the resolution or to leave the proxy holder free to exercise his discretion. Shareholders holding over ninety-three thousand votes had directed that their votes be cast for the resolution, while in respect of fifty-five thousand shares instructions had been received to vote against, and holders of twenty-six thousand shares had left the matter to the proxy holder's discretion. The ballot papers used did not require any indication of the number of votes intended to be cast. The proxy holder marked his ballot "for" the resolution, but the chairman refused to count any of his votes. It was held to be unnecessary to decide whether the votes conferred on him in respect of the fifty-five thousand shares from shareholders who wanted to vote against the resolution had been cast in its favour because on a decision that he had cast the one hundred and nineteen thousand votes for the resolution it would have been carried. The court decided that those one hundred and nineteen thousand votes had been effectively cast. There was no question whether the fifty-five thousand votes had been cast against the resolution.

However, a suggestion to the effect that there is a legal duty to exercise proxies that have been solicited is found in the judgment of Athwatt J in *Second Ceylon Trust* v *Ceylon Amalgamated Tea and Rubber Estates Ltd*[204], in which he held that the chairman who held proxies acquired as a result of a management solicitation was under a duty to

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203. [1963] 3 All ER 330.
204. [1943] 2 All ER 567, 570 as discussed above, 361.

exercise his power to call for a poll. Such a duty may be supported by the argument that there is a contract between the solicitor and the shareowner by which the shareowner agrees to give the proxy holder the necessary authority and the proxy holder impliedly agrees to exercise it.

Some light is cast on the question of whether such a contract can be implied by the American case of *Duffy* v *Loft Inc*[205]. Although this case was decided in 1930, there is no more recent decision on this question for the reason that the provisions adopted under the Securities Exchange Act are so formed as to expressly require the solicitor to enter into an undertaking to vote the shares represented by any proxies which he obtains[206].

In *Duffy* v *Loft Inc*, the Chancellor found that it was the manifest intent and desire of the stockholders from whom proxies were solicited that their proxy holder attend the meeting and vote in their behalf and that the stockholders thought that the solicitors of the proxies would exercise them. He held that the stockholders could not

> "by the mere entertaining of such an intent...permanently fasten the relationship of agency upon those named in the proxies so that the latter cannot refuse to act. An agent can always abandon his agency at the risk of assuming the risk of liability if the circumstances are such that the law attaches liability."*207*

This judgment cannot be said to be decisive of the question; however, the judgment of Pennewill LJ in the same case on appeal went far towards establishing a distinction between solicited and unsolicited proxies. He held that in the circumstances there was a duty on the persons holding proxies to attend the meeting and to vote the stock which they

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205. (1930) 151 A 223 (Del Ch), affirmed 152 A 849.
206. CFR s 240.14a-4(c); see also Can Bus Corp Act s 146(1); Bus Corp Act (Ont) s 120(c).
207. (1930) 151 A 223, 227 (Del Ch).

represented[208]. It was inequitable for the said proxy holders to try to prevent the meeting from being conclusive. The decision in *Duffy* v *Loft Inc* was not finally conclusive of the question in the United States of America, first because it did not bind courts in other jurisdictions, and secondly because it could be limited by reference to its facts.

In particular, a question arose as to whether a proxy solicitor would be obliged to vote proxies where they were returned with instructions to vote against the position advocated by the solicitor. In *Duffy* v *Loft Inc* the proxies were given in the tenor requested. There were various views as to the proper practice to be followed when this was not the case. The question was discussed briefly by both Axe and Dean. The opinion expressed by Axe was that the solicitor was not obliged to vote such a proxy. The practice, he stated, was to return the proxies with a letter stating that the persons named as proxy holders did not feel that they should vote the proxy since they did not agree with the proxy given as to the merits of the proposal in question[209]. Dean, on the other hand, while conceding that it was not clear whether the nominee was duty bound to accept the authority, suggested that the nominee who decided not to accept such a proxy was under a duty to notify a stockholder that he did not wish to accept the proxy relationship on this basis[210]. He stated further that it was considered better practice for the nominee to vote in accordance with the instructions except in the case of elections of directors[211]. In Australia there is no requirement whether statutory or under the Stock Exchange Listing

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208. *Duffy* v *Loft Inc* (1930) 152 A 849, 853 (Del SC).
209. Axe, *op cit*, 252 n 251.
210. Dean, *op cit*, 493.
211. *Ibid*, 493 n 25.

Requirements which would oblige a proxy holder, whether or not he was present at the meeting and whether or not he had solicited the proxy, to exercise it. Despite the fact that it would be considered ethically improper not to do so where the shareholder had specified how the vote should be used, it is suggested that the Australian legislation should be amended to incorporate such a requirement.

2. ABSENCE OF TITLE IN THE PROXY HOLDER

In most circumstances the grant of a proxy does not create a right to attend and vote at the meeting that the proxy holder can assert against the shareowner. This proposition is supported by *Cousins* v *International Brick Co Ltd*[212].

The relevant articles of association in that case contained a provision equivalent to regulation 45 of the Table A articles that votes given under the terms of a proxy should be valid unless the company had been given written notice of revocation. In a poll taken at an adjourned meeting, C claimed a right to vote under proxies held by him despite the fact that certain of the shareholders who had given those proxies were present and voted in person. It was admitted, on authority[213], that certain purported revocations by shareholders who had not attended the meeting were ineffective under the terms of the article and that C should have been allowed to cast those votes. As to the votes which the shareholders who attended the meeting cast, no difference was made between instances where the proxy had, in terms, been revoked and those where the shareholder voted personally without such formality. It is submitted that in the circumstances of this case, the intention to

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212. [1931] 2 Ch 90.
213. *Spiller* v *Mayo (Rhodesia) Development Co* [1926] WN 78.

revoke the proxy was equally clear in both situations.

Luxmoore J, in his first instance judgment, held that

> "the proxy is merely the agent of the shareholder who appoints him. As between himself and the proxy he can determine the agency and the agent is not entitled to vote if the proxy is in fact determined."*214*

It is suggested in the light of this statement that, in an action between C and those shareholders who had "revoked" their proxies but had not attended the meeting, it would have been held that C had no right to vote such shares provided merely that the revocation had been communicated to him whatever the situation between the company and the shareholder or between C and the company, but this point did not arise.

Powers of attorney when coupled with a pecuniary interest such as arises under a contract have been held irrevocable in English[215] and Canadian[216] courts, and there is no reason to suggest that the same does not apply to proxies[217]. There appears to be no authority on the point in Britain or Australia[218].

There is also American authority for the proposition that as the proxy holder is a mere agent his powers exist only at the will of his principal and may be revoked at any time[219]. The fact that there might be an independent contract giving the agent a right to exercise the authority

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214. *Cousins* v *International Brick Co Ltd* [1931] 2 Ch 90, 95-96.
215. *Knight* v *Bulkeley* (1858) 22 LJ Ch 592.
216. *Richardson* v *McClary* (1906) 16 Man R 74.
217. See also Pickering, M.H., *"Shareholder's Voting Rights and Company Control"* (1965) 81 LQR 248 where he suggests that the law should look more favourably on irrevocable proxies given for consideration. But see now *Coachcraft Ltd* v *SVP Fruit Co Ltd* [1978] VR 706.
218. In *Ansett* v *Butler Air Transport (No 2)* (1958) 75 WN (NSW) 309 the question did not arise. The issue was whether the proxy had been revoked. See above, 366.
219. *Schmidt* v *Mitchell* (1897) 101 Ky 570, 72 Am St R 427, 432.

has been held not to affect the principle although contractual liability may arise[220].

Generally it is suggested that the law is concerned here to see that the company does not become embroiled in disputes between the proxy holder and the shareowner. In questions between the proxy holder and the shareowner, moreover, it has been held in the United States that there is no such thing as an irrevocable proxy not coupled with an interest[221], as such proxies are void as contrary to public policy[222]. The public policy here referred to is that against the separation of voting power from ownership[223], and this objection is not present when the proxy is coupled with an interest or based upon consideration[224]. A relevant interest obviously exists when, for example, there is a contractual agreement to sell or purchase shares[225], but it has also been held more recently that a voting pool agreement will constitute the requisite legal consideration[226].

3. DISCRETION OF THE PROXY HOLDER

In authorizing another to act as proxy holder for him, the shareholder confers on that other a certain discretion and this appears to be true whether or not the grant of authority is accompanied by certain explicit instructions. Unless a shareowner, as well as instructing his proxy holder to vote in a certain fashion on specified resolutions, instructs

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220. *State ex rel Everett Trust & Savings Bank* v *Pacific Waxed Paper Co* (1945) 157 P 2d 707 (Wash SC).
221. *Luthy* v *Ream* (1915) 110 NE 373 (Ill SC); *Roberts* v *Whitson* (1945) 188 SW 2d 375 (Tex Civ App); *Burleson* v *Hayutin* (1954) 273 P 2d 124 (Colo SC).
222. *Bache* v *Central Leather Co* (1911) 81 A 571 (NJ Ch).
223. *Bache* v *Central Leather Co* (1911) 81 A 571 (NJ Ch).
224. *Roberts* v *Whitson* (1945) 188 SW 2d 375 (Tex Civ App).
225. See for example *Groub* v *Blish* (1926) 152 NE 609, 153 NE 895 (Ind AC).
226. *Abercrombie* v *Davis* (1956) 123 A 2d 893.

him that he is not to take any part in the discussion and is not to vote on any other notion, even including those of a procedural nature, all of which appears inconceivable, this will remain true. However, the discretion is limited, first by any explicit instructions which may accompany the grant of authority, and secondly, by the duty imposed on the proxy holder under the laws of agency obliging him as fiduciary to act in the best interests of his principal.

The proxy holder's discretion is limited in that he has no authority to represent his principal in any capacity other than as shareholder. Furthermore, his authority is deemed to be limited by reference to the notice issued in respect of the meeting concerned. The basis of this limitation where the proxy is related to a particular meeting is obvious. In the case of general proxies not limited in their scope to a particular meeting, it is found in the presumption that a shareholder who has received notice that a particular topic would arise for decision at the next meeting authorizes his proxy holder to vote in either manner on the question because he does not revoke the proxy or take other action to make his views effective. This presumption does not arise in the absence of a valid notice of meeting or in respect of matters not included in a valid notice.

It has always, in all jurisdictions, been open to the shareowner to attach restrictions to the grant of authority. This was so even in the face of the attitude adopted in *Attorney-General* v *Scott*[227] discussed above. While it was felt that the instructions might make the delegation more objectionable, it was not suggested that the restrictions were not operative. Similarly, the historical existence of a provision in the Ontario statute, forbidding the inclusion of such restrictions in the

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227. (1749) 1 Ves Sen 413, 27 ER 1113.

instrument conferring a proxy[228], did not prevent the shareowner giving secret but binding instructions to his proxy holder so long as the restriction did not appear on the face of the instrument, when it would oblige the company to inquire as to whether the terms had been observed[229].

It has been noted[230] that company articles may, and the Stock Exchange Listing Requirements do, provide for the use of two-way proxy forms by which the shareowner directs the proxy holder to vote for or against each individual resolution. The use of such forms should, it is submitted, be mandatory under the statute when proxies are solicited. Otherwise the use of such forms is at the discretion of the person who drafts the proxy form, that is, the solicitor. It is not a satisfactory compromise to leave it to the articles to require the use of such forms inasmuch as the company articles are too much within the power of company management. To leave it to the articles to impose such a restriction on solicited proxies is virtually to leave it to the company's management, the party most likely to solicit proxies. Where the shareholder takes the initiative in appointing a representative, the same arguments do not apply inasmuch as the shareholder is likely to be his own draftsman. No unnecessary restrictions should apply to make this task more difficult for him. This is the position adopted by the Canadian legislation on the recommendation of the Dickerson committee[231].

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228. RSO 1937 c 25 s 52(4). However, this provision was repealed by RSO 1960 c 71 s 75(3) even before the new scheme of proxy regulation was adopted.
229. *Montreal Trust Co* v *Oxford Pipeline Co* [1942] 2 DLR 619, 623.
230. See above, 347 *et seq.*
231. Dickerson, R.W.V., Howard, J.L. and Getz, L., *Proposals for a New Business Corporations Law for Canada*, (Ottawa, Information Canada, 1971) vol 1, 309.

The discretion which may be conferred on a proxy holder is closely defined in the United States by the Securities and Exchange Commission's proxy rules. The relevant provisions appear in Proxy Rule 14a-4(c), which stipulates that a proxy may confer discretionary authority with respect to certain matters including matters which the solicitors do not know are to be presented to the meeting and matters incident to the conduct of the meeting. Otherwise the proxy form must provide means whereby the shareholder may instruct his proxy to vote for or against each matter. It is further stipulated that a proxy may confer discretionary authority where such a choice is not indicated provided the form states how the solicitor intends to vote in such an event[232].

(a) Unmarked Proxies

A proxy which is returned without an indication as to how the votes are to be cast on each resolution has been called an "unmarked proxy". The fact that the solicitor is permitted to use such proxies was strongly criticized by Gilbert, who stated that "in many instances our heaviest defeats were not defeats at all but merely the process of being snowed under by unmarked proxies"[233]. He advocated a rule that "unmarked proxies, unfailingly voted for management, be voted in accordance with the majority votes tabulated when the unmarked proxies have not been counted"[234]. It is submitted that there is insufficient evidence to support Gilbert's premise that unmarked proxies have been unthinkingly returned. This criticism has been repeated more recently by another American commentator. It is, as R.N. Schwartz points out[235], difficult to

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232. CFR s 240.14(a)-4(b)(1).
233. Gilbert, *op cit*, 50.
234. *Idem*.
235. Schwartz, R.N., *op cit*.

estimate the extent of the advantage that the use of such unmarked or discretionary proxies confers on management. It may be that these proxies represent the shares of those supporters of management who have advisedly decided that they wish to confer a broad discretion on management and there are many cases in which such trust will be justified. On the other hand, to the extent that these proxies represent the votes of apathetic shareholders and encourage unthinking across the board endorsement of management proposals, the system does undercut true shareholder democracy. Schwartz points out that it is arguable that prohibition of such proxies would infringe on the right to vote by proxy but favours such prohibition where it is not contrary to statute[236].

Were such a prohibition to be enacted, the shareholder might elect to follow the "party line" and to vote as management recommends without weighing the arguments put forward. This would not advance shareholder democracy and, in the event, which remains a theoretical although unlikely eventuality, that the solicitor should execute a complete *volte face*, he would be bound to exercise the proxies as initially recommended even though the persons executing such proxies had accepted the recommentation blindly.

The possibility, which can be drawn from Gilbert's proposal , of offering the shareholder an option as to whether his unmarked ballot should be cast as management dictates or "in accordance with the majority votes tabulated" before they are counted carries more interest. Such an option could be offered on the proxy form or could be pre-empted by the articles of association. Were such an option offered on the proxy form, some rule would have to be adopted for dealing with proxies in which the

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236. Schwartz, R.N., *op cit*, 1163-1165.

option was not exercised. Such a rule would involve a choice between three possibilities: such stubbornly unmarked ballots might be cast for management, with the majority, or might be used solely for the purpose of determining a quorum. It is submitted that to elect this third method would not prevent a special resolution being passed under section 144 but it might delay certain decisions for which an absolute majority is requisite under the company articles and which, in the absence of the rule, would be carried. However, it could be provided that the third possibility should not apply where to cast the votes with management would be to cast them with the majority. This is a question which has recently been reviewed by the Securities and Exchange Commission, but as yet no recommendations have resulted from the inquiry[237].

(b) The Discretion as to Amendments

Where instructions to vote for or against a certain resolution are given, the question arises whether the authority conferred stretches to allow the proxy holder to vote in favour of the resolution as amended. There is no Australian authority in point, but the question was considered by Slesser LJ in the English Court of Appeal[238]. The proxies in question contained instructions as to how to vote on the main question before the meeting and the point in issue was whether they could be used to vote on a motion for adjournment proposed in the form of an amendment to the substantive resolution. It was held, as a matter of construction, that the proxy holder could vote on any incidental question that might

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237. See below, 394-395, but see now 35.
238. *Re Waxed Papers Ltd* [1937] A11 ER 481.

need to be decided in the course of the meeting. As the question was decided on the basis of construction, the decision is not particularly helpful.

A Canadian decision on the question of whether a proxy form which stipulated that "unless specifically directed to the contrary" the nominees would vote in a specified manner, allowed them to vote for an amended resolution is even less helpful[239]. The meeting in question was held pursuant to a court order which specified use of the particular proxy form. At the meeting the company's solicitors stated that the proxies could not be used to vote for the amended resolution. The court was called upon to decide whether in the circumstances the original arrangement so approved was valid. The court held that it was not, but divided as to the reasons for the decision. Middleton JA stated that directions as to the form of proxy should not have been given[240]. This, with respect, begged the question and would mean that the shareholder could not be given an opportunity to express an opinion. It is submitted that the other two judges took the better view when they disagreed with Middleton JA on this point[241]. Masten JA's opinion was governed by the provision then in force by which no restriction on the voting power could appear in the proxy form. He held that if the proxy was valid as being a general proxy then, regardless of the original intention, the proxy holder had a duty to exercise the power in what he deemed was the best interest of his *cestui que trust* and to vote for the arrangement as modified[242]. Henderson JA held that the solicitor's

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239. *Re Langley's Ltd* [1938] 3 DLR 230.
240. [1938] 3 DLR 230, 233.
241. [1938] 3 DLR 230, 245.
242. [1938] 3 DLR 230, 244.

ruling disenfranchised the bulk of the shareholders from voting for the alteration and thus invalidated the meeting[243].

A relevant distinction between the British and the Canadian case is that the power of the proxy holder to vote against the amendment and thus in favour of the proposal as it originally stood was in question in the British case while the contrary was true in the Canadian case. It must be easier to hold that the proxy holder has the power to vote on an amendment when what he seeks to do is to observe the letter of his instructions than when he seeks to abandon the letter of his instructions arguing that by so doing he will be better serving his principal's interests. However, it appears that the courts will be much readier to allow this flexibility in the case of a proxy relationship than in the case of any other agency relationship[244].

The reason, it is suggested, that the court is willing to allow the proxy holder a certain discretion in interpreting his instructions is that the proxy holder is not solely responsible for the decisions that will result from the exercise of his powers. Further, unless the proxy holder is to be allowed some degree of discretion, the corporate meeting concept which puts a value on the interaction of those present at the meeting as conducive to producing a reasoned decision must be abandoned and a postal ballot or some other device for registering an absolute vote be substituted for the proxy vote.

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243. *Re Langley's Ltd* [1938] 3 DLR 230, 245.
244. Cohen, *Introduction* to Aranow and Einhorn, *op cit*, xiv-xv.

E. ACCESS TO THE CORPORATE PROXY SYSTEM

Subsequent to and depending upon the decisions cited above to the effect that corporate funds could properly be expended in efforts to solicit proxies, it has become common practice in Australia, as in both Britain and North America, for the managements of listed companies to solicit proxies from their shareholders. This operation is staffed by company employees and funded from company assets, thus it is necessarily under direct management control. Nevertheless, it should be remembered that this machinery is designed to serve corporate purposes and not exclusively management purposes. Now this proxy system has developed to the point where it supplants the shareholders meeting in some cases[245]. In these circumstances it is appropriate to ask whether the proxy system effectively fulfils all the roles of the shareholders' meeting or whether certain traditional shareholder rights will be lost by the substitution of the proxy process for the meeting. In analysing the proxy system with this question in mind, concern centres on the question of individual access to the machinery.

Theoretically the shareholders' meeting is an assembly at which members of the company may propose, consider and decide upon proposals for company action. At one stage in the evolution of the proxy, the shareholder who chose to delegate his powers customarily did so with few restrictions. However, under the proxy rules in force in the United States, as under the Stock Exchange Listing Requirements here, the shareholder whose proxy is solicited must be given an opportunity to limit his proxy

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245. Eisenberg, *Access to the Corporate Proxy Machinery, op cit*, 1494; see also Schwartz, D.E. and Weiss, E.J., "*An Assessment of the SEC Shareholder Proposal Rule*." (1977) 65 Geo LJ 635.

holder's powers by use of a two-way proxy form. The shareholder's powers of decision have thus effectively been restored to him. But the use of the proxy system also affects his rights to put forward proposals. Even where the shareholder himself attends the general meeting, if he addresses not his fellow shareholders but a pile of proxies[246], his right to make a proposal at the meeting will be ineffective. In such circumstances a proposal may only be made effectively where access to the proxy statement, that is, to the statement sent out by management when it solicits proxies, outlining the questions to be presented to the meeting, is possible. It is, of course, possible for a shareholder who wishes to undertake the effort to solicit his own proxies, but is there any alternative available to him? Does the individual shareholder have access to the corporate proxy system?

The common assumption, as Eisenberg asserts[247], is that, in the absence of any statutory provision, the law gives management virtually exclusive access to this machinery. In the United States, the Securities and Exchange Commission's shareholder proposal rule is an obvious exception, but this exception does not include proposals relating to the election of individual officers, that is, to nominations of candidates, nor does it include counter-proposals to management resolutions[248]. Eisenberg has therefore looked beyond this rule in an effort to discover whether access is barred as a general rule. It is his contention that the common assumption that, in the absence of statute, management's access is virtually exclusive is

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246. *Hearings HR 1413, HR 1821 and HR 2019 Proxy Rules before the House Committee on Interstate and Foreign Commerce,* 78th Cong 1st Sess 174-175 as quoted by Schwartz, *op cit,* 1139 n 4.
247. Eisenberg, *op cit,* 1491.
248. CFR s 240.14a-8(a).

wrong in principle[249]. Because there is little or no direct authority to bar shareholder access to the corporate proxy machinery, Eisenberg refers to general corporate principles, which he elaborates in the light of considerations of practicality and policy, to support his contention.

As far as access to the corporate proxy machinery in connection with the election of directors is concerned, Eisenberg questioned both whether management access to this machinery for this purpose could be justified and whether shareholder access could be denied. Pointing out that corporation law generally vested the power to elect directors in the shareholders, and that the distinction between questions of personnel and questions of policy drawn by the courts in validating corporate expenditure on proxy contests was an attempt to conform to this principle, he concluded that the policy-information reasonability test was fundamentally defective. Its fault was that it lost sight of the statutory principle that a director serves only a limited term of office, a principle designed to ensure that shareholders have the right to elect new directors who favour policy changes and that an incumbent board has no authority to address itself to the policy the corporation should follow after the expiration of its term of office. Furthermore, in considering such a question, he contended, the board inevitably put itself in a position where the individual interests of the directors would conflict with their fiduciary duty to the company. An incumbent whose re-election is at stake could not be expected to take an even-handed approach to the policy issues at stake in the election. Eisenberg did, however, offer as a justification for the expenditure of corporate

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249. Eisenberg, *Access, op cit*, 1492.

funds to support management candidates for directorships the argument that this could prevent corporate offices from falling inexorably into the hands of those who have personal funds to expend on proxy campaigns. Management, in his view, should be permitted to meet the insurgents on equal terms but not to outspend them vastly at the expense of the corporation. Management expenditure to support its position from corporate funds should be subjected to a test which would allow it to match but not to exceed the expenditure of the insurgents[250].

General corporate principles will, Eisenberg argues, entitle shareholders to nominate candidates for corporate office in the corporate proxy materials. His chief argument to this effect is that such a right is a corollary to the exclusive power granted to shareholders under American statutes to elect the board of directors. To deny the shareholders access to the corporate proxy materials is virtually tantamount to giving management power to elect the board. This argument is supported by subsidiary arguments to the effect that corporate funds and facilities cannot be applied to the personal benefit of directors and that corporate assets cannot be applied to the benefit of individual shareholders in a non-even-handed manner. Shareholders as a body, he concludes, have the right to designate candidates for corporate office in the corporate proxy materials although such a right would be subject to regulation by corporate by-laws[251].

When it comes to a question of practicalities, Eisenberg suggests that shareholders should be permitted to designate candidates for directorships through the proxy materials sent out by corporate management by a

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250. Eisenberg, *Access, op cit*, 1491-1502.
251. *Ibid*, 1502-1511.

method analogous to that currently applied to shareholder proposals. The importance of his suggestion is that a revision of the proxy rules would not be necessary to allow a corporation to make such a right available to the shareholders, although such a revision might still be necessary to allow the shareholders to enforce the right where managements were unwilling to concede it. Eisenberg himself suggests that corporations which deem an unrestricted shareholder right to designate candidates impracticable can adopt a by-law limiting the right to shareholders owning in the aggregate some minimum percentage of the shares[252].

Access to the corporate proxy materials in connection with matters other than election to office does not present problems of the same order. Management will often have explicit statutory authority to put these matters before the shareholders and solicitation of proxies will frequently be necessary to obtain the necessary approval for major corporate transactions. Furthermore, in these instances if the board is motivated by self-interest, its actions are readily subjected to scrutiny. Shareholder access to the proxy materials sent out by corporate management for the purpose of putting proposals other than counter-proposals to management initiatives is presently covered by the shareholder proposal rule mentioned above. As far as access to the proxy machinery for the purpose of putting forward such counter-proposals and counter-arguments is concerned, Eisenberg does not advocate such a right. He sees substantial problems of feasibility involved and states that the absence of such a right does not lead to the presentation of a one-sided view inasmuch as management is required to disclose all relevant information in the materials it issues[253].

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252. Eisenberg, *Access, op cit*, 1502-1511.
253. *Ibid*, 1517-1524.

Eisenberg's arguments are, it is submitted, sound and persuasive; however, his conclusions do not correspond with present reality. R.N. Schwartz, writing four years after Eisenberg's arguments were first published, stated not only that Eisenberg failed to cite a single case in support of his argument that existing corporation law entitles shareholder nominees for director to be designated in the corporation's proxy materials but, further, that he, Schwartz, had been unable to discover any case based on that rationale and considered it unlikely that any state court would so hold[254]. Schwartz therefore argued that steps should be taken to secure the adoption by way of legal reform of some measure to guarantee the shareholder the right to nominate candidates for the office of director. Having canvassed the various means by which this could be done, he concluded that amendment of the proxy rules would be the best possible method[255]. Another American commentator reviewed various methods to make corporate elections more open and noted that management could include in its proxy material, without charge, additional nominations made by shareholders, a step which would go a long way towards making proxy solicitations more open and would help put outside groups on a more equal footing with management[256]. He too made reference to the possibility of the revision of Schedule 14-A to make such inclusion mandatory. It should therefore be noted with interest that the recent Securities and Exchange Commission inquiry did address the question[257]. However, the question is controversial and action on this particular aspect of the inquiry will accordingly be delayed[258].

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254. Schwartz, R.N., *op cit*, 1152-1153.
255. *Ibid*, 1157.
256. Feis, W.J., *"Is Shareholder Democracy Attainable?"* (1976) 31 Bus Law 621.
257. SEC Release No 34-13482 (5.4.1977); SEC Release No 34-13901 (8.31.1977).
258. SEC Release No 34-14970 (7.10.1978).

Having examined the theoretical arguments advanced in the United States for giving the shareholder access to the corporate proxy materials, it is still necessary to turn our attention briefly to the Securities and Exchange Commission's Proxy Rule 14a-8 governing shareholder proposals[259]. It has been said of this rule, because it permits a direct participation by shareholders in the affairs of every corporation whose proxy solicitations are subject to the rules, that it represents a last outpost of corporate democracy[260], and undoubtedly it does offer the individual shareholder access to corporate decision-making. It permits any shareholder who complies with the rule and whose proposal does not fall within the provisions allowing management to exclude it, to put forward a proposal, to be voted on at the general meeting, in the proxy form. The principal substantive exclusion is of those proposals not deemed to be a proper subject for action at the general meeting. As this question is related to the question of division of powers between the general meeting and the board of directors, it has been considered at length in that section of the thesis. It is considered unnecessary now to explore the details of those rules which establish the threshold requirements

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259. See generally Allen, P.H.,*"The Proxy System and the Promotion of Social Goals"* (1970-71) 26 Bus Law 481; Bane, C.A.,*"Shareholder Proposals on Public Issues"* (1970-71) 26 Bus Law 1017; Bayne, D.,*"Basic Rationale of Proper Subject"* (1957) 34 U Det LJ 575; Chilgren, A.D., *"A Plea for Relief from Proxy Rule 14a-8"* (1963-64) 19 Bus Law 303; Clusserath, T.M.,*"The Amended Stockholder Proposal Rule, A Decade Later"* (1964-65) 40 ND Law 13; *"Comment: SEC Shareholder Proposal Rule 14a-8 Impact of the 1972 Amendments"* (1972-73) 61 Geo LJ 781; Manne, H.G.,*"Stockholder Proposals Viewed by an Opponent"* (1972) 24 Stan L Rev 481; *"Note: Liberalizing SEC Rule 14a-8 through the Use of Advisory Proposals"* (1971) 80 Yale LJ 845; *"Note: Proxy Rule 14a-8: Omission of Shareholder Proposals"* (1971) 84 Harv LR 700; Schulman, S.,*"Shareholder Cause Proposals: A Technique to Catch the Conscience of the Corporation"* (1971-72) 40 Geo Wash L Rev 1; Silvers, M.H.,*"Shareholder Proxy Rules"* (1976) 1 Glendale L Rev 317; Thorson, L.J.,*"The Ethical Investor and the SEC"* (1976) 2 J Corp Law 115.

260. Black, L.S. and Sparks, A.G.,*"The SEC as Referee"* (1976-77) 2 J Corp Law 1.

and administrative framework for the application of the rule. As a matter of general policy, the rule is designed to allow proposals in which shareholders are interested and upon which they should act, and to screen out those which would supersede the directors' role in the corporation and which are designed to capture the corporate proxy machinery to publicize matters which interest only a small minority of shareholders[261].

In Australia, the provisions which make it mandatory for a company on the requisition of its members to give notice of a resolution to be proposed at the next general meeting[262] serves a similar function to the shareholder proposal rule. A significant difference is found, however, in the provision that this shall be done at the expense of the requisitionists. This stipulation should, it is submitted, be abolished. There are other ways to ensure that the provision is not used frivolously or to harass company management[263]. To penalize the shareholder for taking an interest in his company is bad policy. It may be noted that the American experience indicates that such proposals may significantly affect company policy even if they are not adopted[264]. No separate consideration has been given in Australia to the question of access to the materials sent out by the company together with the proxy forms circulated by management. This omission should be remedied and in particular

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261. Black and Sparks, *op cit*, 6.
262. UCA s 143.
263. See above, 239; see also Ontario Legislative Assembly, *Interim Report of the Select Committee on Company Law*, (1967) para 8.4.3; *Dickerson Report*, *op cit*, para 289.
264. Black and Sparks, *op cit*, 2 citing Roche, *Ethics Social Responsibility Resolutions Lost Again in '76 but Activists Did Score*, Wall Street Journal 25 May 1976 at 11, col 1; Cohen, *op cit*, 102.

consideration should be given to revising nomination procedures so as to allow the shareholder some scope for nominating candidates for the position of director, rather than leaving this privilege exclusively to management.

F. THE ROLE OF THE SECURITIES AND EXCHANGE COMMISSION

The Securities and Exchange Commission has played an important role in the United States of America in the development of the law governing the solicitation and use of proxies since the mid-1930's. The basis of this role is the legislative provision which makes it unlawful for any person to solicit any proxy in contravention of such rules and regulations as the Commission may prescribe as necessary or appropriate in the public interest or for the protection of investors[265]. Acting under this power, the Commission began to regulate proxy solicitation in 1935 and, although since that time the rules have undergone several major revisions[266], the procedure they lay down has remained substantially the same. Proxy material must be filed with the Commission in preliminary form a stilupated time before it is to be issued. This allows the Commission staff to review it with an eye to ensuring that it is properly informative and avoids misstatements. Where a proxy contest is under way or management is opposing a shareholder's attempt to have a proposal included in the material, the Securities and Exchange Commission's

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265. Securities Exchange Act, 48 Stat 895 (1934) s 14(a), 15 USC s 78 n(a); see *Securities and Exchange Commission* v *O'Hara Re-election Comm* (1939) 28 F Supp 523 (D Mass) as discussed by Aranow and Einhorn, *op cit*, 451-455.

266. Silvers, *op cit*.

role resembles that of a referee[267], although the power to formulate the rules of the contest may lead to a confusion of roles. Staff recommendations will be communicated to those who have filed the materials and a process of negotiation may follow, culminating in the production of approved materials. Alternatively, on the request of one of the applicants, the staff recommendation may be referred to the Commissioners for review, and it has recently been established that the decision of the Commission will be reviewable by the courts[268].

The Commission has no independent authority to prevent or suspend a proxy solicitation if any person should proceed in contravention of the proxy rules. However, it does have authority to seek an injunction from the courts to enforce the proxy rules[269]. On the motion of the Commission, courts have prevented the use of proxies obtained in violation of these rules, and have postponed the meeting to which they are related[270].

The powers of the equivalent Canadian Commissions are not nearly so extensive. Numerous details which are laid down in the Securities and Exchange Commission's proxy rules are prescribed by the legislation itself in Canada[271]. Further, the Kimber Committee decided against recommending that material be filed with the governmental agency before it is issued to the shareholders[272], and accordingly the only requirement is that a copy of the circular be sent to the Director of Companies

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267. Cohen, *The SEC and Proxy Contests*, *op cit*, 97
268. *Medical Comm for Human Rights* v *Securities Exchange Commission* (1970) 432 F 2d 659 (DC Cir) discussed by Allen, *op cit*, 488-490. Cohen's argument that these decisions are not reviewable (Cohen, *op cit*, 103) is now of mere historical interest.
269. Securities Exchange Act, 48 Stat 895 (1934) s 21.
270. *Securities Exchange Commission* v *O'Hara Re-election Comm* (1939) 28 F Supp 523, cited by Aranow and Einhorn, *op cit*, 451-452.
271. See above, Part B generally.
272. *Kimber Report*, *op cit*, para 6.26; Getz, *op cit*, 41.

when it is sent to the shareholders[273]. Whether the various governmental agencies may sue to prevent violations of the new proxy legislation is a question that has yet to be answered[274]. Similarly, the scope of a private right of action to enforce this legislation is also unclear, although there is a decision arising under the Ontario legislation in which the question was adverted to[275]. However, the case was decided on other grounds. The judge, in referring to the point in issue, apparently took the view that the duty in question existed independently of the proxy legislation and was owed to the company rather than to the individual shareholders, so that the rule in *Foss* v *Harbottle* became applicable. As the plaintiff shareholders, although the action was not in derivative form, succeeded on other grounds, this holding may be regarded as *obiter*. It is still possible to hope that this approach will not prevail. It is the writer's view that this approach would go far to defeat the aims of the new legislation, which is to limit the power management derives from its control of the mechanisms of the company meeting, and should not be adopted.

Clearly the Canadian legislators have not regarded the establishment of a governmental agency with the extensive powers of the Securities and Exchange Commission as a necessary adjunct to closer regulation of the solicitation and use of proxies. Nevertheless, the question may be posed whether such a bureaucratic structure could be readily set up in Australia. The powers of the American Commission differ in two regards from those presently accorded to the Corporate Affairs Commissions. The

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273. Can Bus Corp Act s 144(2). The Bus Corp Act (Ont) does not require any filing of proxy information but does contain a provision to penalize false statements: s 256.

274. Getz, *op cit*, 42-48.

275. *Charlebois* v *Bienvenue* (1967) 64 DLR (2d) 683, discussed by Getz, *op cit*, 45.

Australian Commissions do not presently enjoy wide regulation-making powers and, further, the checking procedures which they currently employ are largely mechanical.

Although the Commissions' duties in checking prospectuses may extend beyond a duty to ensure that the prospectus complies with the statute[276], this is not true generally where the statute requires documents to be registered with the Commission. Indeed, in a recent decision of the Queensland Supreme Court[277], it was held that the principle of company law which prevents the court from interfering in the internal management of companies also prevents the Commissioner from refusing to register a document which on its face complies with the statutory requirements[278]. The effect, as Baxt points out, is to prevent the Commissioner from acting as a kind of ombudsman for the shareholders in order to dig out information which would allow them to challenge certain courses of conduct by the directors[279]. The decision constitutes the first time in recent years that the courts have examined the power of an Australian authority to act in a capacity not unlike that of the American Securities and Exchange Commission[280].

The question of granting rule-making powers to a governmental Commission arose for consideration when the Corporations and Securities Industry Bill was investigated by a Senate Sub-Committee in 1973. That bill proposed to set up a Commonwealth Commission which would have extensive

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276. UCA s 42(2)(d); and see *Sen Sel Comm Rep, op cit,* 798-799, testimony of Commissioner Ryan.
277. *Mutual Home Loans Fund* v *Commissioner of Corporate Affairs* (1978) CCH Corp Affairs Reporter para 40-436.
278. *Ibid,* para 30-080 per Campbell J.
279. Baxt, R., *Note* in *Chartered Accountant in Australia,* Nov 1978, 36-37.
280. *Idem.*

rule-making powers. Numerous objections to this feature of the Bill were expressed. The basis of these objections was that it is a tenet of our system of government that no substantive provision of law should be embodied in a regulation rather than in a statute[281]. Those witnesses not inexorably opposed to such rule-making power were concerned to narrow the scope of the power[282], to require a process of consultation before it was exercised[283], and to make it subject to review[284]. The normal procedure for regulations dealing with procedural matters is that they must be tabled in Parliament and are subject to disallowance, but in this case proposals were put forward to require positive affirmation of such rules by Parliament[285]. Concern was also expressed over the proper relationship between the Government and the Commission. The Attorney-General's submission put the argument that, as the Government was responsible for legislation, the proposal to give the Governor-General in Council additional powers to make regulations independently of the Commission and also the proposal to allow the Attorney-General to give policy directives to the Commission were justified[286]. Other witnesses argued that the Commission's independence should be a fundamental principle[287]. Finally, suggestions were made that if such a rule-making power were to be entrusted to a Commission it would be necessary to set up a Senate Standing Committee, on the American model, to supervise its activities[288]. It therefore appears that there are problems of constitutional principle which make it unlikely that Australia

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281. *Sen Sel Comm Rep, op cit,* 17, 313, 1267, 2279, 2382, 2682, 2725, 3332.
282. *Ibid,* 1446, 2382, 2517, 3341.
283. *Ibid,* 315, 1447, 2724.
284. *Ibid,* 17-20, 489, 1468, 2278, 2411.
285. *Ibid,* 18, 2278, 2287, 2411, 2679.
286. *Ibid,* 377, 489, 506.
287. *Ibid,* 320, 2287, 2518.
288. *Ibid,* 19, 1450.

could successfully set up a governmental agency fully analogous to the Securities and Exchange Commission and the fact that such an agency, on the basis of the Canadian experience, does not appear to be a necessary adjunct of closer proxy regulation should be carefully noted.

G. CONCLUSION

In this section of the thesis, one aspect of the machinery of corporate democracy has been examined in detail. The first step in this examination was to weigh the arguments against the use of the proxy voting device. It was concluded that, in large companies having a share capital, some device for allowing absentee voting was essential and therefore that proxy voting should be a statutory right of members in such companies. The second step was to examine the details of the proxy machinery; in the course of this examination certain improvements were suggested. The third step of this treatment of the proxy device was an attempt to come to grips with the concept of solicitation which was subsequently seen to affect relationships between the proxy holder and the shareholder. In the last two sections an attempt was made to deal with two aspects of proxy regulation which are not as yet live questions in Australia: the role such regulation should play in giving the shareholder access to the corporate decision-making process and the rule of a bureaucratic agency in forming and enforcing such regulation. It is suggested that many reforms in this area can be adopted without giving any governmental agency such power as the Securities and Exchange Commission has in the United States of America. One issue which has not been treated here is the role of proxy regulation as a scheme for providing the shareholder with more information about the company. This omission is explained by the writer's intention to deal with all disclosure

provisions together in Part VI of this thesis. It was felt that the matters explored were important enough to merit separate treatment.