SHAREHOLDER APPROVAL OF FUNDAMENTAL CHANGE? AN ANALYSIS OF S 129 OF THE COMPANIES ACT 1993 (NZ)

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I. THE STATUTORY FRAMEWORK

Section 129 of the *Companies Act 1993* ('the Act') was proposed by the New Zealand Law Commission in 1989 as both a regulatory and governance strategy. For s 129 provides that a company must not enter into a major transaction, unless the transaction has been approved by a special resolution[1] of shareholders or is contingent on such approval being obtained. A major transaction is defined in s 129(2) in relation to a company as follows:

(a) the acquisition of, or an agreement to acquire, whether contingent or not, assets the value of which is more than half the value of the company's assets before the acquisition; or
(b) the disposition of, or an agreement to dispose of, whether contingent or not, assets of the company the value of which is more than half the value of the company's assets before the disposition; or
(c) a transaction that has, or is likely to have, the effect of the company acquiring rights or interests or incurring obligations or liabilities, including contingent liabilities,[2] the value of which is more than half the value of the company's assets before the transaction.

This section was part of a package of reforms proposed by the Law Commission in its 1989 Report*, Company Law: Reform and Restatement*[3] (the 1989 Report) to create a 'comprehensive system for protection of minority shareholders'.[4] This package also included the introduction of buy-out rights,[5] which are more commonly known as 'appraisal rights' in North American corporate law. Buy-out rights operate to provide minority dissenting shareholders, who have voted against a special resolution to approve a major transaction, with an avenue to exit the company by having their shares acquired by the company[6] or a third party,[7] subject to certain financial safeguards contained within the Act.[8] Like its North American counterparts, unsuccessfully voting against a major transaction is not the only pathway to be entitled to exercise such rights. The other triggering transactions specified in the Act[9] are when a shareholder votes against a special resolution to adopt, alter or revoke a constitution and the proposed alteration imposes or removes a restriction on the activities of the company;[10] when a minority shareholder votes

1 *Companies Act 1993* (NZ) s 2 defines 'special resolution' as a resolution approved by a majority of 75 per cent or, if a higher majority is required by the constitution, that higher majority, of the votes of those shareholders entitled to vote and voting on the question.'
2 *Companies Act 1993*(NZ) s 129(2B) provides that matters similar to those relevant to the solvency test under s 4 are to be considered when determining the value of a contingent liability.
3 New Zealand Law Commission, *Company Law: Reform and Restatement,* Report No 9 (1989).
4 Ibid 2.
5 Buy-out rights in a limited form already existed in New Zealand corporate and securities law. Section 208 of the *Companies Act 1955* (NZ) applied to a shareholder who dissented from an offer to purchase all the shares of the company and of which 90% of other shareholders have accepted; replaced by Part 7 of the *Takeovers Code Approval Order 2000* (NZ) and s 209 of the *Companies Act 1955* (NZ) which conferred a power on the High Court to order various forms of relief including the purchase of the minority shareholders shares if just and equitable to do so.
6 *Companies Act 1993* (NZ) s 112.
7 *Companies Act 1993* (NZ) s 113.
8 *Companies Act 1993* (NZ) ss 114-5.
9 *Companies Act 1993* (NZ) s110.
10 *Companies Act 1993* (NZ) s 110(a)(i).

against a resolution to change class rights;[11] and also when a shareholder votes against a long-form amalgamation pursuant to s 221 of the Act.[12]

This paper focuses on the 'major transaction' approval requirements. Following an overview of the background to and objectives behind the introduction of the section, it examines the relatively sparse number of cases that have considered the section to date. As the New Zealand Law Commission in 1989 identified the Canadian corporate law statutes as working models for the new Act,[13] the paper then contrasts the essentially quantitative formulation contained in s129 with the more qualitative test in the Canadian Business Corporations Act and considers whether the quantitative, bright line formulation of fundamental change adopted in New Zealand has achieved its legislative objectives.

II. BACKGROUND AND OBJECTIVES

A. Shareholder Protection

Although the principal purpose of a Memorandum of Association was to govern the relationship between the company and the outside world,[14] limits on the capacity of the company contained in a Memorandum also operated to protect shareholders from uncontrolled and unforeseen changes in business direction. However, one consequence of the development through the 20th century of all-purpose object clauses in a Memorandum of Association, was a decline in the importance of this constitutional document, ultimately, to its statutory demise. In New Zealand, by 1984, the *Companies Act 1955* had been amended to provide that, subject to certain conditions,[15] companies had the rights and powers of a natural person.[16] This evolution in the vast majority of companies effectively removed any real protection afforded to shareholders from fundamental changes to the nature of the business of such companies. The New Zealand Law Commission observed, in its 1987 discussion paper, 'Company Law',[17] that since the 'abolition of the *ultra vires* doctrine it may be said that shareholders have insufficient protection against substantial and rapid change which may transform the nature of the business'.[18]

This discussion paper identified a number of options for reform including a proposal that all substantial decisions be passed or ratified by the same majority of shareholders as is required for alteration of class rights, and by providing for buy-out rights for those who dissent.[19] However, the Law Commission at that time was not convinced of the necessity of these reforms. The Commission considered that courts already had the power to require a company to acquire minority dissenting shareholders shares under s 209 of the *Companies Act 1955*, taking into account that this section had been amended in 1980 to enlarge the range of circumstances in which a court had the power to intervene in cases of shareholder oppression. Also, the Law Commission stated 'there may be substantial

11 See *Companies Act 1993* (NZ) s 118, where a shareholder that has voted against a special resolution that affects the rights attached to shares (as that term is defined in s 117(2)) is thereby entitled to require the company to purchase those shares in accordance with s 111 of the Act.

12 *Companies Act 1993* (NZ) s 110(d) further provides that if the triggering resolution as set out in s 110(a)(i) or (ii) is passed by under section 122 by a resolution in lieu of meeting, then the right to require the company to acquire a shareholder's shares under s 111 arises upon the shareholder not signing the resolution. Section 122(1) requires that for a resolution in lieu of notice to be as valid as if it had been passed at a meeting of shareholders, it must be signed by (a) 75 per cent or (b) such other percentage as the constitution may require for passing a special resolution, whichever is the greater, of the shareholders who would be entitled to vote on that resolution at a meeting of shareholders who together hold not less than 75 per cent (or any higher percentage as required by the constitution) of the votes to be cast on that resolution.

13 New Zealand Law Commission, above n 3, [32-3].

14 John Farrar & Mark Russell, *Company Law and Securities Regulation in New Zealand,* (1985) 62.

15 Companies registered before 1 January 1984 continued to be regulated by the Second Schedule of the *Companies Act 1955* (NZ) and the list of 'incidental and ancillary' objects and powers therein listed unless the company had expressly adopted the new section 15A setting out that the company had the right, powers and privileges of a natural person.

16 *Companies Act 1955* (NZ) s 15A.

17 New Zealand Law Commission, *Company Law — A Discussion Paper,* Preliminary Paper 5 (1987).

18 Ibid [278].

19 Ibid [278].

difficulties in defining fundamental change.'[20] However, in the 1989 Report, the New Zealand Law Commission abandoned such reservations and recommended the adoption of major transaction and buy-out right provisions, including potential provisions in the draft *Companies Act* that formed part of this Report. The Law Commission had concluded that the oppression remedy then contained in s 209 was an insufficient remedy in itself as buy-out rights would arise on the occurrence of certain changes to a company, its activities or rights attached to shares, regardless of 'whether or not the action taken by the company is unfairly prejudicial to the shareholder.'[21] As Vanessa Mitchell in 1996 observed, the Law Commission views when read together with the legislation 'appear to be saying that something can be 'unfair' without necessarily being "unfairly prejudicial"'.[22]

B. Increased Shareholder Determination

The major transaction requirement in the 1989 Report formed part of a larger package of reforms designed to increase shareholder protection from abuse where management of the company is given to the directors.[23] Shareholder determination was identified as one method to increase protection from such abuse. Section 129 is located in Part 8 of the Act, which is headed 'Directors and Their Powers and Duties', and specifically is grouped with two other sections under the heading 'Powers of Management'.[24] Accordingly, the inclusion of the 'major transaction' provision in the Act must not only be viewed as a conduit for minority shareholders to exit a company, but also as a strategy to increase the rights of shareholders as a class. The requirement that 75 per cent of shareholders must confirm or ratify fundamental transactions ensures the alignment of the interests of the board with those of the shareholders. Finally, its enactment can also be seem as facilitating the rights of the majority to use the corporate structure for legitimate entrepreneurial activity, without being concerned with a disaffected minority.

One of the underlying tensions in modern corporate law, with its concentration on the importance of delegation of management to the board, is the problem of optimal delegation. As Kraakman and others stated in their seminal text, *The Anatomy of Corporate Law,*[25] while 'the efficiencies of the corporate form require centralizing management power, shareholders need not (and generally do not) delegate all authority to act for the corporation to the board of directors'.[26] They identify shareholder decision rights in this context as a governance strategy, expanding the rights of principals to intervene in a firm's management, albeit as *ex post* ratification of the most fundamental corporate decisions. This role of s 129 as a governance strategy to reduce agency costs is often overlooked in commentary and case law. However, this attitude is not surprising given that Kraakman and others comment that a corporate law system's decision rights strategies will be much less prominent than its appointment rights strategies. Moreover, this 'disparity is a logical consequence of the fact that the corporate form is designed as a vehicle for the delegation of managerial power and authority to the board of directors.'[27]

20 New Zealand Law Commission, above n 17, [281]. In this paragraph, the Law Commission also observed that if a company wanted buy-out rights to be triggered on the happening of certain events, then a company could chose to include a provision to this effect in its articles, although this observation was clearly contingent on the proposed recommendation, also contained in the discussion paper, that the existing strict rules on a company purchasing its own shares should be relaxed.

21 Above n 3, [202].

22 Vanessa Mitchell, 'The US Approach Towards the Acquisition of Minority Shares: Have We Anything To Learn?' (1996) 14 *Company and Securities Law Journal* 283, 306.

23 New Zealand Law Commission, above n 3, [85].

24 The other two sections are s 128, which sets out the rights of the board to manage the company, and s 130 that establishes which powers of the board they may delegate.

25 Reinier R Kraakman et al, *The Anatomy of Corporate Law: A Comparative and Functional Approach* (2004).

26 Ibid 131.

27 Ibid 26.

C. Buy-out Rights

In terms of buy-out rights, the rationale put forward by the Law Commission reflects the current North American 'appraisal right' rationales[28] based on shareholder expectations and fairness for minority shareholders (rather than shareholders generally). At paragraph 499 of the 1989 Report, the Law Commission states that the provision is:

> [b]ased on the view that some dealings have such far-reaching effects that they should be referred to shareholders. Shareholders should not find that massive transactions have transformed the company they invested in without warning. Clearly, unless the constitution of a company restricts its activities, all shareholders will have to accept a large measure of change. Normally that may be achieved over some time, permitting the shareholder who does not like the direction the company to leave or to exercise his rights to call management to account. What we are concerned with is abrupt and substantial change which transforms the nature of the enterprise.[29]

Buy-out or appraisal rights provisions were included in the Act among a number of other reforms designed to increase minority shareholders rights and protections, although the introduction of this concept into New Zealand corporate law formed a central platform of the reforms.[30] The 1989 Report further provides that buy-out rights create a mechanism for dissenting shareholders to exit a company, when that company has undertaken a 'level of change to which it was unreasonable to require shareholders to submit'[31] and that this remedy arises 'where there is an alteration of class rights or a fundamental change to the company',[32] and therefore a 'dissenting shareholder does not inevitably have to accept the majority decision. The shareholder will instead have the option of leaving the company.'[33] Kraakman and others discuss exit rights in agency theory terms. They argue that the corporate law adopted by a jurisdiction should include, as a regulatory strategy, controls as to how principals can enter and exit from a relationship with particular agents.[34] By the use of regulations in this regard, corporate law can attempt to reduce agency costs between shareholders as principals and their agents. Kraakman and others identify buy-out or appraisal rights as one method of allowing a principal to escape opportunistic agents *ex post.* Dissenting shareholders can avoid a prospective loss if they believe a proposed major transaction is a value reducing decision.

Many commentators originally viewed the inclusion of these two connected reforms as an important innovation of the new Act. As David Goddard[35] stated in 1997,[36] the fact that '[t]he majority of shareholders (for major decisions, a 75 per cent majority) has been given much greater freedom to make decisions regarding the future of the company, with the remedy for an aggrieved minority shareholder being (able to) exit at a fair price'[37] was one of the successes of New Zealand's new company law. However, as is the case with many great ideas, the devil is in the detail and subsequent cases have undermined its potential.

28 In fact, the historic justification for appraisal rights was compensation for the loss of the unanimous consent requirement for shareholder agreement to change. See Barry M Wertheimer 'The Shareholders' Appraisal Remedy and how Courts determine Fair Value' (1998) 47 *Duke Law Journal* 613.

29 The New Zealand Law Commission, above n 3, [499].

30 The New Zealand Law Commission identifies these other reforms as including provisions to grant standing to shareholders to enforce through the courts, obligations owed to the company and directly to shareholders. See New Zealand Law Commission, above n 3, [10].

31 Ibid [206].

32 Ibid [202].

33 Ibid [203].

34 Kraakman, above n 25, 25.

35 David Goddard, 'Company Law Reform — Lessons from the New Zealand Experience' in Andrew Borrowdale, David Rowe & Lynne Taylor (eds), *Company Law Writings: A New Zealand Collection* (2002) 145.

36 Ibid. Footnote 1 explains that although this article first appeared in (1998) 16 *Company and Securities Law Journal* 236, the article had been developed from a paper presented at a 'conference on Australia's Corporate Law Economic Reform Program (CLERP) in Canberra in November 1997.'

37 Goddard, above n 35, 152.

III. QUANTITATIVE TEST?

A. Inconsistent Approach

Although the Law Commission described the intended purpose for s 129 in its 1989 Report in terms of the need to protect shareholders from 'massive transactions' and from 'abrupt and substantial change', the test for major transactions used in the Draft Act which was attached to that Report and in the *Companies Act 1993* by contrast is quantitative in nature — for the s 129 (2) definition focuses on whether the value of the proposed transaction is more than half the value of the company's current assets.[38] Boards are called upon to assess if a proposed transaction has a value greater than 50 per cent of the existing value, in monetary terms, of the entity before the transaction. The inconsistency between these approaches was highlighted in the 2004 High Court decision of *Re Fletcher Challenge Forests Ltd.*[39] This case arose out of a complex series of transactions to be undertaken by various subsidiaries of Fletcher Challenge Forests Ltd (FCF). FCF was a holding company and listed on the New Zealand Stock Exchange. Its assets comprised shares in, and loans to, its various subsidiary companies, including three companies which owned certain forestry assets that were proposed to be sold. It was not disputed that the value of the forest assets to be sold by each subsidiary was more than half the total value of each subsidiary's assets before the sale transaction. Accordingly, each sale was required to be approved by special resolution of the shareholders which, given their subsidiary status, was not problematic.

The matter came before the court as FCF sought a declaratory judgment, that although the value of the assets to be disposed of by the subsidiaries was more than half the value of FCF's total assets before the proposed sales, FCF was not itself undertaking a major transaction. This was on the basis that it was not disposing of its assets or incurring obligations or liabilities and FCF was not a party to any of the transactions.[40] Counsel appointed to represent the contrary view to the company argued at paragraph 36 that to 'interpret the section as other than including the holding company and its subsidiaries would be to utterly defeat the purpose of the section'. However, Justice Salmon preferred FCF's argument that there 'is nothing in the Act itself which would support an interpretation for s129 different to that conveyed by the words used'.[41] Accordingly, in his Honour's opinion, as the words of the statute are clear, it was not permissible to find a context outside of the words used, regardless of the fact 'the observations of the Law Commission seem to be at odds with the wording of the section prepared by the Commission.'[42] Therefore, the quantitative nature of s 129 did not allow an extended interpretation of the section and must be strictly construed as applying to the value of assets and liabilities of only one company.[43]

B. Quantitative Approach: An exclusive Test?

However in a subsequent case, the High Court in *Central Avion Holdings Ltd v Palmerston North City Council & Anor*[44] took a less literal approach when deciding whether a certain transaction needed to comply with s 129. This cause of action was secondary to the primary claims of unfair prejudice under s 174 and of undue influence over the majority shareholder's nominee directors on the board of the company, Palmerston North Airport

38 *Companies Act 1993* (NZ) s 129(2). This defines 'assets' to include property of any kind, whether tangible or intangible.
39 (2004) 9 NZCLC 263,447.
40 Also, as Fletcher Challenge Forest Ltd's (FCF) constitution required a special resolution when the company, including its subsidiaries, entered a transaction that may have changed the essential nature of the FCF business or the gross value of the transaction was in excess of the 50% of the lesser of the average market capitalisation of FCF or the gross value of assets of the FCF Group in accordance with the New Zealand Stock Exchange Listing Rules, declarations as to these matters were also sought.
41 *Re Fletcher Challenge Forests Ltd* (2004) 9 NZCLC 263,447, [37].
42 *Re Fletcher Challenge Forests Ltd* (2004) 9 NZCLC 263,447, [40].
43 *Re Fletcher Challenge Forests Ltd* (2004) 9 NZCLC 263,447, [40].
44 [2006] HC CIV 2003-454-559 (Unreported, Goddard J, 15 June 2006).

Ltd (PNAL). The origin of the dispute was an alleged binding agreement or understanding between PNAL and the majority shareholder as to the circumstances in which PNAL would make a call on unpaid share capital. The claim of non-compliance with s 129 concerned a board decision to proceed with a proposal to extend the runway at Palmerston North Airport. The total cost of the extensions was estimated at $15 million. As at 31 December 2004, PNAL's Statement of Financial Position stated that its current assets were valued at $17,783,967. However, Justice Goddard did not find there had been non-compliance with s 129 because she decided that the runway extension was not a single transaction, but a series of individual transactions and what had been approved was a phased business plan to be implemented in stages, with each stage requiring an individual assessment and approval of funding.[45] As the first stage consisted of a transaction valued at less than 50 per cent of the assets of the PNAL before the acquisition in question occurred, it did not, in the words of Goddard J at paragraph 153, 'fall foul of s129'.[46] In reaching this conclusion, she also relied on qualitative analysis based on the substance of the transaction to support this analysis. In formulating this qualitative test, Goddard J relied on the language of the Law Commission discussed above and concluded that the facts of case were sufficient to take the proposed runway expansion outside the Law Commission's characterisation — namely, that the transactions in this case were outside the nature of a 'major transaction' as described by the Law Commission, that is 'a single large transaction, of which the investors had no warning and which will abruptly transform the nature of the company'.[47] As the plaintiff in this case had acquired its shares in PNAL in full knowledge of the proposed runway extensions, the decision was undoubtedly correct in the circumstances. However, an implication of the focus in this case on a 'single large transaction' as a requirement of a major transaction under s 129 may be to encourage avoidance of s 129 procedure by structuring large projects as series of separately approved, but linked transactions.

In reaching this conclusion, Justice Goddard distinguished the earlier High Court decision of *Hogg v Shephard*.[48] In this case Paterson J had held a series of individual agreements in reality did constitute one major transaction. He concluded that 'the fact that the 95 sections were sold by 95 individual agreements, does not in my view, deprive the sale of major transaction status'[49] because the agreements were all with a single purchaser and on identical terms. Paterson J took the view that 'notwithstanding the form of the sale, it was in substance a major transaction', although this comment needs to be interpreted as simply referring to the method of calculating the value of the transactions involved, rather than an assertion that the courts should decide if the transaction in question fundamentally changed the business of the company. The test applied in this case was essentially quantitative, focusing on the total cost of the sale and the identical character of the sale and purchase agreements without any discussion of whether the transactions fundamentally changed the nature of business.

IV. ALTERNATIVE FORMULATIONS

A. Canadian Business Corporations Act

The Law Commission in its 1989 Report supported the introduction of buy-out rights into New Zealand's corporate law environment as such rights had 'long been a feature of United States corporation statutes … and has been a feature of the Canadian statutes

45 *Central Avion Holdings Ltd v Palmerston North City Council & Anor* [2006] HC CIV 2003-454-559 (Unreported, Goddard J, 15 June 2006), [153].
46 *Central Avion Holdings Ltd v Palmerston North City Council & Anor* [2006] HC CIV 2003-454-559 (Unreported, Goddard J, 15 June 2006), [153].
47 *Central Avion Holdings Ltd v Palmerston North City Council & Anor* [2006] HC CIV 2003-454-559 (Unreported, Goddard J, 15 June 2006), [153].
48 [2003] HC CP 448/02 (Unreported, Paterson J, 4 September 2003).
49 *GHS Hogg and J Haigh & Ors v BH Shephard & Anor* [2003] HC CP 448/02 (Unreported, Paterson J, 4 September 2003), [21].

introduced following the Dickerson Committee Report in 1971.'[50] Appraisal rights were introduced in 1975 into the Canada Business Corporations Act (CBCA) and were based on New York's Business Corporation Law. Under the CBCA, a right of dissent and appraisal,[51] in contrast to s 129 of the New Zealand Act, arises upon 'a sale, lease or exchange of all or substantially all of the property of a corporation other than in the ordinary course of business of the corporation'.[52] Most states also have some version of this right.[53]

B. Non-Inclusion of Acquisitions

Section 129 not only differs from the Canadian provision in terms of its more qualitative focus, but also in terms of the range of transactions potentially requiring shareholder approval. Section 129 applies not only to dispositions, but also to acquisitions of assets and rights, provided the value of the transaction exceeds the 50 per cent value requirement. The inclusion of acquisitions as a qualifying transaction is unique to the New Zealand statutory formulation of fundamental change. The Law Commission did not explain why it chose to include acquisitions within the range of transactions that are covered under s 129 other than a means of ensuring shareholder participation in transformational transactions generally. The inclusion of acquisitions is potentially the most problematic for start-up companies, as it is likely that any large purchase could trigger s 129 without necessarily being a fundamental change to a company, although, perhaps this is mitigated by the fact that for start-up companies, shareholders and directors, interests should be aligned.

C. All or Substantially All

The CBCA provision requires that the transaction must involve 'all or substantially all' of the corporation's property and be other than in the 'ordinary course of business'. As this may not always be clear-cut, at least in comparison to a quantitative test reliant on asset valuations, the overall approach of the courts has been 'to look at the effect of a transaction, not its form when considering these issues.'[54] In terms of the phrase 'all or substantially all', although some of the earlier Canadian cases held that 'substantially all' required there to be a sale that would effectively destroy a corporation's business,[55] later cases have rejected this approach as too narrow and instead have focused on whether the transaction is a radical and fundamental change to the corporation.[56] In *Canadian Broadcasting Corporation Pension Plan v BF Realty Holdings Ltd,*[57] the Court of Appeal for Ontario followed a two-stage inquiry proposed by the Quebec Court of Appeal in *Cogeco Cable v CFCF Inc.*[58] This inquiry requires:[59]

> '(1) in the interpretation of s 189(3) of the Act, it is appropriate to take into account both quantitative and qualitative criteria;
>
> (2) the concept of 'substantially all of the property' has acquired a special meaning in this area of law;
>
> (3) it is difficult to fix a percentage, but in my view, when the sale involves 75% of the value of the property, it ought to be submitted for shareholders' approval;
>
> (4) if the case cannot be decided by using the quantitative test, then we must proceed with a qualitative analysis of the transaction;

50 New Zealand Law Commission, above n3, [203].
51 *Canadian Business Corporations Act*, RSC 1985, c C-44, s 190(1).
52 *Canadian Business Corporations Act,* RSC 1985, c, C-44, s 189(3).
53 Marcus Koehnen, *Oppression and Related Remedies* (2004) 411.
54 Ibid, 414.
55 See *85956 Holdings Ltd v Fayerman Bros Ltd Ltd* (1986]) 25 DLR (4th) 119, 125 (Sask CA).
56 See *Benson v Third Canadian General Investment Trust Ltd* (1993) 14 OR (3d) 493, 507 and *Canadian Broadcasting Corp. Pension Plan v BF Realty Ltd* (2000) 10 BLR (3d) 188, 205.
57 *Canadian Broadcasting Corp. Pension Plan v BF Realty Ltd* (2000) 10 BLR (3d) 188.
58 *Cogeco Cable Inc v CFCF Inc* [1996] AC No 1069; [1996] RJQ 1360.
59 *Canadian Broadcasting Corp. Pension Plan v BF Realty Ltd* (2000) 10 BLR (3d) 188, 205.

> (5) in such a case, it must be determined whether the proposed transaction constitutes a fundamental reorientation which strikes at the heart of the company's activities — in other words, whether this is a transaction which is out of the ordinary and which substantially affects the company's purpose and existence; and
>
> (6) application of the qualitative test must take quantitative criteria into account; the greater the proportion of property sold in relation to all of the company's property, the more likely we would be to conclude that the transaction strikes at the heart of the company and necessitates the shareholders' approval.'

Although the two-stage approach in this case has received some criticism as overly emphasising the importance of the quantitative test,[60] it does highlight that the judicial approach is to compare the nature of the company's business before and after the transaction. Inexorably, the question of whether that business is fundamentally altered after the transaction in question will require consideration of what was the ordinary course of business of the company before the transaction.

D. Ordinary Course of Business

The issue of what is the ordinary course of business is always a question of fact that a court must determine from the record and activities of the corporation. Koehnen stated that 'generally speaking, ordinary course of business refers to day-to-day business activities of the sort that a manager can carry out on his own initiative without prior or subsequent reporting to superiors',[61] which will vary depending on the nature and size of the business. In a leading Canadian case, *85956 Holdings Ltd v Fayerman Bros Ltd,*[62] a decision to sell the inventory of company was held not be in the ordinary course of business because a decision had been made not to replace the inventory. This decision, while only representing approximately 33 per cent of the value of the company, would have the effect that 'it will be a holding company with no ability to accomplish the purpose or objects for which it is incorporated.'[63]

The New Zealand Law Commission did consider whether the major transaction provision in the 1993 Act should include an exemption for transactions that were in the 'ordinary course of business'. However, the Commission decided against this exemption given the 'imprecision of such a test and the possibilities of abuse.'[64] Instead, they took the view that for any transaction large enough to be caught by the provision, then the section should apply to it and the 'shareholders be given an opportunity to determine it, whether or not it can be said to be in the ordinary course of business.'[65] There is some merit in this reasoning, but together with the fact that s 129 applies to acquisitions, it does extend the potential application of the provision far beyond s 189 of the CBCA. Further, it is a surprising conclusion given the stated intention for s129 was to ensure that dissenting shareholders do not inevitably have to accept a 'fundamental change to the nature of the enterprise' which self-evidentially should not include a transaction in the ordinary course of business. This point aside, the concerns that the Law Commission expressed as to the potential for abuse due to the imprecision of an 'ordinary course of business' exception has validity. As O'Neal and Thompson[66] state with regard to this exception, which operates in many of the American states, establishing what is the nature of the business of a corporation is not always straightforward[67]and this can act to the detriment of minority shareholders wishing to challenge a transaction.

60 Koehnen, above n 52, 414.
61 Koehnen, above n 52, 415.
62 *85956 Holdings Ltd v Fayerman Bros Ltd* (1986) 25 DLR (4th) 119; (1986) 32 BLR 204 (Sask CA).
63 *85956 Holdings Ltd v Fayerman Bros Ltd* (1986) 25 DLR (4th) 119, 129; 32 BLR 204, 214 (Sask CA).
64 New Zealand Law Commission Report, above n 3, [502].
65 Ibid.
66 O'Neal and Thompson's *Oppression of Minority Shareholders and LLC Members,* (first published 1975, 2nd revised ed, 2004).
67 O'Neal and Thompson, ibid, Vol 1, 5.19.

It is perhaps ironic that one of the first cases to consider s 129 took into account 'ordinary course of business' considerations to narrow the application of the section. In *Flight Trainers Ltd v McGormick*[68] one of the allegations was that the affairs of the company in question had been conducted by the two directors in a manner that was unfairly prejudicial to one shareholder in that they had entered into a debenture in contravention of s 129(2)(b). It was accepted by all parties that the debenture had not been the subject of a special resolution or contingent upon one, 'so if it was by definition a major transaction, it would have been entered into [in] contravention of s 129'.[69] Salmon J however held that that the debenture was not a disposition within the meaning of s 129(2)(b). Part of his reasoning was a view that Parliament could not have intended that a special resolution would be required every time a company granted a debenture, given the prevalence of their use. Although subsequent cases have not developed this ordinary course of business exception, it should be noted that subsequently s 129 was amended in accordance with this decision.[70]

E. Exclusive Remedy

In the United States, there is some debate as to whether or not the right of dissent and appraisal is an exclusive remedy available to minority shareholders. For example, Mitchell stated in 1996 that 'the law on exclusivity varies between jurisdictions and has been changed both by statute and case law.'[71] In the New Zealand context, she commented that the New Zealand *Companies Act* 'does not address this issue,' but she suggests that it 'would be highly likely that the New Zealand courts would allow for other possible remedies in cases whether the actions of the corporation or its directors and management were particularly reprehensible'. Further, in cases of fraud or illegality, 'it would appear remedies other than appraisal would also be available, in particular the oppression remedy'.[72] This question is now apparently settled, for example, with the courts willing to hear claims based on both failure to comply with s 129, as well as prejudice or oppression claims under s 174[73] or as the basis for placing a company in liquidation under s 241.[74] There is a clear relationship between the right of shareholders to bring an action under s 174 and non-compliance with s 129, as failure to comply with s 129 is expressly deemed by s 175(1)(l) to be unfairly prejudicial for the purposes of section 174.

The High Court decision in *Dunning v Chabro Holdings Ltd*[75] provides a useful example of the relationship between these two sections. In this case, it was alleged that Chabro had guaranteed a subsidiary's obligation and provided funds to that subsidiary to enable it to acquire a commercial property. The transactions in question were approved by the shareholders in Chabro by a resolution in lieu of a meeting to which the plaintiff in this case, who held 10% of the shares in Chabro, did not consent and in fact had not received notice of as required by the Act. The judge was not willing to find that the provision of the guarantee and the loan finance did not breach s 129, as detailed evidence of the financial position of Chabro at the time of the resolutions was not presented to the court. The judge 'was not prepared to speculate to the extent required' given the consequences of non-compliance. However, the fact that a 10% shareholder had been excluded from any involvement in the decision-making about 'what was an important transaction to Chabro'

68 (1999) 8 NZCLC 261, 998.
69 *Flight Trainers Ltd v McGormick* (1999) 8 NZCLC 261, 998, 262, 007.
70 The addition of new subsection s 129(2A) by s 10 of the *Companies Act 1993 Amendment Act 2001* (NZ) to extend its application to dispositions under section s 129(2)(b) has been taken as approval of the approach taken in this case.
71 Mitchell, above n 22, 293.
72 Ibid 299.
73 See *GHS Hogg and J Haigh & Ors v BH Shephard & Anor* [2003] HC CP 448/02 (Unreported, Paterson J, 4 September 2003), and *Dunning v Chabro Holdings Ltd* [2006] (Unreported, HC, Auckland, CIV 2005-404-4903, Allan J, 4 September 2006).
74 See *Flett v JH Flett Ltd* (1999) 8 NZCLC 261, 893
75 *Dunning v Chabro Holdings Ltd* [2006] (Unreported, HC, Auckland, CIV 2005-404-4903, Allan J, 4 September 2006).

reinforced his Honour's view that the company was being operated in a way that was oppressive and unfairly prejudicial to the plaintiff shareholder.

V. CONCLUSION

One question that is difficult to assess is the degree of non-compliance with the requirement of shareholder approval for major transactions, given that 'a transaction that satisfies the definition of a major transaction may not necessarily involve a fundamental change to the nature of a company.'[76] As Lynne Taylor observed 'an investment company that sells a major asset but replaces it with an almost identical asset — both the sale and purchase fall within the definition of a major transaction but the nature of the company remains unchanged.'[77] This question is unanswerable, but given the broad application of the section, especially for start up companies, it is very surprising that there have only been two cases to date where the courts have been required to interpret the buy-out rights provisions contained in ss 110-115 of the Act.[78] The inadequacies of this remedy have received some articulation, with one judge even describing them as defective.[79] This judicial criticism and the subsequent recommendations of the Law Commission[80] to amend the remedy have been incorporated in the *Companies (Minority Buy-Out Rights) Amendment Act 2008* that came into force on 16 September 2008.[81] One amendment contained in the Act is a new requirement that companies, when giving shareholders notice of any special resolution under Schedule 1 of the Act, will not only be required to provided the text of that special resolution but also, in the case of the resolution triggering buy-out rights, the existence of such rights.[82] It may be difficult to assess the success of the amendments contained in the *Amendment Act* as private arbitration has been retained as the method of resolving valuation disputes. However, one implication is that as companies are now required to advise shareholders when buy-out rights arise, there will be greater incentives for companies to structure transactions so as to avoid compliance with s129 in the future.

Overall, the few cases to date to consider the scope of s 129 have generally taken a literal approach to its construction, with judges focusing on the bright line formulation of fundamental change used in s 129(2) to concentrate on the value of a transaction, rather than whether the transaction, or transaction as a whole, will fundamentally change the business of the company. If a Canadian 'fundamental change' approach had been adopted when the *Companies Act 1993* was drafted, it may not have actually resulted in different outcomes for the *Hogg v Shephard, Central Avion Holdings Ltd v Palmerston North City Council* and *Flight Trainers Ltd v McGormick* cases. In terms of the *Fletcher Challenge Forests* case, the position is less clear and this would depend on the exact nature of the company's business. However, while most of these cases were probably correctly decided as to whether they involved fundamental change to the business of the respective companies, the rationales put forwarded in the respective judgments are inconsistent and cumulatively have undermined the statutory objective for the provision. However, the certainty provided by the bright-line transaction based test does have the advantage of setting a minimum backstop for transactions that are deemed to fundamentally change the business of a company. Accordingly a mixed approach is recommended which requires compliance with the section for transactions that change the essential nature of a company or exceed in value a specified minimum comparative value in relation to the value of the existing assets of the company. This value could be greater than 50 per cent of the value of

76 Lynne Taylor 'Minority Buy-Out Rights in the Companies Act 1993' (1997) 6 *Canterbury Law Review* 539, 549.
77 Ibid.
78 *Natural Gas Corporation Holdings Ltd v Infratil 1998 Ltd* and *Trans Tasman Properties Ltd v Gibson* (2007) 10 NZCLC 264, 298.
79 *Natural Gas Corporation Holdings Ltd v Infratil 1998 Ltd* [2001] 3 NZLR 727, 728.
80 New Zealand Law Commission, *Minority Buy-Outs,* Report No 74 (2001).
81 *Companies (Minority Buy-Out Rights) Amendment Act 2008, No 69* (NZ).
82 *Companies (Minority Buy-Out Rights) Amendment Act 2008* (NZ), s 10.

assets, as companies would still need to consider the essential nature of the business for transactions with a smaller comparative value. It is, however, not recommended that an 'ordinary course of business' exception be adopted.