SOME ASPECTS OF MODERN COMPANY STRUCTURE.*

Perhaps the most disturbing feature of the spectacular company failures which have occurred in Australia during the last half decade is that in most cases the public continued to invest money in the companies until a relatively short time before the collapse occurred. It is obvious that not all of these people acted without advice or against the advice of their stockbrokers, solicitors, bankers and accountants. Indeed it is notorious that some brokers continued to advise investment in some of these companies until a matter of a few weeks prior to their collapse. It therefore follows that many of these advisers were unable, by a perusal of the published accounts and prospectuses, to see any indication of the failure which was to occur.

The system, then, failed or at least proved ineffective. There have been many subsequent amendments to the Companies Act and perhaps one may feel justified in hoping that these will go a long way towards preventing, or giving more adequate warning of, future failures from the same causes but it is quite another thing to feel confident that they will necessarily prove effective to prevent or give adequate warning of future large scale failures which, if and when they occur, will be no doubt due to a new set of causes.

Amendments to the Act seem to flow in a fairly continuous stream and increasing burdens are placed upon company administrators. In view of the fact that the very great majority of public companies appear to function satisfactorily it is evident that the good suffer with the bad.

My perusal of the various reports written by inspectors appointed to investigate the affairs of companies and my own experience in investigating the affairs of the Reid Murray Group in Victoria have led me to wonder whether some of our thinking in relation to the company structure has not become outmoded and is no longer appropriate to the modern large public company.

The historical background of English company law is admirably set out by Professor Gower in his book *Modern Company Law* and I will not attempt to summarise it here. Basically, however, it is easy to understand the need for the creation of a device which would permit numerous persons to subscribe a limited amount of money for the purpose of conducting what amounted to a joint enterprise. It is also easy to understand that all the subscribers could not take

* A paper read at the 1966 Law Summer School held at the University of Western Australia.

part in the management of the enterprise and therefore reposed the responsibility of management in a small number of persons elected by them who in turn employed a staff. Out of these needs arose a fictional legal personality called the company. Unlike many other legal concepts which remain but dimly understand by laymen, the concept of corporate personality seems to have been readily accepted by laymen. It has also attracted a great deal of attention by scholars of jurisprudence who have expressed widely differing theories as to the true nature of corporate personality. Wolff[1] claims that there are no less than sixteen such theories. The separateness of the corporation from its corporators has flourished under the influence of judicial decision. Thus we might have expected to find that directors, as the elected managers of the shareholders, would be held to owe their duties to the shareholders, but we find that they owe their duties, not to the individual shareholders as such, but to the company.[2] Similarly, we find the general meeting being described by lawyers as one of the organs of the company[3] whereas, at least if it were well attended, we might have been forgiven for thinking that it really is the company itself in its nearest approach to a tangible form.[4] We find that the directors are not bound to obey the directions of the general meeting on matters within their powers and that, if they do not, the remedy of the shareholders is to remove the directors. We find that it is not correct to say that the shareholders are the owners of the assets of the company.[5] They are the owners of certain rights which lawyers find difficult to describe concisely. We find the shareholders, far from being persons who have subscribed their money to a joint enterprise with others and who jointly undertake the risks of that enterprise, are largely people who have purchased their shares on the stock exchange at a price which bears little relation to the money which was originally subscribed to the company and who in most cases have no knowledge of the company's affairs and sometimes indeed but a dim idea of the company's business. Except in rare cases there is difficulty in persuading them to attend meetings. The election of directors and the appointment of auditors is more often than not a mere formality, and indeed a formality well under the directors' control. The shareholders

1 *On the Nature of Legal Persons,* (1938) 54 L. Q. REV. 494, at 496.

2 Percival v. Wright, [1902] 2 Ch. 421; Bell v. Lever Brothers, Ltd., [1932] A.C. 161.

3 GOWER, MODERN COMPANY LAW (2nd ed.) 16.

4 Salmon v. Quin, [1909] 1 Ch. 311; Shaw & Sons Ltd. v. Shaw, [1935] 2 K.B. 113. Compare Isle of Wight Railway v. Tahourdin, (1883) 25 Ch. D. 320.

5 Short v. Treasury Commissioners, [1948] 1 K.B. 116, at 122; Foster & Sons v. Commissioners for Internal Revenue, [1894] 1 Q.B. 516.

seem to have faded more and more into the background and with the size and complexity of modern companies it is small wonder that this should be so.

Whatever be the correct jurisprudential or philosophical explanation, the large public company has become a personality in itself, quite apart from its directors and shareholders, and a personality of enormous importance in our economic structure. It is almost impossible to think of our great banks, insurance companies, steel companies, newspaper companies and manufacturing companies in terms of their shareholders, a faceless and ever changing body of people. It is perhaps easier to think of them in terms of their directors, but even these gentlemen are a changing body who frequently possess very small shareholdings in the companies they control. The company itself is permanent and real and indeed in some cases a national institution.

In these circumstances we may think it strange that we still maintain the principles that the directors, while they owe their fiduciary duties to the company itself, are nevertheless bound to exercise those duties for the benefit of the members and the members only. By and large the law will still not permit them to have regard to the staff of the company, the community or the nation.

There have been instances when directors have sought to recognise the reality of their obligations to interests other than those of the shareholders. The facts of some of these cases are worthy of note. In the famous *Ford Company Case*[6] the facts were that the company was formed in 1903 with an issued capital of $100,000 of which $49,000 was subscribed in cash. In 1908 the issued capital was increased to $2,000,000 by a declaration of a stock dividend out of accumulated profits. Thereafter the directors regularly declared cash dividends at the rate of 60% on the issued capital of $2,000,000 and between 1911 and 1915 additional special dividends amounting in all to $41,000,000 were declared. In 1916 a special cash dividend of $2,000,000 was declared but the directors intended thereafter to content themselves with an annual dividend of 60%. The directors proposed to enlarge the production capacity of the company and erect blast furnaces and similar plant to enable the company to become more self-sufficient. The plan of Mr. Henry Ford was stated by him in the following terms:

> "My ambition is to employ still more men, to spread the benefits of this industrial system to the greatest possible number, to help build up their lives and their homes. To do

6 Dodge v. Ford Motor Co., (1919) 3 A.L.R. 413, 204 Mich. 459.

> this we are putting the greatest share of our profits back into the business."

His object was to reduce the price of his product to $360 which would have also reduced the company's profit margin considerably. The plan involved paying, for the year 1916, a dividend of a mere $1,200,000 on the capital of $2,000,000 and putting the balance of the profit made in that year, some $58,000,000 back into the business.

One of the stockholders, who was fortunate enough to own about one-tenth of the stock of the company, sought to restrain the company from employing its profits in accordance with this plan.

It was argued by counsel for the company that, although the company could not engage in humanitarian works as its principal business, the fact that it was organised for profit did not prevent the existence of an implied power to carry on with humanitarian motives such charitable works as were incidental to the main business of the company.

This argument failed and the Court ordered a distribution of a further $19,000,000 which, on the issued capital of $2,000,000, must be considered a satisfactory dividend for any shareholder.

Another case of some interest is *Parke v. Daily News Ltd.*[7] in which a company owned two newspapers which had been operating at a substantial loss. The directors entered into a contract to sell the newspapers to a newspaper group controlled by Lord Rothermere for £2,000,000. The directors proposed to devote the purchase monies to the staff and pensioners of the company by way of compensation for the loss of pension rights and benefits and payment in lieu of notice. The company had previously entered into a long-term contract with a Canadian company for the purchase of newsprint and, when the directors explained their intended disposal of the £2,000,000 to the Canadian company, the latter agreed to forgo any rights it had under its long-term contract, provided that the £2,000,000 was distributed promptly to the former employees and pensioners of the defendant company. Payment of nearly half the purchase money was clearly justified by way of settling accrued rights to which employees and pensioners were entitled. The balance represented a payment of compensation for loss of pension rights of approximately one week's salary for each year of service. A shareholder of the company brought an action to restrain the directors from making this last mentioned payment and the action succeeded upon the grounds that, on the evidence before the court, the payment would be in the nature of an *ex gratia*

[7] [1961] 1 W.L.R. 493.

payment and, in the absence of evidence to show that it was reasonably incidental to the carrying on of the company's business, and would be for the benefit of the company and would promote the prosperity of the company, it was ultra vires.

This decision is probably quite correct, but it is hardly satisfactory. Presumably the Canadian company would feel perfectly justified in demanding compensation for the premature termination of its contract and the ultimate benefit the shareholders would receive would therefore have been problematical.

Incidentally, it is interesting to reflect that if the directors of the English company were acting beyond their powers in attempting to compensate their employees, it seems that the directors of the Canadian company were even further beyond power in agreeing to waive their company's contractual rights to enable the English directors to carry out the plan.

In his book *The Future of Private Enterprise*[8] Goyder develops some very interesting theories upon the obligation of public companies.

Goyder's theory is that basically an industrial enterprise owes its existence and well-being to four parties, its shareholders, its workers, its consumers and the community. He considers therefore that enterprises which achieve a certain status in the order of things in the community should owe their responsibilities to those four parties and not just to one of them. He reasons that when a company has liquid assets which exceed its total paid up capital it becomes "literally nonsense to speak of the risk-taking function of capital." It may be fair, Goyder says, to reward capital for past risks but that reward should not continue in perpetuity any more than a member of the staff is paid in perpetuity after his retirement.

Goyder believes that, under the present system of company law, conflict between capital and labour is inevitable because it is fundamentally against human dignity for the staff of a company to be working under a system which recognizes only one of the four proper objects of its responsibilities, namely, the shareholders. He points to the fact that directors of a company which has made large profits are chary of declaring dividends which, in terms of percentage, are very high. Goyder believes that for this reason mere profit sharing and employee-bonus schemes have never proved very successful in promoting harmony between capital and labour. What is required in his view is a system whereby the recognised objects of the enterprise extend beyond the supplies of capital.

[8] THE FUTURE OF PRIVATE ENTERPRISE (London, 1951).

Goyder's theory is that once a company has operated for a period of say fifty years and has achieved the necessary financial status it should be run thereafter upon the basis of a trust for the benefit of all four parties and no longer simply for the benefit of the share-holders.

Goyder is not alone in believing that the law's recognition of only one of the parties is wrong. John Ruskin[9] wrote of the recognition conferred upon corporate personality by the English Act of 1862:

> "The idea that directions can be given for the gaining of wealth irrespective of consideration of its moral sources is perhaps the most insolently futile of all that ever beguiled men through their vices."

Years later Lord Eustace Percy wrote:

> "The human association which in fact produces and distributes wealth consisting of workmen, managers, technicians and directors is not recognised by the law—while the association which the law does recognise is by itself incapable of production or distribution."

In an address delivered in 1958 Lord Denning said:

> "Do directors realise the responsibilities that rest on them? The answer I think is yes, but the law does not do so. . . . They must not have regard to the interests of the workers or the customers except insofar as these are relevant to the primary object of making profit. This view is completely out of date . . . I foresee that one of the great tasks before us in the coming years is to modify the company system. Directors would no longer be regarded by the law as managing on behalf of the shareholders only but regarded as representatives of all vital interests."

Whatever shade of political opinion one may hold, it seems that directors of large public companies which have achieved an institutional status have some nice problems to decide. For instance, under the law as it now is, have the directors of a great newspaper the right to determine its policies by reference to anything but the long term interests of the shareholders? I once expressed the view to a director of a newspaper with a large circulation that I thought that its standards had been falling and that it was turning itself into a sensationalist type of publication. He agreed that this was so, but said that sensationalism was what sold newspapers, and that the directors were there to make profits for the shareholders. As a matter of law he was probably right, but is this really a satisfactory situation?

9 UNTO THIS LAST (London, 1862).

Another difficult situation can arise when the directors of a company have to decide whether to rebuff or encourage a tentative approach by another company with a view to a take-over. Suppose the directors bona fide and possibly quite correctly believe that it would be contrary to the national interest to allow the company to be taken over and ultimately absorbed by a large foreign company, are they entitled to take this belief into account? The proposed offer may be in cash and may represent a substantial margin over the market price of the shares. It may not be possible to predicate that the shares would otherwise be likely to attain such a price in the foreseeable future. Are the directors obliged to restrict their consideration of the offer simply to the financial benefit which the shareholders would receive, or are they entitled to have regard to these other factors? In the *Savoy Hotel Case* the inspector appointed by the Board of Trade to investigate the affairs of the company criticised the directors for endeavouring to place a hotel owned by the company beyond the reach of a take-over by competitors who would probably have proceeded to close it. The directors acted bona fide in what they considered to be the best interests of the community but, in the opinion of the Inspector, they were misguided in acting by reference to such considerations.

We have built up a corporate personality which, even though a creature of statute, has become a living reality and perhaps the law now lags behind the development of what it created.

In some cases the concept of corporate personality becomes a shield and yet in others, where the same concept might well be used to justify actions which benefit both the company and the community, the shield becomes ineffective and the bare financial interests of the shareholders are held to prevail.

In practice I have no doubt that the directors of many large public companies are either ignorant of the law in this regard or choose to ignore it. Many companies are probably more generous to their staffs than they are strictly entitled to be and it is obviously a good thing that this is so. Many companies are also motivated by communal and national interests in some of their policies. Having recognised the corporate personality to the degree that we have for some purposes, it seems that logic would demand that the law should recognise it for other purposes, many of which are more laudible.

The Act has already moved in this direction by virtue of section 19 which enacts that the powers of a company shall include power to make donations for patriotic and charitable purposes and by the power included in the Third Schedule relating to benefits to employees. In his Draft Report on the Company Law of Ghana Professor Gower recommended that the Act provide that in considering whether a particular transaction or course of action is in the best interests of a company as a whole, a director should have regard to the interests of the employees, as well as the members, of the company, (section 198(3)). It may be therefore that the future trend will be to recognise the right of the directors of a company to act for the benefit of its employees and the community in general.

I now turn to the ever-fruitful topic of the responsibilities of directors. The trend of amendments to the Act has been to endeavour increasingly to fix the directors with responsibility for their management. Notwithstanding this, Romer J.'s classic definition and analysis of the nature and extent of the duty imposed upon directors still seems to be the law—namely that a director must act honestly and must exercise such degree of skill and diligence as would amount to the reasonable care which an ordinary man might be expected to take, in the circumstances, on his own behalf. But he need not exhibit a greater degree of skill than may reasonably be expected from a person of his knowledge and experience.[10]

Section 124(1) of the Victorian Act provides that a director shall at all times act honestly and use reasonable diligence in the discharge of the duties of his office. This sub-section may have created a new statutory offence, but it seems to have fallen short of enacting the existing common law obligation, if that indeed was the intention of the legislature. In *Byrne v. Baker*[11] the Victorian Full Court held that an information for failing to use reasonable diligence and relying upon a number of acts and omissions was bad for duplicity. The Court considered that each particular act or omission should be the subject of a specific charge. In the course of its judgment the Court referred to the use of the word "diligence" and regarded the omission of the word "skill" as significant. Consequently it would appear that, provided a director acts honestly and with diligence, the question of skill, for the purposes of the sub-section, is irrelevant. This may however be more a matter of words than of substance, because if it was shown that a director was a professional man and acted in a transaction which was within the scope of his professional knowledge, it would follow almost inevitably that he could not be said to have acted with diligence if he failed to exercise a reasonable amount of skill.

10 Re City Equitable Fire Insurance Co., [1925] Ch. 407.
11 [1964] V.R. 443.

When the companies fail and the directors are examined by inspectors, their limited knowledge of the operation and accounts of their company is revealed and indeed, relied upon. They plead ignorance of the bad debts which had been accumulating and which were disguised in the accounts as current assets. They plead ignorance of insufficient provisions for unearned income on long term contracts and ignorance of profits brought to account before they have been received; and in my opinion in most cases they are quite justified in doing so. How can the average director, if he is not also a full time employee of the company, be expected to know of such things? Are we right in seeking to attach more and more responsibility to directors qua directors? Surely in the vast majority of cases the directors of a company must perforce base their decision on the facts presented to them by the executive management. It follows that the decision is only as good as the presentation of the facts. This suggests that the real management of a company is often vested in the executive officers, the manager, the chief accountant and other senior executives. Somewhere in each company is a man or a number of men who produced the figures which later proved to be so misleading. Somewhere in each company is a man who decided not to acquaint the directors with certain facts or who wrote a misleading memorandum for consideration by the Board. These men may or may not be themselves directors. If they are not, then the Act is almost completely silent as to their responsibilities. Should this be so? Or has the time come when we should re-assess our concept of legal responsibility and contemplate imposing duties and responsibilities upon the executives of companies rather than upon directors as such. Should there perhaps be two classes of directors referred to in the Act—full time directors and outside directors, who might perhaps be called Advisory Directors and carry less onerous responsibilities?

The attempted imposition of responsibility upon directors becomes even more difficult in the case of group companies. It is common enough to find that the directors of a holding company appoint either one of their number or a senior member of the staff of the holding company to the board of the subsidiaries. In practice it seems commonly to be accepted that the directors of the subsidiaries so appointed are merely there to do the bidding of the holding company. This attitude is apparently justified upon the basis that the holding company, as the only beneficial shareholder of the subsidiary is the owner of it, and is therefore entitled to determine the conduct of its affairs. This of course is not how the directors of the holding company regard their own position qua the shareholders of the holding company. The subsidiary is treated as a branch or a division of the parent company and the board of the subsidiary meets formally only to comply with the provisions of the Act. A director or a senior executive of the holding company may find himself a director of twenty or thirty subsidiary companies in this way and it is quite obvious that he can have only the barest acquaintance with the business of the subsidiaries. In practice, the conduct of the day to day affairs is left to the individual managers of the subsidiaries, subject to the direction of the directors of the holding company. In my opinion this situation is highly undesirable. In the event of failure the directors of the subsidiaries can plead almost total ignorance of its affairs. The manager of a subsidiary can plead that he acted in accordance with directions given to him by the holding company. Similarly, the directors of the holding company themselves can seek to pass the blame to the directors of the subsidiary, and in fact, the directions which are given to subsidiaries from the holding company usually come, not from its Board, but from its executives, who may or may not be directors of the holding company. In this way the chief accountant of the holding company can impose methods of accounting upon the accountant of the subsidiary which the latter may not be happy to accept, but, as the chief accountant has the authority of the holding company, he feels bound to comply with the direction. It seems too much to expect that, when an executive of the holding company is appointed to the board of a subsidiary, he should suddenly take on a new role of independence of his employers and, whatever his position is as a matter of law, no one could regard a prosecution of such a director with enthusiasm when, in effect, he was merely doing what he was told by those who employed him.

If a subsidiary is to be treated in practice merely as a branch or division of the holding company, then should not the law be changed to make those in fact responsible for the actions of the subsidiary also responsible in law? And should not consideration also be given to obliging parent companies to guarantee their subsidiaries?

There are numerous other situations which commonly exist in groups of companies to which lawyers might well give some thought. It is not uncommon, for instance, to find that a highly reputable public company has a large, or even a controlling, interest in another company which borrows money from the public by way of debentures or notes. The association of the former company with the latter gives the investing public confidence in the security and stability of the latter. But in the event of a calamity overtaking the latter is it safe to assume, as we are apt to do, that the reputable company will find the necessary money to save the situation and pay out the debenture and noteholders? If the amount involved is large enough, might not a situation arise in which the directors of the large company might say "Much as we would like to do so, we cannot authorise the payment of so much of the company's funds when the company has no legal obligation to make such a payment?" Going a step further, might not a shareholder of the company successfully restrain the directors from doing so? It could be argued on behalf of the directors that such a payment was necessary to maintain the company's reputation, but would the argument prevail if the amount involved were large enough, and the company, apart from allowing its name to be used as being a large shareholder, had not permitted any representation that it guaranteed or was in any way responsible for the other company? Might not a court hold that payment in such circumstances would be *ex gratia* and unjustified?

The anomalies which can arise between groups of companies are indeed legion. A subsidiary frequently has practically no capital of its own and yet, by virtue of unsecured advances from its parent company, it can carry on an extensive business and incur heavy liabilities. The reality of corporate personality can then be brought home to its creditors with a shock. It may even have a substantial issued capital of its own, which, upon the allotment of shares to its parent, disappears by way of unsecured loan to another subsidiary company in the group.

These difficulties are by no means assisted by the present requirement in the Act for companies either to present the accounts of individual subsidiaries or to present a consolidated profit and loss account and a consolidated balance-sheet. Companies almost invariably choose the latter alternative and consolidated accounts often actually prevent a true and fair picture of the affairs of a group from being presented. In many cases consolidation conceals the fact that certain subsidiaries, supposed by investors to constitute the real strength of the company, have been operating unprofitably and are in a perilous position.

The problem of adequate presentation of the accounts of a group has been discussed by many committees, including the Cohen Committee.[12] More recently the three inspectors appointed to investigate the affairs of the Latec Group have made some cogent remarks on the topic. It is obvious that something must be done to find a solution which will not involve too much additional work for the company administrators but which, at the same time, will ensure

[12] CMD. No. 6659, at paras. 115-122 (1945).

that something nearer to a true picture of the affairs of group companies emerges than at present is the case.

The position of the auditors in group companies is another matter which obviously requires attention by both the accounting profession itself and by the legislature. Situations can arise in which auditors have information which would be of considerable use to the auditors of other companies in a group. They may hesitate to communicate this information, not because they wish to help in the concealment of facts, but because they believe that such communication would be unauthorised and outside the scope of their duties. They would probably welcome the imposition of a duty to disclose matters of this kind. Section 167A of the Act has taken a step in this direction by imposing on auditors a duty to disclose to the trustee for the debenture holders relevant matters of which they become aware. The position of the auditors of subsidiaries in relation to the auditors of the parent company and of other subsidiaries still remains to be clarified. Consideration should perhaps be given to requiring the auditors of subsidiaries to report separately and directly to the auditors of the parent company. As the situation now stands an auditor of a subsidiary is faced with the alternative of qualifying his report (in which case the parent company is bound to publish the substance of the qualification by virtue of class 6 of the Ninth Schedule), or drawing the attention of the parent company to the matters which give him cause for concern. By adopting the former course he is taking what, in my view unfortunately, is in Australia still regarded as a drastic step. By adopting the latter course, although the matter is brought to the attention of the shareholders—the parent company—it may never reach the auditor of the parent company, and certainly not the shareholders of the parent company.

It may be that auditors generally would welcome the imposition of a duty to disclose matters which, even though not sufficiently grave to warrant a qualification of their report, nevertheless give them cause for feelings of disquiet. Such a disclosure could be made without publicity to an official such as the Registrar who would be empowered to make further inquiries, again without publicity. The existence of such a duty might strengthen the position of auditors in their relationship with the company and the existence of the power in the Registrar might force directors to face up to situations which showed signs of developing, at an earlier stage than at present.

Whereas, in the vast majority of cases, directors and auditors work in complete harmony and directors welcome the closest attention of the auditors, in those few cases when relations become strained the position of the auditor can be very unsatisfactory. For example the auditor may consider it necessary to embark on a long and costly examination of the debtors' ledgers and the directors may consider this to be entirely unnecessary. This examination may result in a substantial increase in the auditors' fees which, particularly if the directors' view proves to be correct, the directors may resent paying or even refuse to pay. The possibility of this situation arising may colour an auditor's judgment as to whether the examination is or is not in fact necessary.

Qualifications of reports are still regarded most seriously and usually attract the attention of the financial press. This very fact in itself probably leads to auditors being more reluctant to qualify a report than they otherwise might. A qualification is, in many cases, simply an expression of a different opinion, but it seems too often to be regarded as carrying overtones reflecting upon the integrity of the directors. An auditor may even be fearful of the possibility of an action for defamation and the inclusion of a specific qualified privilege in the Act might well be a desirable step.

Basically however, in my opinion, the fundamental difficulties which beset the auditor arise from the fact that he is employed by and must necessarily have close contact with, the very people who compile the accounts upon which he eventually has to report. Until we can find a solution to this aspect of the matter it seems inevitable that auditors will from time to time face difficult problems arising from this relationship.

The last topic upon which I propose to touch relates to investigations under Division 4 of Part VI of the Act. These investigations have proved a fruitful source of litigation in Victoria, although it seems that in other states companies and the directors have been more inclined to resign themselves to their fate.

In 1962 in *The Queen v. Coppel Ex parte Viney Industries Pty. Ltd.*[13] the Full Court held that an investigation under the 1958 Victorian Act was not such that the inspector was obliged to act judicially. It therefore rejected the claim, put forward on behalf of the company, to appear by its counsel and to take part in the proceedings.

The High Court by a narrow majority took the same view in *Testro Bros. Ltd. v. Tait*[14] and this decision was in relation to the slightly altered provisions of the 1961 Act.

A further attempt was made in the course of the investigation

13 [1962] V.R. 630.
14 [1963] A.L.R. 769.

into the Stanhill group of companies to establish the right of an individual director to be informed by the inspector of any allegations which had been made against him, to be given a copy of the transcript of the whole investigation and to have the right to recall and cross-examine previous witnesses. These were said to form part of the content of the rules of natural justice under which the inspector was bound to operate. The High Court refused to depart from its decision in *Testro Bros. Ltd. v. Tait* and the Privy Council refused leave to appeal.

It is therefore now well settled that an inspector is not bound to conduct his investigation as a judicial proceeding. Whether the rules of natural justice themselves in the case of a company investigation would require an inspector to comply with all that was claimed in those cases is, in my opinion, another matter. From my own experience I know it would be almost an impossibility to inform every witness of every allegation or insinuation which had ben made against him nor would it be feasible for the inspector to inform every witness of every unpleasant conclusion he might by possibility reach at the end of his investigation. Most inspectors commence an investigation knowing little or nothing of the company being investigated and laboriously build up their knowledge of its affairs and of the people associated with it.

This is not to say that there are not some unsatisfactory features attaching to company investigations. An inspector may make most damaging comments about individuals and the individuals concerned have no real opportunity of reply. The press may not accord them sufficient space or prominence and, moreover, quite often an adequate reply will necessarily involve the agrieved party making damaging statements about his erstwhile associates.

The powers conferred upon an inspector are perhaps wider than is generally appreciated. The inspector may question any officer or agent of the company, and such officer or agent is liable to punishment if he refuses to answer the inspector's questions. The width of the power is only fully appreciated when it is realised that by section 168(2) an officer or agent includes a person who is capable of giving information concerning the promotion, formation, trading, dealings, affairs or property of the corporation and, where there are reasonable grounds for suspecting or believing that a person is a person of the kind referred to, that person. In plain language, if an inspector has reasonable grounds for believing that a person may be able to give him some information concerning the affairs of the corporation, no matter whether that person was in fact connected with the company or not, he is for the purposes of the investigation an officer or agent of the company. The only limitations of the power appear in section 171(5) and (6) which maintain in a very attenuated form the right to object to answering a question in cases where the answer may tend to incriminate and also in section 367 which preserves legal professional privilege.

The inspector's functions thus drastically depart from the traditional judicial concept of accusatorial proceedings and are indeed inquisitorial in character. If a witness objects to answer a question on the ground that the answer might tend to incriminate him, his answer cannot be used against him in evidence in subsequent proceedings, but he is still in an infinitely worse position than he would have been if he had had the right simply to remain silent.

A sub-committee appointed by the Executive of the Australian Law Council has recently considered the problem which arises from the publicity attaching to the reports of inspectors. The committee proceeded upon the basis that the possible uses to which the report of an inspector might be put were—

(1) to place before the Crown Law authorities the facts elicited by an inspector thereby both assisting in the preparation and conduct of criminal or civil proceedings, and also enabling decisions to be made whether to institute such proceedings where this might otherwise be a matter of doubt.

(2) to provide, by its contents, a ground for the winding up of a company under section 222(1)(g).

(3) to state the evidence given before the inspector so that, as so stated, it may be used in criminal or civil proceedings.

(4) to express to Parliament and through it to the public at large the inspector's views as to the reasons for a company's financial situation and the conduct of the persons who have had the control of the company's affairs.

Upon this premise of the four uses to which an inspector's report might be put, the sub-committee expressed its opinion that the last three uses were most undesirable unless the inquiry was conducted in accordance with the minimum requirements of natural justice. (The sub-committee accepted the view that the application of the principles of natural justice to company investigations would deprive them of their usefulness.) The sub-committee therefore concluded that the reports of inspectors should only be used for the first purpose, namely to place before the Crown Law authorities the facts elicited by the inspector to assist those authorities in the preparation and conduct of criminal and civil proceedings and in the decision whether or not such proceedings should be instituted. Having reached this conclusion the sub-committee thought that there was no justification whatever in allowing the reports of inspectors to be presented to Parliament or to become available to members of the public. Upon the same basis the sub-committee recommended the repeal of section 222(1)(g) which provides that the inspector's report may be used as a ground for winding up. The sub-committee said that it appreciated that company failures, particularly where they involved large enterprises and jeopardised the investments of many members of the public, were regarded both by the public at large and by legislators as involving matters of general public interest. However neither the satisfaction of public curiosity and popular indignation, nor the identification of individuals as specific objects against whom parliamentary and popular censure could be directed, could be regarded as ends justifying the publication of reports, unless those reports resulted from inquiries conducted in a manner consistent with natural justice.

With great respect to the sub-committee, I find it difficult to agree with its report in its entirety. In the first place, as I have indicated, the view proceeds upon the basis that the only use to which the report should be put is to inform the Crown Law authorities and thereby assist them in the preparation of criminal or civil proceedings and to assist them in deciding whether any such proceedings should in fact be instituted.

I find this view difficult to accept. So far as criminal proceedings are concerned the concept involves accepting the proposition that the primary function of the inspector is to use his inquisitorial powers with the object of obtaining evidence from and against persons who may later be accused of criminal offences. These persons would ordinarily be entitled to remain silent. If the inspector's powers are to be used to such an end, and confined to such a use, I would have supposed that a more justifiable attack could have been launched by the sub-committee upon the basis that the removal of the privilege of refusing to answer questions upon the ground of possible incrimination is itself contrary to the long established principles of the administration of our criminal law. The task of an inspector would indeed be distasteful to the average lawyer if he felt that he was merely conducting a type of glorified police investigation, with his possible victims in a position far more disadvantageous than their position would be if questioned by an investigating detective.

Insofar as the report refers to civil proceedings, I assume that the proceedings which the sub-committee has in mind are those which the Minister may bring in the name of the company under section 169(7). But surely these are proceedings which should be brought by the company itself, if it has the necessary information or, where the company is in liquidation, by the liquidator. A situation may therefore arise in which the Minister may have in his possession a report giving the clearest evidence of misfeasance on the part of former directors and yet he may not give it to the company or to the liquidator.

It appears to me that probably the primary importance of a company investigation, if competently and fairly carried out, lies in disclosing, not only to the Minister but to the Parliament and to the public what went wrong and why the system of safeguards involved in the various requirements of the Act proved ineffective. No such system can prevent deliberate dishonesty and fraud and in cases where deliberate fraud is involved there is very much less to be said for publication of the inspector's report, certainly before criminal proceedings have been taken. But where large companies or groups of companies have been conducted by honest if misguided men, audited by reputable and competent auditors, and yet still collapse with little warning, surely sections of the community bona fide interested in such matters should be entitled to study the facts.

The sub-committee's answer to this view is that there are many other means of achieving this result, ranging from legislation down to discussion in professional journals and newspaper reports of relevant legal proceedings. Presumably remedial legislation is to be introduced without the need for it being explained by reference to facts which have happened. Newspaper reports of legal proceedings are necessarily limited to the particular individual transactions which are the subject of the charge. How can professional journals contain intelligent discussion of the issues involved unless the writers and readers alike know something of the facts which give rise to the discussion? I am afraid that I am unconvinced by the sub-committee's answer.

It does not follow that I regard the present situation as entirely satisfactory. The inspector's report is plainly and on its face only the opinion of the inspector, but it is frequently given a prominence which seems to clothe it with authority. It is therefore most important that inspectors should be cautious and restrained and do their utmost to observe the principles of justice and fair play. I know of no investigation in recent years in which an inspector has refused the application of any witness to be represented by counsel. What has been refused, and is plainly impracticable, is the application which involves counsel being present not only while his client is being examined, but on all other occasions in addition. It is also desirable that consideration be given to withholding reports or sections of reports which may give rise to the institution of criminal proceedings, at least until those proceedings are completed. For this purpose I think inspectors should consider, in cases where they find that persons have been guilty of serious criminal offences, the desirability of preparing their reports in such a way as will enable publication of parts only. If the principle that reports be never made available to the public be adhered to however, a Minister may find himself in the position of having in his possession a report which, being adequately documented, clearly demonstrates that a director or directors have been incompetent and unmindful of their obligations towards their companies and their shareholders. These gentlemen may be in the process of forming new companies or reconstructing old ones and calling upon the public for subscriptions to them. Is the Minister in such circumstances simply to watch this process and remain silent? Similarly, the creditors of a company may be asked to compound their debts and agree to a scheme of arrangement. Is the Minister to withhold publication of a report which might be important to them in arriving at their decision?

The problem is by no means simple and is undoubtedly a conflict between the desirability of protecting individuals against attacks upon their integrity on the one hand, and the need, which I believe to be a real one, of making public a report which may assist professional bodies and the public generally to prevent future company failures on the other. Perhaps the answer is that each case should be looked at individually and the decision to publish or to withhold publication of a report taken after a careful consideration of the relevant facts. Nor should it be forgotten that the reports of inspectors frequently serve to exonerate many people who have been associated with a company which has failed. To many members of the public it seems almost axiomatic that, if a company fails and large sums of money are lost, part of that money at all events must have gone into the pockets of directors. Most reports of inspectors in recent years have done much to exonerate many former directors and have no doubt been welcomed by them.

May I conclude by saying what is probably entirely unnecessary—namely that the views I have expressed in this discussion are entirely my own and that it would be quite wrong to regard them as ncessarily related in any way to the views of any Victorian Ministers.

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