THE FIDUCIARY NATURE OF A COMPANY BOARD'S POWER TO ISSUE SHARES

The fiduciary status of a company's board of directors affects all their powers under the memorandum and articles of association. In the result, an act of a board, though within a literal construction of a power, may be vitiated by reference to limitations which spring from its fiduciary character.

The particular power with which this article is concerned is the power to issue shares. The subject will be dealt with under these headings: (1) Historical sources of the board's power to issue shares; (2) the fiduciary nature of a board's powers generally; (3) For what purposes may shares properly be issued?; (4) The problem of an issue of shares for mixed purposes; (5) Proof of a board's purpose in issuing shares; (6) Consequences of an issue of shares for an improper purpose.

(1) HISTORICAL SOURCES OF THE BOARD'S POWER TO ISSUE SHARES

The first Companies Act, the U.K. Act of 1844[1] left it to the company to define and confer a power to issue shares in the deed of settlement.[2] The Act of 1856[3] introduced the memorandum and articles of association as the company's constitutive documents and an optional "model" set of articles in a Table in a Schedule to the Act. However, both the Act and Table B in the Schedule thereto were silent on the power to issue shares, except for Article 46 which was a general provision vesting in the directors the power to manage the company's business and to exercise all its powers not required by the Act or by

1 The Joint Stock Companies Registration Act, 1844 (7 & 8 Vic., c. 110).

2 The Act did empower the directors of any joint stock company registered under the Act "to conduct and manage the affairs of the company according to the provisions and subject to the restrictions of this Act, and of the deed of settlement, and of any by-law, and for that purpose to enter into all such contracts and do and execute all such acts and deeds as the circumstances may require; . . ." (s. 27). Moreover, s. 7 of the Act required a company's deed of settlement to make provision "For determining whether, and under what Circumstances, and on what Conditions, the Capital of the Company may be augmented, . . . by the Issue of new Shares or otherwise" and "For determining whether the Amount of new Capital shall or shall not be divided so as to allow such Amount to be apportioned amongst the existing Shareholders": Schedule (A), cll. 33, 34.

3 The Joint Stock Companies Act 1856 (19 & 20 Vic., c. 47).

the articles to be exercised by the company in general meeting. This "general management article" has been repeated almost verbatim in the scheduled Tables of all subsequent U.K. and Australian State Acts[4] and is now to be found in Article 73 in Table A in the Fourth Schedule to the "uniform" Australian Acts of 1961 and 1962.[5] Since the issuing of shares is not required by the Act, or, typically, by the articles, to be performed by the company in general meeting, the general management article makes this power exercisable by the directors.[6]

One further article in Table A calls for mention. Article 41 provides, in its first sentence,

> "Subject to any direction to the contrary that may be given by the company in general meeting, all new shares shall, before issue, be offered to such persons as at the date of the offer are entitled to receive notices from the company of general meetings in proportion, as nearly as the circumstances admit, to the amount of the existing shares to which they are entitled."

This article appeared in the Tables to earlier Acts.[7] "New shares" in this article means shares created by a resolution which increases nominal share capital. That this is so is made clear by the fact that the article follows Art. 40 which, in the light of s. 62 of the Act, deals with the increasing of share capital by the creation of new shares. It is anomalous that there is no similar express restraint on directors' disposition of shares forming part of a company's original capital.[8]

4 Cf. 1862 Act (U.K.), art. 55; 1929 Act (U.K.), art. 67; 1948 Act (U.K.), art. 80; 1936 Act (N.S.W.), art. 67; 1943 Act (W.A.), art. 67.

5 Article 73 reads as follows: "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 the aforesaid regulations or provisions, as may be prescribed by the company in general meeting; but no regulation of 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."

6 Obiter dicta in Campbell v. Rofe [1933] A.C. 91 (reversing 45 C.L.R. 82), at p. 99. Article 2 of Table A in the Fourth Schedule to the 1961 Act expressly acknowledges that "shares in the company may be issued *by the directors*" (emphasis supplied). There is no counterpart in the English Table A of 1948.

7 Cf. 1936 Act (N.S.W.) Art. 35; 1943 Act (W.A.), art. 35.

8 It may be thought that Art. 41 is superfluous since an ordinary resolution will be necessary to the creation of new shares and this will be passed only if shareholders know and approve of what is to become of them. Moreover, Art. 41 makes the pro rata distribution of new shares subject to nothing

As a result of the foregoing analysis, it may be accepted that the typical articles of association, and certainly Table A, vest in the directors without express qualification power to issue shares forming part of the original capital.[9]

(2) THE FIDUCIARY NATURE OF A BOARD'S POWERS GENERALLY

Directors have been referred to both as "agents" and as "trustees", sometimes casually, and at other times with qualification.[10] But analysis of the theoretical status of directors demonstrates that they are not properly classified either as agents or trustees but are *sui generis.* Upon incorporation of a company, the board is invested by law with those powers designated as theirs in the articles. The board is not a delegate either of the company itself or of the shareholders. Rather, like the shareholders in general meeting, it is a "constitutional organ" of the body corporate. "Constitutional organ" is apposite to denote those humans or groups of humans in whom some power of the body corporate is vested originally by the operation of the law on the registered constitution (the memorandum and articles) and on whatever additional factum may be necessary in the particular case, e.g. the appointment of directors by the subscribers or by the shareholders in general meeting. The constitutional organs of the company are to be distinguished from those humans who may be described as its "organs" in particular circumstances on the pragmatic "directing mind and will" test developed in and since Viscount Haldane's judgment in *Lennard's Carrying Co Ltd v. Asiatic Petroleum Co Ltd,*[11] though the board will usually satisfy that test too.

Although directors are not properly classifiable as agents or as trustees, yet like them, directors belong to that broad class called

more onerous than "any direction to the contrary that may be given by the company in general meeting". The effect of Art. 41 is to require, where an ordinary resolution does no more than create new shares, that they be offered to existing shareholders pro rata in accordance with the code set out in Art. 41, and to require that any other method proposed by the directors for the disposition of the new shares be brought to the shareholders' notice and approved by them.

9 Nor is there any Stock Exchange requirement either that shares in listed companies be offered to existing shareholders pro rata or that a listed company's articles require this, though there is an Exchange Recommendation "that new issues for cash should be offered to existing shareholders on a pro-rata ratio to the number of shares or class of shares held": A.A.S.E. Listing Manual, Section E, para. (2).

10 Cf. Ferguson v. Wilson (1866) L.R. 2 Ch. App. 77; Selangor United Rubber Estates Ltd v. Cradock (No. 3) [1968] 1 W.L.R. 1555 and cases there cited; Richard Brady Franks Ltd v. Price (1937) 58 C.L.R. 112 per Dixon J. at 142.

11 [1915] A.C. 705.

"fiduciaries".[12] With the directors may be contrasted the position of the company's other constitutional organ—the shareholders. A shareholder is under no duty to exercise his voting power for the benefit of the company as a whole and may vote with only his own private interests in mind.[13] Although the Court has always been prepared to interfere with an abuse of its power by a *majority* of shareholders,[14] it will more readily interfere with the exercise of powers of directors because of the fiduciary duty incumbent upon the latter.[15]

Directors have often been referred to and held accountable as agents or trustees[16] and their status and duties have been developed by reference to those of agents and trustees. Where, for example, directors have made a secret profit out of a share issue, they are, like agents accountable for the profit made.[17] The fiduciary duty of directors is usually thought to be adequately described by the statement that they must act *"bona fide* for the benefit of the company as a whole". This linguistic formula[18] derives from the judgment of Lord Lindley M.R. in *Allen v. Gold Reefs of West Africa Ltd,*[19] a case concerned with abuse of the power of a majority of shareholders to alter articles, but has been adopted and adhered to with remarkable consistency in cases concerned with alleged abuses of directorial powers.[20] Sometimes the expression has become *"bona fide and* for

12 It seems that the categories of fiduciary relationships, like those of negligence, are never closed. Members of bodies corporate constituted under the Conveyancing (Strata Titles) Act 1961 (N.S.W.) have recently been classified as fiduciaries by analogy with company directors: Re Steel & Ors and the Conveyancing (Strata Titles) Act 1961 (1968) 88 W.N. (Pt. 1) (N.S.W.) 467.

13 North-West Transportation Co Ltd v. Beatty (1887) 12 App. Cas. 589.

14 The question has arisen chiefly in respect to an alteration or proposed alteration of articles; cf. Allen v. Gold Reefs of West Africa [1900] 1 Ch. 656; American Delicacy Co Ltd v. Heath (1939) 61 C.L.R. 457.

15 Ngurli Ltd v. McCann (1953) 90 C.L.R. 425, 439.

16 Madrid Bank v. Pelly (1869) 7 Eq. 442; Hirsche v. Sims [1894] A.C. 654; Parker v. McKenna (1870) 10 Ch. App. Cas. 96.

17 Eg. see Shaw v. Holland [1900] 2 Ch. 305 (C.A.); In re Madrid Bank; ex parte Williams (1866) 2 Eq. 216; Parker v. McKenna (1870) 10 Ch. App. Cas. 96; Boston Deep Sea Fishing & Ice Co v. Ansell (1888) 39 Ch. 339; Furs Ltd v. Tomkies (1936) 54 C.L.R. 583; Regal (Hastings) Ltd v. Gulliver [1942] 1 All E.R. 378.

18 Which, according to Rich J., "tends to become a cant expression but is not yet a shibboleth": Richard Brady Franks Ltd v. Price (1937) 58 C.L.R. 112 at 138.

19 [1900] 1 Ch. 656.

20 Cf. Isaacs J. in Australian Metropolitan Life Assurance Co Ltd v. Ure (1923) 33 C.L.R. 199 at 217 and cases there cited; Latham C.J. in Richard Brady Franks Ltd v. Price, ante cit., at 135; though cf. Viscount Finlay in Hindle

benefit of the company".[21] The conjunction has not been intended to signify a change in meaning though the original formula is preferable, because the cases show that the expression

> means not two things but one thing. It means that [a director] must proceed upon what in his honest opinion, is for the benefit of the company as a whole.[22]

The expression is purposive; emphasis must be placed on "for" not "benefit"; the formula requires directors to have acted for what they believed, not for what a Court may conclude, or may otherwise be demonstrated, to have been as a matter of objective fact, for the company's benefit.[23] The test is not failed by directors merely because their act can be shown not to have benefited the company; nor will a plaintiff fail if he cannot prove as much.[24]

"The company *as a whole*" in the classical formula means that the duty is to be *measured* by reference to the company's corporators, that is the general body of shareholders.[25] As Barwick C.J. observed in *Ashburton Oil N.L. v. Alpha Minerals N.L.*[26] the words "as a whole" in the classical formula are somewhat tautologous.[27] However, they do serve to emphasize that "the company" is not a mere majority of its shareholders.

Failure to consider the general body of shareholders at all will apparently enable a purported exercise of a power to be challenged

---

v. John Cotton Ltd (1919) 56 Sc. L.R. 625: "Directors exercising their discretionary powers, . . . , must not do so capriciously, arbitrarily or corruptly, and they must exercise their powers in good faith": ibid., 630.

21 Cf. Helsham J. in Provident International Corporation v. International Leasing Corporation (1969) 89 W.N. (Pt. 1) (N.S.W.) 370 ("Provident International") at 376; Starke J. in Mills v. Mills (1938) 60 C.L.R. 150, at 175.

22 Per Evershed M.R. in Greenhalgh v. Aderne Cinemas Ltd [1951] Ch. 286, at p. 291. The subjective nature of the test to be applied had been similarly emphasized by the Earl of Selborne in Hirsche v. Sims [1894] A.C. 654: "[Did the defendants] truly and reasonably believe at the time that what they did was for the benefit of the company?" (ibid., 661).

23 In Re Smith and Fawcett Ltd [1942] Ch. 304, 306.

24 Cf. Menzies J. in Ashburton Oil N.L. v. Alpha Minerals N.L. (1971) 45 A.L.J.R. 162, at 166 E.

25 Per Helsham J. in Provident International, ante cit., at p. 377, citing Greenhalgh v. Aderne Cinemas Ltd [1951] 1 Ch. 286; and this is thought to be the meaning of Dixon J.'s dictum in Richard Brady Franks Ltd v. Price: "the fiduciary duty of the directors is to the company *and the shareholders*": (1937) 58 C.L.R. 112, at p. 143 (emphasis supplied).

26 (1971) 45 A.L.J.R. 162.

27 Ibid. 163.

by them.[28] The difficulty and indeed the inappropriateness of applying this general formula where shareholders are not all of the one class so that a measure will affect them discriminately was considered in *Peters' American Delicacy Co Ltd v. Heath.*[29] Dixon J. was led in that case to observe that "the reference to 'benefit as a whole' is but a very general expression negativing purposes foreign to the company's operations, affairs and organisations."[30] The mere fact that a measure has a discriminatory effect[31] or favours a majority against a minority[32] does not vitiate it.

It has become acknowledged law that the powers of directors, like those of agents generally and persons having powers of appointment[33] must be exercised only for the purpose for which they were granted and that an exercise of a power for an improper purpose will warrant judicial interference by way of declaration or injunction.[34] Exercise of a power for an extraneous purpose is called "fraud on a power"[35] and was thus explained by Lord Parker in *Vatcher v. Paull*:[36]

> The term 'fraud' in connection with fraud on a power does not necessarily denote any conduct on the part of the appointor amounting to fraud in the common law meaning of the term or any conduct which could properly be termed dishonest or immoral. It merely means that the power has been exercised for a purpose, or with an intention, beyond the scope of or not justified by the instrument creating the power.[37]

---

28 Provident International, ante cit., at 377.

29 (1939) 61 C.L.R. 457.

30 Ibid. 512.

31 Ibid. per Latham C.J. at 480.

32 Ibid. per Rich J. at 495.

33 Cf. Aleyn v. Belcher (1758) 1 Eden 132; Vatcher v. Paull [1915] A.C. 372.

34 "Directors are fiduciary agents and their powers must be exercised honestly in furtherance of the purposes for which they are given. Under the general law of agency it is a breach of duty for an agent to exercise his authority for the purpose of conferring a benefit on himself or upon some other person to the detriment of his principal": Richard Brady Franks Ltd v. Price (1937) 58 C.L.R. 112 per Dixon J., at p. 142. And see the cases cited under the next side-heading. On the question, what a plaintiff must prove in order to obtain injunctive relief, see Ashburton Oil N.L. v. Alpha Minerals N.L. (1971) 45 A.L.J.R. 162.

35 E.g. see Lord Hatherley L.C. in Topham v. Duke of Portland (1869) 5 Ch. App. 40: "The Court will not allow him [the appointor] to interpret the donor's intention in any other sense than the Court itself holds to be the true construction of the instrument creating the power and a literal execution of the power, with a purpose which it does not sanction, is regarded as a fraud on the power": ibid., 59.

36 [1915] A.C. 372 (P.C.).

37 Ibid. 378.

This raises the question of the relationship between impropriety of purpose and the concept of acting *bona fide* for the benefit of the company as a whole, a question which has been the subject of some academic interest.[38] At the outset it must be acknowledged that in many dicta impropriety of purpose seems to have been regarded either as synonymous with or at least as a manifestation of lack of *bona fides,* e.g.

> Where the question is one of abuse of powers, the state of mind of those who acted, and the motive on which they acted, are all important, and you may go into the question of what their intention was, collecting from the surrounding circumstances all the materials which genuinely throw light upon that question of the state of mind of the directors so as to show whether they were honestly acting in discharge of their powers in the interests of the company or were acting from some bye-motive, possibly of personal advantage, or for any other reason.[39]
>
> . . . it must be exercised as all such powers must be, bone fide—that is, *for the purpose for which it was conferred,* not arbitrarily or at the absolute will of the directors, but honestly in the interests of the shareholders as a whole.[40]
>
> The validity of the directors' resolution, therefore, must depend on the question whether they exercised the power in good faith for the purpose for which the power was given.[41]
>
> Directors of a company are fiduciary agents and a power conferred upon them cannot be exercised in order to obtain some private advantage or for any purpose foreign to the power.[42]
>
> Directors are fiduciary agents and their powers must be exercised honestly in furtherance of the purposes for which they are given.[43]
>
> The power must be used bona fide for the purpose for which it was conferred, . . .[44]
>
> If in fact, he exercised the power for an ulterior purpose it would not be in law a bona fide exercise thereof.[45]

---

38 Cf. Afterman, COMPANY DIRECTORS AND CONTROLLERS, 1970, p. 64; Parsons, *The Directors' Duty of Good Faith* (1967) 5 Melb. Univ. L.R. 395, 419.

39 Per Viscount Finlay in Hindle v. John Cotton Ltd (1919) 56 Sc. L.R. 625, 630-631.

40 Per Isaacs J. in Australian Metropolitan Life Assurance Co Ltd v. Ure (1923) 33 C.L.R. 199, 217.

41 Per Rich J. in Mills v. Mills (1938) 60 C.L.R. 150, 169.

42 Per Dixon C.J. in Mills v. Mills, ante cit., at 185, describing the appellants' contention.

43 Per Dixon J. in Richard Brady Franks Ltd v. Price (1937) 58 C.L.R. 112, 142.

44 Per Williams A.C.J., Fullagar and Kitto JJ. in Ngurli Ltd v. McCann (1953) 90 C.L.R. 425, 439-440.

45 Ibid. 444.

> . . . powers conferred on directors by the articles of association of a company must be used bona fide for the benefit of the company as a whole and not to obtain some private advantage.[45a]

The linking of propriety of purpose with the notion of subjective good faith is understandable for in many cases the particular improper purpose in question was that the directors were seeking to benefit themselves at the expense of the company; in other words, on the facts of the particular cases, impropriety of purpose was co-extensive with a kind of directorial culpability, if not amounting to fraud at common law.[46]

Three further factors which have caused impropriety of purpose to be linked inextricably with lack of good faith may be noted. The first is the convenient though simplistic categorization of the relevant directorial purposes in any case into two: an ostensible and legitimate purpose on the one hand, and a "real" and illegitimate purpose on the other; e.g.,

> [The power to issue shares] must not be used under the cloak of [raising sufficient capital for the benefit of the company as a whole] for the real purpose of benefiting some shareholders or their friends at the expense of other shareholders . . .[47]

The complexity of what might be the purposes and motives of a board has rarely been confronted by the courts.

The second factor referred to is the apparently inevitable use of morally charged terms to refer to the actions of directors who use a power for an unwarranted purpose. "Improper" itself is a prime example. Even in the passage from *Vatcher v. Paull* noted earlier, although it was said that fraud on a power did not necessarily involve fraud in the common law sense, yet the notion of *abusing* a power by exercising it for an *improper* purpose *under colour* of a legitimate purpose is present. All this and mention of "cloaks" and "ulterior" purposes gives "improper" a moral connotation rather than a mere sense of "unwarranted". Morally neutral expressions e.g. "a collateral

---

45a Per Gibbs J. in Ashburton Oil N.L. v. Alpha Minerals N.L., ante cit., at 171G.

46 Moreover, "It could be that in any particular case subjective good faith on the part of the directors is a material element for consideration in determining the question of any abuse of power," per Helsham J. in Provident International, at 377.

47 Ngurli Ltd v. McCann (1953) 90 C.L.R. 425, 440; and cf. the recurrent notion of "ulterior" purpose, ibid. 444, 445. And cf. R. v. Brighton Corporation (1907) 96 L.T.R. 762 per Vaughan Williams L.J. at 763; Moulton L.J. at 764 and Buckley L.J. at 765.

and extraneous object"[48] have been the exception rather than the rule in this area of the law.

A third factor is the well known phenomenon of the moral colour given to actions by the very legal sanctions attaching to them.

The effect of the foregoing has been to elevate propriety of purpose from its status as a demonstration of subjective good faith into an independent and objective test of validity. But this poses a difficulty, in that "for a proper purpose" looks suspiciously like the objective notion "for the benefit of the company" which the courts had rejected. A solution seems to be that there was always an objective element in "bona fide for the benefit of the company as a whole," namely that the directors must have "truly *and reasonably* believed at the time that what they did was for the benefit of the company,"[49] and it is not permitted directors to say that they reasonably believed that it was *bona fide* for the benefit of the company for them to exercise a power for an improper purpose. Perhaps this is what Helsham J. had in mind when he said,

> . . . it is my opinion that the requirement of bona fides of a director must be considered in relation to the power and the exercise of it, not his belief or state of mind.[50]

The solution offered enables the requirements that directors act honestly and that they exercise their powers for proper purposes to be viewed as sub-classes of the general formula that they act "*bona fide* for the benefit of the company as a whole". The alternative is to treat the latter formula as synonymous with the requirement that directors act honestly, so that there are but two independent rules: honesty and propriety of purposes. Whichever is preferred, clearly the requirements of honesty and propriety of purpose are distinct, though overlap will occur, e.g. where directors deceitfully seek to achieve an improper purpose under colour of a proper one.

(3) FOR WHAT PURPOSES MAY SHARES PROPERLY BE ISSUED?

Where a power is conferred by one individual upon another, the task of ascertaining the purpose for which it is properly exercisable may be a relatively simple matter. A duty not to exercise a power for

48 Per Dixon J. in Mills v. Mills, ante cit., at 185.

49 Per Earl of Selborne in Hirsche v. Sims [1894] A.C. 654, 661.

50 Provident International, at 377 citing Ngurli Ltd v. McCann, ante cit., and Vatcher v. Paull, [1915] A.C. 372, 378. If the word "exclusively" had appeared between the words "not" and "his" there could be no argument with this dictum.

a purpose other than that for which it was given seems to have been recognized chiefly in cases concerning powers of appointment. In such cases the purpose of the donor of the power was manifest.[51] After all, such conferrals of power are usually isolated acts for specific objects. Thus, in *Aleyn v. Belcher*[52] the Court had no difficulty in applying the general principle to a power of appointment:

> No point is better established than that, a person having a power, must execute it *bona fide* for the end designed, otherwise it is corrupt and void. The power here was intended for a jointure, not to pay the husband's debts. The motive that induced *Edmund* to execute it was not a provision for his wife.[53]

In *Fraser v. Whalley,*[54] an early authority on the issue of shares for an improper purpose, the "proper" purpose was single and manifest. The shareholders of a statutory railway company authorised the directors to issue shares to raise capital to invest in shares in another company. This authority was not implemented, but two and a half years later, the directors, purporting to act on it, proposed to issue shares (a) to persons favourably disposed to them, (b) to raise capital to *lend* to the other company. An injunction issued to restrain them.

But unlike the situation in *Fraser v. Whalley,* the power to issue shares vested in a registered company's board is a universal rather than an isolated and special phenomenon. If, upon incorporation, the promoters did entertain an intention as to how the power to issue shares should be exercised by the company's first directors and this was known to the latter, presumably evidence thereof would be admissible to establish the scope of "propriety of purpose". However, this does not seem to have occurred in any decided case and the question of what is a proper purpose has been left at large for the Court.

Although the first task of the Court is always to construe the power, it is usually subject to no express limitation.[55] The general proposition that the object of raising capital is the primary purpose and always a proper purpose for the exercise of the power to issue shares, does

51 Cf. Aleyn v. Belcher (1758) 1 Eden 132; Vatcher v. Paull, ante cit. Doubtless a similar observation is applicable to a delegation of authority from principal to agent.

52 (1758) 1 Eden 132.

53 Ibid. 138.

54 (1864) 2 H. & M. 10.

55 Cf. Barwick C.J. in arguendo in Harlowe's Nominees Pty Ltd v. Woodside (Lakes Entrance) Oil N.L. (1968) 121 C.L.R. 483, 486.

not seem to have been doubted.[56] But an issue of shares does not necessarily produce capital—at least not immediately—and even if it does so, that may not have formed any part of the directors' purpose, and even if it did, it may have formed only a minor part.

The decided cases seem to establish the following points in relation to propriety of purpose in the exercise of the power to issue shares:

(1) Absence of any consideration at all of the capital to be raised by an issue supports an allegation of impropriety of purpose: *Ansett v. Butler Air Transport Ltd (No. 1)*.[57]

(2) A board's purpose of securing its control by installing as shareholders, persons who are favourably disposed to the existing directors, or, what has been treated as the same thing, of preventing an interest unfavourable to them from gaining power, is, by overwhelming authority, improper: *Fraser v. Whalley*;[58] *Punt v. Symons & Co Ltd*;[59] *Abbotsford Hotel Ltd v. Kingham*;[60] *Piercy v. Mills & Co Ltd*;[61] *Australian Metropolitan Life Assurance Co Ltd v. Ure*;[62] *Grant v. John Grant & Sons Pty Ltd*;[63] *Ngurli Ltd v. McCann*;[64] *Ansett v. Butler Air Transport (No. 1)*;[65] *Hogg v. Gramphorn Ltd*;[66] *Harlowe's Nominees Pty Ltd v. Woodside (Lakes Entrance) Oil Co N.L.*;[67] *Bamford v. Bamford*;[68] *Provident International Corporation v. International Leasing Corporation*;[69] *Ashburton Oil N.L. v. Alpha Minerals N.L.*[70] In several of these cases the decision to issue shares was prompted by an

56 Cf. Harlowe's Nominees Pty Ltd v. Woodside (Lakes Entrance) Oil N.L. (1968) 121 C.L.R. 483, 493; Ngurli Ltd v. McCann (1953) 90 C.L.R. 425, 439-440. The same remark can be made of the power to make calls: Savoy Corporation Ltd v. Development Underwriting Ltd (1961) 80 W.N. (N.S.W.) 1021.

57 (1958) 75 W.N. (N.S.W.) 299.

58 (1864) 2 H. & M. 10—that the directors intended to allot to persons who would support them was mentioned as a subsidiary ground for restraining them.

59 [1903] 2 Ch. 506.

60 (1910) 102 L.T.R. 118, 119.

61 [1920] 1 Ch. 77.

62 (1923) 33 C.L.R. 199.

63 (1950) 82 C.L.R. 1 esp. per Williams J. at 32.

64 (1953) 90 C.L.R. 425.

65 (1958) 75 W.N. (N.S.W.) 299 ("Ansett").

66 [1967] Ch. 254 ("Hogg").

67 (1968) 121 C.L.R. 483 ("Harlowe's Nominees").

68 [1969] 2 W.L.R. 1107.

69 (1969) 89 W.N. (Pt. 1) (N.S.W.) 370, 379.

70 (1971) 45 A.L.J.R. 162.

actual or suspected attempt at a take-over[71] and sometimes the device used was to issue shares to trustees for the company's employees.[72]

Only two dissonant notes have been sounded against the tenor of these cases. *Australian Metropolitan Life Assurance Co Ltd v. Ure, ante cit.*, makes it clear that it may be proper for directors to exercise at least one power (the power disapprove a share transfer) in order to prevent a person thought to be "undesirable" (he was a disbarred solicitor) from being elected to the board. Why not issue shares for the same purpose? In *Savoy Corporation Ltd v. Development Underwriting Ltd*[72a] it was held proper for directors to consider the possibility of a take-over when deciding whether to make a call on shares. Why not consider it when deciding whether to issue shares? No general legitimization of self-entrenchment by directors could be mounted on these frail bases.

(3) A purpose of qualifying the allottees to be elected as directors is improper: *Grant v. John Grant & Sons Pty Ltd.*[73]

(4) Directors' undisclosed interest in the allotment precludes a finding of a *bona fides*: *In re Madrid Bank; ex parte Williams.*[74]

(5) A purpose of presenting the company to other interests as one having a substantial paid up capital is improper: *Provident International Corporation v. International Leasing Corporation.*[75]

(6) A purpose of raising capital for the immediate needs of the company is not an essential element to the validity of every issue of shares. This statement calls for some elaboration. As long ago as 1903 in *Punt v. Symons % Co Ltd,*[76] Byrne J. said of the issue of shares in that case,

> I'm satisfied that the directors' intention here was to enable the minority shareholders to control the majority. A power of this kind must be exercised for the benefit of the company: primarily it is given to enable them to raise capital.[77]

---

71 Cf. Ansett; Hogg; Harlowe's Nominees; Bamford v. Bamford.
72 Ansett; Hogg.
72a (1961) 80 W.N. (N.S.W.) 1021.
73 (1950) 82 C.L.R. 1.
74 (1866) 2 Eq. 216.
75 (1969) 89 W.N. (Pt. 1) (N.S.W.) 370, 377-378.
76 [1903] 2 Ch. 506.
77 Ibid. 515-516.

In *Grant v. John Grant & Sons Pty Ltd*[78] Williams J., taking an expression from the headnote to *Piercy v. S. Mills & Co Ltd*,[79] said,

> When a company is not in need of further capital directors are not entitled to use this power for the purpose of maintaining their control or the control of themselves and their friends.[80]

and two and a half years later, in *Ngurli Ltd v. McCann*[81] it was said that

> the power must be used bona fide for the purpose for which it was conferred, that is to say, to raise sufficient capital for the benefit of the company as a whole.[82]

These passages, at least when taken in isolation from the cases in which they occurred, made it appear that the object of raising capital for the company's immediate needs must always be at least part of a board's purpose in issuing shares. *Harlowe's Nominees Pty Ltd v. Woodside (Lakes Entrance) Oil Co N.L.*[83] now makes it clear that this is not so,[84] and that a desire to give financial stability to the company in its future programme will do so.[85]

(7) Offering to allot shares to some existing shareholders and not to others is *prima facie* improper.[86] However, little evidence of special circumstances will be needed to justify the board's dis-

---

78 (1950) 82 C.L.R. 1.

79 [1920] 1 Ch. 77.

80 (1950) 82 C.L.R. 1, 32.

81 (1953) 90 C.L.R. 425.

82 Ibid. 439-440.

83 (1968) 121 C.L.R. 483.

84 "The principle is that although primarily the power is given to enable capital to be raised when required for the purposes of the company, there may be occasions when the directors may fairly and properly issue shares for other reasons, so long as those reasons relate to a purpose of benefiting the company as a whole, as distinguished from a purpose, for example, of maintaining control of the company in the hands of the directors themselves or their friends": ibid. 493.

85 Ibid. per Kitto J. at 487, per Barwick C.J. at 488. Strictly this was not a novel approach, in spite of the line of authority referred to. In Punt v. Symons & Co Ltd [1903] 2 Ch. 506, Byrne J. had observed that there might be proper reasons for issuing shares other than the raising of capital, and he instanced the creation of a sufficient number of shareholders to enable statutory powers to be exercised!

Harlowe's Nominees has now been cited in Provident International Corporation v. International Leasing Corporation (1969) 89 W.N. (Pt. 1) (N.S.W.) 370.

86 Ngurli Ltd v. McCann (1953) 90 C.L.R. 425.

crimination. Preference of one *creditor* to another has been held not to be acting contrary to the interests of shareholders even where the preferred creditor was a director: *Richard Brady Franks Ltd v. Price.*[87] That case raises the possibility that where two or more shareholders are also creditors of the company, the directors may prefer one against the other in their capacity as creditors.

(8) It is an abuse of power to allot shares to persons who, the directors know and intend, will ultimately transfer the shares to or otherwise confer a benefit upon the directors themselves.[88]

(4) THE PROBLEM OF AN ISSUE OF SHARES FOR MIXED PURPOSES

It has already been observed[89] that the cases show a remarkable uniformity in categorizing the purposes to be considered in any set of circumstances into two: one, ostensible and proper; the other, real and improper. It may well be that the facts of share issue cases naturally lend themselves to this sort of categorization. In *Mills v. Mills*[90] for example, it was observed expressly that there were "only two sensible purposes or reasons",[91] "two rival explanations",[92] to be considered. But such explicitness is not common.

The recurrent facile contradistinction of real and ostensible purposes says little if it is accepted that an ostensible or apparent purpose is no purpose at all. If it can be predicated that a board is seeking to achieve one thing under colour of seeking to achieve another, only the former is to be regarded in a consideration of propriety of purpose, though the pretence will be relevant to the issue of the directors' subjective good faith.

But is it not possible for a board to have more than one real purpose? If so, the need to act for "*a* proper purpose" will have to be more precisely defined. Indeed perhaps the common judicial analysis into "real" and "ostensible" purposes is, in some cases, as well expressed in terms of two real purposes, one effective and the other ineffective.

There seem, *a priori,* to be four relevant possibilities as to what a plaintiff must prove in order to establish "improper purpose":

87 (1937) 58 C.L.R. 112.

88 In re Madrid Bank; ex parte Williams (1866) 2 Eq. 216; Madrid Bank v. Pelly (1869) 7 Eq. 442; Parker v. McKenna (1870) 10 Ch. App. Cas. 96.

89 See p. 000 ante.

90 (1938) 60 C.L.R. 150.

91 Ibid. per Rich J. at 170.

92 Ibid. per Dixon J. at 187-8.

(a) That the board's purpose was totally improper. In *Ansett v. Butler Air Transport Ltd (No. 1)*[93] this was alleged to be the fact and apparently this approach was accepted by the judge. It was the approach taken in *Richard Brady Franks Ltd v. Price*[94] by Long Innes C.J. in Eq.[95] but was considered too stringent by Latham C.J. in the High Court on appeal.[96] Of course the common finding that a board's purpose was, as a matter of fact, wholly bad does not determine the legal point being discussed; cf. *Fraser v. Whalley;*[97] *Piercy v. S. Mills & Co;*[98] *Ngurli Ltd v. McCann;*[99] and *per* Lowe J., the trial judge, in *Mills v. Mills.*[100] But there is no decision to the effect that a plaintiff will fail if he proves anything less than a "totally improper purpose".

(b) That the board's purpose was predominantly improper. In practice, once an improper purpose is shown to exist, it will probably be shown to be the predominant purpose.

In *R. v. Brighton Corporation*[101] Buckley L.J. noted that if the defendant council there had two purposes, one proper and one improper, this alone would afford no ground for the Court's interference. This suggests that a plaintiff would have to prove that the improper purpose was dominant.

In no case was the question of mixed purpose in the issue of shares considered so thoroughly as in *Mills v. Mills.*[102] The trial judge, Lowe J., thought that the directors' "*main* reason for passing the resolution" was a proper one,[103] (though he had formulated the issue by asking whether the resolution was passed *solely* for the improper purpose.)[104] Latham C.J. said,

> A resolution may have been passed honestly in the exercise of the directors' discretion but also with a view of creating voting power to which it was thought that ordinary shareholders, in view of the relative extent of their interests in the assets of the company were fairly entitled. Again, even

93 (1958) 75 W.N. (N.S.W.) 299.
94 (1937) 58 C.L.R. 112.
95 Ibid. 122.
96 Ibid. 144-145.
97 (1864) 2 H. & M. 10.
98 [1920] 1 Ch. 77.
99 (1953) 90 C.L.R. 425: "Horace was thinking only of himself" (ibid. 446) and the finding of the trial judge Mayo J. (ibid. 440).
100 (1938) 60 C.L.R. 150, 161.
101 (1907) 96 T.L.R. 762.
102 (1938) 60 C.L.R. 150.
103 Ibid. 179, emphasis supplied.
104 Ibid. 161.

> though the view of the directors in passing the resolution was not *solely* that of creating voting power which could be used by them as desired, yet, if the substantial object of the directors was to bring about this result, the resolution might be held to be invalid.[105]

To a generally similar effect, Dixon J. said

> . . . it may be thought that a question arises whether there must be an entire exclusion of all reasons, motives or aims on the part of the directors, and all of them, which are not relevant to the purpose of a particular power. When the law makes the object, view or purpose of a man, or of a body of men, the test of the validity of their acts, it necessarily opens up the possibility of an almost infinite analysis of the fears and desires, proximate and remote, which, in truth, form the compound motives usually animating human conduct. But logically possible as such an analysis may seem, it would be impracticable to adopt it as a means of determining the validity of the resolutions arrived at by a body of directors, resolutions which otherwise are ostensibly within their powers. The application of the general equitable principle to the acts of directors managing the affairs of a company connot be as nice as it is in the case of a trustee exercising a special power of appointment. It must, as it seems to me, take the substantial object the accomplishment of which formed the real ground of the board's action. If this is within the scope of the power, then the power has been validly exercised. But if, except for some ulterior and illegitimate object, the power would not have been exercised, that which has been attempted as an ostensible exercise of the power will be void, notwithstanding that the directors may incidentally bring about a result which is within the purpose of the power and which they consider desirable.[106]

This "dominant" or "substantial" motive approach assumes that any issue of shares has one "actuating motive",[107] or "moving cause"[108] and that an issue of shares cannot be prompted by two equally powerful purposes.

(c) That the improper purpose was at least as influential as the proper purpose. There is no clear judicial endorsement of this test. The dicta most favourable to it are the following. In *Hogg v. Gramphorn Ltd*[109] Buckley J. observed that the issue had not

---

105 Ibid. 161-162.
106 Ibid. 185-186.
107 Per Dixon J. in Mills v. Mills (1938) 60 C.L.R. 150 at 188.
108 Per Lord Shaw in Hindle v. John Cotton Ltd (1919) 56 Sc.L.R. 625 at 631.
109 [1967] Ch. 254.

been made "with the single-minded purpose *or even the primary purpose* of benefiting the company"[110] and in *Mills v. Mills*[111] Latham C.J.[112] and Rich J.[113] suggested that if the proper purpose was anything less than dominant, the issue was vitiated. Their Honours may, however, have taken it for granted that a concomitant of a less than predominant proper purpose, is a predominant improper purpose.

(d) That the improper motive was, to any extent, influential. The dicta most favourable to this view are the following. In *Hogg v. Cramphorn Ltd*[114] Buckley J. observed that the issue had not been made *"with the single-minded purpose* or even the primary purpose of benefiting the company".[115] In *Mills v. Mills*[116] Latham C.J. thought it sufficient for the plaintiff to show that a "substantial" object was improper.[117] The majority judgment in *Harlowe's Nominees* suggests that proof of *a* purpose of an improper nature, would have vitiated the issue.[118] In *Ashburton Oil N.L. v. Alpha Minerals N.L.*, Gibbs J. considered that on an application for an interlocutory injunction, what must be established is that "a substantial purpose" was improper.[119] These cases are inconclusive.

It can, however, be confidently asserted that the incidental promotion of directors' own interests or purposes merely in the course of promoting those of the company will not render them chargeable with breach of fiduciary duty.[120]

The preponderance of authority favours test (2) but this may be because, in practice, one purpose dominates, or because the courts feel obliged to identify one purpose as dominant. But it may be asked whether it is not consistent with the fiduciary character of the directors' powers to require that they should not have been exercised for an improper purpose to any "significant"

110 Ibid. 270, emphasis supplied.
111 (1938) 60 C.L.R. 150.
112 Ibid. 161-162.
113 Ibid. 170.
114 [1967] 1 Ch. 254.
115 Ibid. 270, emphasis supplied.
116 (1938) 60 C.L.R. 150.
117 Ibid. 161-2.
118 (1968) 121 C.L.R. 483, 494-5.
119 (1971) 45 A.L.J.R. 162, 172 G.
120 Cf. Earl of Selborne in Hirsche v. Sims [1894] A.C. 654, 660-661; Mills v. Mills (1938) 60 C.L.R. 150 per Latham C.J. at 163-4; Harlowe's Nominees, 493.

or "substantial", even though less than dominant, degree, and to permit a plaintiff, notwithstanding the judgment of Dixon J. in *Mills v. Mills* quoted at p. 16 *ante,* to succeed if he proves impropriety even to this limited extent.

(5) PROOF OF A BOARD'S PURPOSE IN ISSUING SHARES

The decided cases, and in particular *Harlowe's Nominees,* give the impression that it is difficult for a plaintiff to prove impropriety of purpose.[121] Certainly the cases bear out the dictum of Latham C.J. that

> A court . . . does not presume impropriety . . . The onus is on the plaintiff who challenges the action of the directors to establish that they did not act bona fide for the benefit of the Company.[122]

Moreover, a plaintiff-appellant will have to convince the appellate court that there was no evidence which could support a finding of propriety of purpose,[123] and an appellate court will be reluctant to interfere when so much depends on the conduct of witnesses in the witness-box.[124]

A plaintiff will be fortunate indeed if an improper motive is to be found in the board's minutes. In the more common case, he will have to adduce evidence of circumstances surrounding the passing of the resolution and persuade the Court to draw inferences adverse to the board.[125] Although the Court will impute a purpose to persons passing a resolution[126] it will not readily impute an improper one.

It is suggested that in the absence of special considerations, a plaintiff must prove an improper purpose on the part of a majority of the board's members.[127] Sometimes this will be done by proving positive impropriety on the part of one or more directors and acquiescence

121 The plaintiff also failed in Abbotsford Hotel Ltd v. Kingham (1910) 102 L.T.R. 118; Australian Metropolitan Life Assurance Co Ltd v. Ure (1923) 33 C.L.R. 199 and Mills v. Mills (1938) 60 C.L.R. 150.

122 Richard Brady Franks Ltd v. Price (1937) 58 C.L.R. 112, 135.

123 Cf. Bankes L.J. in Shuttleworth v. Cox Brothers & Co Maidenhead) Ltd [1927] 2 K.B. 9: "In the present case it seems to me impossible to say that the action of these defendants was either incapable of being for the benefit of the company or such that no reasonable man could consider it for the benefit of the company": ibid. 19.

124 Cf. Harlowe's Nominees.

125 Cf. Ngurli Ltd v. McCann (1953) 90 C.L.R. 425, 441.

126 Peters American Delicacy Co Ltd v. Heath (1939) 61 C.L.R. 457 per Dixon J. at 512-513.

127 This was asserted in Harlowe's Nominees at 489, and seems to have been accepted by the High Court at 492.

on the part of others.[128] But, the point is that in any case impropriety of purpose must be shown to have "tainted" a majority.

The reasoning which, it is submitted, leads to this conclusion is as follows: (1) at common law, not only were the members of a company "incorporated" but so were the individuals comprising any smaller organ[129] and, like the corporators, they were an "essential part of the corporation".[130] (2) There is nothing in the Companies Act to exclude the application of this principle to registered companies; (3) at common law, a corporation's power to act was exercisable by an act of all the members of the relevant constitutional organ[131] or, where a definite number of individuals were incorporated, after notice of meeting to all and a major part attended, by an act of a major part of that major part so assembled.[132] (4) Since a board of directors consists at any one time of a definite number of individuals, the common law quorum is a bare majority of that number, and unless the articles fix the quorum at a larger number (a provision of which an outsider would have constructive notice), an outsider could successfully set up as an act of the board, a joint act purporting to be that of the board, participated in by a bare majority; (5) at the meeting at which a board performs the *act* of resolving to issue shares, it may evince its purpose and so long as that purpose was shared,

128 As was attempted in Harlowe's Nominees.

129 A-G v. Davey (1741) 2 Atk. 212 esp. per Hardwicke L.C. at 212: ". . . I am of the opinion that the three are a corporation for the purpose they are appointed."

130 So that a bare resolution by the general meeting to remunerate directors for their services was held to be nudum pactum because, like partners, they were bound to serve as part of their status: Dunston v. The Imperial Gas Light & Coke Co (1832) 3 B. & Ad. 125.

131 Cf. dicta by Rolphe B. in Ludlow Corporation v. Charlton (1840) 6 M. & W. 815, 823 and by Parke B. in Ridley v. Plymouth etc Co (1848) 2 Exch. 711, 717.

132 A-G v. Davey (1741) 2 Atk. 212 (election of a chaplain by three corporators); A.-G. v. Scot (1750) 1 Ves. Sen. 413 (presentation and election of minister by twenty-five parishioners pursuant to Lord Chancellor's decree); and cf. Com. Dig. tit. Franchise, F.11 (the act of "the major part of the corporators corporately assembled"); and R. v. Windham (1776), 1 Comp. 377. "A major part of the corporators" was the phrase used by the 33 Hen. VIII, c.27 in a purported statement of the common law. That would make it clear that a major part of the members must assemble. It was so decided in Hascard v. Somany (1693), 1 Freem.K.B. 504 and affirmed to be the law by Lord Mansfield in R. v. Monday (1777), 2 Cowp. 530, at p. 538. These authorities were cited with approval by Wills J. in Mayor of the Staple v. Bank of England (1887), 21 Q.B.D. 160 (C.A.) at p. 165 and are taken as representing the law in Halsbury's Laws of England (3rd ed.) Vol. 9, pp. 48-49.

whether by overt expression or tacit acquiescence, by a majority, then the foregoing principles governing proof of an *act* of directors will apply equally to proof of their *purpose*; (6) more difficult questions may arise where the only evidence available is of separate and independent indications by the directors of their separate and independent purposes, but if these do not coincide, it is thought that a purpose shared by a majority would be that of the board; (7) if no single purpose were shared by a majority, it could not realistically be said that "the directors" or "the board" had *a* purpose in issuing the shares.

(6) CONSEQUENCES OF AN ISSUE OF SHARES FOR AN IMPROPER PURPOSE

(a) Possibility of corporate ratification; *locus standi* of an individual shareholder to sue; *Foss v. Harbottle.*

The fiduciary duty of directors is owed to the company, not to the individual shareholders.[133] Where directors have exercised a power (e.g. by issuing shares) for an improper purpose they have been treated as having breached their fiduciary duty;[134] they have issued and allotted shares, the issue and allotment being merely voidable at the instance of the company.[135] Since a board's fiduciary duty is owed to the company and not to individual shareholders, the company may elect to waive its right of action and ratify the allotment.[136] For this purpose the company acts in the form of its other constitutional organ, the shareholders, and it is noteworthy that approval in advance or a ratification subsequently by ordinary resolution of shareholders of a board's act is not the same thing as controlling the board in the exercise of its powers.[137]

If it is true as a general proposition to say that an issue of shares for an improper purpose may be ratified by an ordinary resolution of shareholders, one would expect that proceedings by an individual

133 Percival v. Wright [1902] 2 Ch. 421.

134 Richard Brady Franks Ltd v. Price (1937) 58 C.L.R. 112, per Dixon J. at 143; Gower, Modern Company Law, 3rd ed., 520.

135 Bamford v. Bamford [1969] 2 W.L.R. 1107 per Harman L.J. at 1111-1112; Richard Brady Franks Ltd v. Price (1937) 58 C.L.R. 112, per Dixon J. at 142-143.

136 This possibility was mooted as early as 1864 in Fraser v. Whalley (1864) 2 H. & M. 10. It has certainly been authoritatively recognized since: Hogg v. Cramphorn Ltd [1967] Ch. 254 approved of by the Court of Appeal in Bamford v. Bamford [1969] 2 W.L.R. 1107. And cf. North-West Transportation Co v. Beatty (1887) 12 App. Cas. 589 esp. per Baggallay J. at 593; Regal (Hastings) Ltd v. Gulliver [1967] 2 A.C. 134 esp. per Lord Russell of Killowen at 150A.

137 Hogg v. Cramphorn Ltd [1967] 1 Ch. 254, 269-270.

shareholder would be defeated by the rule in *Foss v. Harbottle*[138] and that such proceedings could be brought only by the company.[139] It is a fact however that individual shareholders have brought proceedings for injunctive and/or declaratory relief[140] in some cases without the *Foss v. Harbottle* objection being raised,[141] and in other cases with success in the face of that objection,[142] and this on equitable principles and without reference to the *locus standi* conferred expressly upon any shareholder by the Companies Act.[143]

Why are proceedings by individual shareholders in respect of a board's exercise of a power for an improper purpose excepted from the *Foss v. Harbottle* rule? It is difficult to find a satisfactory answer. An answer which has been tentatively offered is that each member has a personal contractual right to have the memorandum and articles observed[144] and that it is, within this principle, an implied term of the articles that directors' powers will be exercised for proper purposes.

138 (1843) 2 Hare 461.

139 The company was plaintiff in Richard Brady Franks Ltd v. Price (1937) 58 C.L.R. 112.

140 It may be noted that the s. 186 remedy will typically not be available because the issue of shares in question will be an isolated act of oppression rather than an oppressive "conducting" of the company's affairs.

141 Punt v. Symons & Co. Ltd [1903] 2 Ch. 506; Piercy v. S. Mills & Co. [1920] 1 Ch. 77; Harlowe's Nominees, ante cit. (Foss v. Harbottle was adverted to in arguendo at 489); Ashburton Oil N.L. v. Alpha Minerals N.L. (1971) 45 A.L.J.R. 162. And cf. Galloway v. Halle Concerts Society [1915] 2 Ch. 233; Peters American Delicacy Co v. Heath (1939) 61 C.L.R. 457.

142 Hogg v. Cramphorn Ltd [1967] 2 Ch. 254; Bamford v. Bamford [1969] 2 W.L.R. 1107. It should be noted that in the case last cited, Russell L.J. raises the problem posed by Foss v. Harbottle:

> "It is true that the point before us is not an objection to the proceedings on Foss v. Harbottle (1843) 2 Hare 461 grounds. But it seems to me to march in step with the principles that underlie the rule in that case. None of the factors that admit exceptions to that rule appear to exist here. The harm done by the assumed improperly-motivated allotment is a harm done to the company, of which only the company can complain. It would be for the company by ordinary resolution to decide whether or not to proceed against the directors for compensation for misfeasance": ibid. 1115.

143 Uniform Companies Acts, s. 155. Cf. Ngurli Ltd v. McCann (1953) 90 C.L.R. 425, 447.

144 E.g. "The plaintiff is not a representative party and is suing because of its personal right and the dilution of its personal interests": Aicken Q.C., for the plaintiff-appellant in Harlowe's Nominees at p. 486; "A shareholder who would be affected by the exercise of a company's powers is entitled to demand and enforce that the company's power should be exercised lawfully": per Menzies J. in Ashburton Oil N.L. v. Alpha Minerals N.L. (1971) 45 A.L.J.R. 162, at p. 167G and cf. Barwick C.J., ibid., p. 162F; Windeyer J., ibid., pp. 167G-168A.

Thus, it was accepted by three High Court judges in *Ashburton Oil N.L. v. Alpha Minerals N.L.*[145] that although a plaintiff had no equity to seek an injunction restraining a share issue by virtue of its being a *majority* shareholder in the defendant company, yet it did have that equity merely *qua* shareholder. On the other hand this proposition leaves unexplained cases in which *Foss v. Harbottle* has been applied.[146]

Another answer which suggests itself on principle is that the *Foss v. Harbottle* rule applies except where ratification itself would inevitably be a fraud on the minority because "the directors" and the majority shareholders represent the same interest. This was the basis of the formulation in *Ngurli Ltd v. McCann*:[147]

> But even in general meeting a majority of shareholders cannot exercise their votes for the purpose of appropriating to themselves property or advantages which belong to the company for that would be for the majority to oppress the minority. The right to issue new capital is an advantage which belongs to the company. Any attempt by directors or by the company to exercise this right not for the benefit of the company as a whole but so as to benefit the majority to the detriment of the minority could be restrained in a suit brought by the minority against the company and the majority.[148]

And in *Cook v. Deeks*[149] the Privy Council held that a diversion of company property in favour of the directors could not be ratified by a general meeting controlled by the votes of the directors themselves (and it may be observed that unissued shares are property of the company). But apparently not every ratification of the directors' "fraud on a power" will be a fraud by the majority shareholders!

The point at issue was dealt with by Helsham J. in *Provident International Corporation v. International Leasing Corporation.*[150] His Honour was able to point to the several cases where individual shareholders have brought suit and to the terse holding by the High Court in *Ngurli Ltd v. McCann*[151] that "in these circumstances the plaintiffs have a clear right to sue in their own names to remedy the breach of trust."[152] His Honour's own conclusion is as follows:

145 (1971) 45 A.L.J.R. 162.
146 See Gower, Modern Company Law, 3rd ed., pp. 264-265.
147 (1953) 90 C.L.R. 425.
148 Ibid. pp. 447-448.
149 [1916] 1 A.C. 554.
150 (1969) 89 W.N. (Pt. 1) (N.S.W.) 370, 380-382.
151 (1953) 90 C.L.R. 425.
152 Ibid. 447.

> The reason why the rule in *Foss v. Harbottle* does not apply in a case of fraud on a power such as the present no doubt resides in the fiduciary nature of the duty owed *and the fact that it is owed to all the corporators of the company.* A breach of duty owed to an individual shareholder as one of the corporators could not be ratified by a majority of shareholders; any attempt by a majority to ratify a breach of fiduciary duty by directors would be no less a fraud qua that shareholder than was the case in the acts of the directors.[153]

This seems to come full circle. The pasage is based on the premise that the duty to exercise powers only for proper purposes is owed to the shareholders individually.

When one turns to the *statutory* right conferred on *inter alia* any member of the company to apply to the Court for rectification of the share register, one finds a surer basis on which an individual shareholder may mount proceedings. "Any member" may apply to the Court under s. 155. No restrictions of the *Foss v. Harbottle* type apply.[154] "Any person" even includes a person who became a member only after the impugned issue of shares was made—the statutory right is not to be interpreted as a kind of codification of the fiduciary duty at common law: *Provident International Corporation v. International Leasing Corporation.*[155]

(b) Defences to an action

It will be a ground for refusing relief, whether the plaintiff's *locus standi* is regarded as depending on common law or on s. 155, that the plaintiff was guilty of laches after he had become aware of the purpose of the allotment[156] or that he knew and approved of and ratified the board's act.[157]

An allotment will not be set aside where the allottee was innocent of the impropriety of purpose.[158] It seems to have been thought that this principle arises from *Royal British Bank v. Turquand.*[159] It may

153 (1969) 89 W.N. (Pt. 1) (N.S.W.) 370, 381.

154 Per Williams J. (with whom McTiernan and Kitto JJ. agreed) in Grant v. John Grant & Sons Pty Ltd (1950) 82 C.L.R. 1, 31-32.

155 (1969) 89 W.N. (Pt. 1) (N.S.W.) 370.

156 Provident International Corporation v. International Leasing Corporation (1969) 89 W.N. (Pt. 1) (N.S.W.) 370, 375; Harlowe's Nominees at 500.

157 Provident International, loc. cit., Harlowe's Nominees, loc. cit.

158 Cf. the position of those debenture-holders other than the directors in Richard Brady Franks Ltd v. Price (1937) 58 C.L.R. 112; and cf. the allegation in the plaintiff's statement of claim in Harlowe's Nominees that the allottee was aware of the facts said to show that the allotment was for an improper purpose: (1968) 121 C.L.R. 483, 484.

159 (1856) 6 E. & B. 327. Cf. Bamford v. Bamford [1969] 2 W.L.R. 1107 (C.A.).

also be seen as a particular application of two more general legal principles: (1) that a person acquires good title where he innocently and for value acquires legal title to property without knowledge of an outstanding equitable interest;[160] (2) that a person acquires good title where he deals with an agent within his ostensible authority and without knowledge that the agent was exceeding a secret restriction or limitation.

Once it is too late for an allotment to be set aside, again the question "To whom is the board's fiduciary duty owed?" arises, this time for the purpose of determining who may sue the directors. The individual shareholders cannot sue the directors for damages, though the company itself might do so.

CONCLUSION

Whilst the broad nature of and limitations on a board's power to issue shares have been well recognized by the courts, a close examination of the classical formulation of the board's fiduciary duty as it affects this power, discloses a number of questions on which the courts have not passed. Some of these may receive attention in the judgment yet to be given in *Ampol Petroleum Ltd v. R. W. Miller (Holdings) Ltd,* a suit of some significance currently before the Supreme Court of New South Wales.

K. E. LINDGREN*

160 Cf. Harlowe's Nominees, ante cit., 500.

* *Professor of Legal Studies, University of Newcastle.*