No 3.

judgment no. 3 1974

IN THE PRIVY COUNCIL No. 9 of 1973

ON APPEAL

FROM THE SUPREME COURT OF NEW SOUTH WALES
EQUITY DIVISION

BETWEEN

| | |
|---|---|
| HOWARD SMITH LIMITED | Appellant (13th Defendant) |
| - and - | |
| AMPOL PETROLEUM LIMITED | Respondent (Plaintiff) |
| R.W.MILLER (HOLDINGS) LIMITED | (1st Defendant) |
| ARCHIBALD N. TAYLOR | (2nd Defendant) |
| SIR EMIL HERBERT PETER ABELES | (3rd Defendant) |
| ELIZABETH MILLER | (4th Defendant) |
| ROBERT I. NICHOLL | (5th Defendant) |
| EVAN DUFF CAMERON | (6th Defendant) |
| KENNETH B. ANDERSON | (7th Defendant) |
| WILLIAM A. CONWAY | (8th Defendant) |
| PETER J. DUNCAN | (9th Defendant) |
| ALAN V. BALHORN | (10th Defendant) |
| F.M.MURPHY (a male) | (11th Defendant) |
| C.J. WATT (a male) | (12th Defendant) |
| SECURITY SHARE SERVICES PTY. LIMITED | (14th Defendant) Respondents |



CASE FOR THE APPELLANT

SUMMARY OF CASE

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## A. THE NATURE OF THE DISPUTE

### I. The Cause of the Litigation.

1. This action was brought by one of two contending parties in a takeover struggle to challenge the validity of an allotment of shares made by the directors of a public company, in unusual and possibly unique circumstances, to the other contender.

2. The challenger was Ampol Petroleum Limited (hereinafter called "Ampol"). The shares in question were shares in R.W.Miller (Holdings) Limited (hereinafter called "Millers"). The Company to which the shares were allotted was Howard Smith Limited (hereinafter called "Howard Smith").

3. The circumstances in which the allotment was made may be briefly summarised as follows :

(a) All three companies named above were large public companies whose shares were listed on Australian Stock Exchanges. Millers and Howard Smith were, inter alia, owners of oil tankers and not otherwise involved in the oil industry. Ampol was an oil company which was a substantial user of tankers.

(b) For various reasons Millers was generally regarded in the market as a prime target for a takeover, and it was inevitable that it would shortly be taken over.

(c) Ampol having acquired by private treaty almost 29% of Millers'

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issued capital made a takeover offer. The offer was regarded as inadequate by all Millers' directors.

(d) Howard Smith made a substantially higher offer.

(e) Ampol and another large Millers' shareholder named Bulkships Limited (hereinafter called "Bulkships") combined to thwart the higher offer by announcing that they would in future act jointly to control the conduct of Millers' affairs and would not accept the Howard Smith offer. The clear purpose of their announcement was to force Howard Smith out of the bedding and to force the other shareholders to accept the original Ampol offer.

p.1268

(f) The majority of the Millers' directors honestly believed that Ampol and Bulkships had plans for Millers which were inimical to its interests as a commercial entity and contrary to the interests of the other shareholders.

(g) Millers was notoriously and substantially under-capitalised.

(h) The majority directors of Millers, without regard to their own personal position or interests, and acting honestly on legal advice, believed they had power to make a large share issue to Howard Smith and they resolved to do so. They would not have been prepared to do so had they not believed that by doing so they were obtaining much-needed capital for the company.

(i) The motives of the directors in making the allotment were mixed. They desired to get a fair deal for the company's shareholders in the takeover situation, and to protect the company and the shareholders from what they saw as the

designs of Ampol and Bulkships. They also saw the opportunity of making the allotment at a premium that would otherwise be unobtainable as one that should not be let pass, and they believed that in making the allotment they were serving a serious need of the company. They believed on legal advice that the capital need in question justified the allotment.

4. The allotment was made by a resolution of the Millers' board passed on the 6th July 1972. It was of 4,500,000 shares of $1.00 each at a premium of $1.30 per share. p.1295 l.39 to p.1303 l.20

II. Proceedings

5. By proceedings commenced in the Equity Division of the Supreme Court of New South Wales on the 7th July 1972 Ampol challenged the validity of the allotment to Howard Smith and sought an Order for rectification of the register by removal therefrom of the name of Howard Smith as a member of Millers in respect of all of the said 4,500,000 shares. p.9

6. The defendants to the proceedings were Millers (which was the first defendant), Howard Smith (which was the thirteenth defendant), all the persons who were the directors, or alternate directors, of Millers at the time of the allotment, and Millers' Share Registrar.

7. Millers instituted a cross-claim against Bulkships, which was not a party to the original action. The cross-claim was ultimately dismissed and is not the subject of this Appeal. Brief reference to the nature of the cross-claim will, however, be made below.

8. The action came on for hearing before His Honour Mr. Justice Street, the

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Chief Judge in Equity, on the 5th September 1972. The hearing lasted 28 days. His Honour gave judgment
p.1126 on the 14th December 1972, in favour of the plaintiff.

9. His Honour declared that the purported allotment and issue of the 4,500,000 shares in the capital of Millers to
p.1195 Howard Smith was invalid, that the name of Howard Smith had been without sufficient cause entered into the
p.1195 Register of Members of Millers as a member of that Company in respect of the said shares, and ordered
p.1196 rectification of the register as claimed and made appropriate consequential orders.

10. Conditional leave to appeal against the above judgment declarations and orders was granted by the Supreme Court of
p.1200 New South Wales on the 20th December 1972, and final leave to appeal was
p.1204 granted on the 16th day of March 1973.

## B. THE BACKGROUND FACTS

11. The background facts and those immediately relating to the disputed allotment appear from the oral and documentary evidence tendered at the hearing before Street J. Most, though not all, of the material facts are
p.1126 set out in the written judgment of Street J. A summary of the material facts is set out below.

### I. General

(See separate Exhibit "A")

12. Millers was incorporated in 1962. It is a public company, and its shares were at all material times up to the 6th July 1972 listed on the Sydney Stock Exchange and other Australian Stock Exchanges. Although incorporated in the Australian Capital Territory its principal office and the centre of its administration has always been in Sydney.

13. The business of Millers falls broadly

into three categories - it owns a number of hotels, it has coal mining interests and it is a ship-owner.

14. From the incorporation of Millers until his death on 26th April 1971 Sir Roderick Miller was Chairman of Directors and Managing Director. He had wide power in conduct of the day to day affairs of the Company and had the complete confidence of the Board. His dominant position was material to the financial position in which the Company found itself in 1972 as appears from paragraph 29 below.

15. At the time of his death Sir Roderick Miller controlled through a family company named Romanda Pty. Limited, 29.8% of the issued shares in the capital of Millers. His Honour said :

> "The prospect of this large shareholding becoming available for purchase on the market, and the inevitable change in the management of Millers consequent upon the removal of Sir Roderick Miller's hand from the helm, overshadowed the future with a cloud of uncertainty. Millers' financial position became a subject of comparatively wide-spread interest in commercial circles, and it was not long before there began to be talk of the possibility of a takeover offer being made in respect of its shares."

p.1128 L1.19-29

Although his Honour does not refer to it it was common knowledge in the market place that Millers was seriously undercapitalised, and was facing recurring crises of liquidity principally owing to the fact that it had been committed to the construction of two large tankers in respect of which it had not obtained

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long term finance.

II. Composition of Millers' Board.

16. (a) On the 6th July 1972 the Directors of Millers were Mr. A.N. Taylor (Chairman), Lady Miller, Sir Peter Abeles, and Messrs. R.I. Nicholl, Duncan, Anderson and Cameron.

16. (b) Mr. Taylor, who was Managing Director of Millers, was the only director who was also an executive of the Company. He had been in the employment of firms or companies controlled by the late Sir Roderick Miller since 1954. He ultimately held the position of a personal assistant to the late Sir Roderick Miller, and on his death became one of the joint Managing Directors, and ultimately the sole Managing Director.

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16. (c) Lady Miller (as she was in July 1972) was the widow of the late Sir Roderick Miller.

16. (d) Sir Peter Abeles had been appointed to the Board in 1971 following the acquisition by Bulkships of a substantial parcel of shares in Millers which had been held by a company named Thomas Nationwide Transport Limited, of which he was also a director. He was also at all material times a director of Bulkships and he had, it appeared from the evidence, a long standing commercial association with Ampol or its Chairman of Directors.

p.1756 l.17

16. (e) Mr. R.I. Nicholl is a Sydney Solicitor practising, in partnership, inter alia, with his father Mr. R.W. Nicholl who was also a witness in the case. He gave evidence that he had originally gone on to the Board of Millers (in August 1968) at the request

p.789

of his father and the late Sir Roderick Miller, and that he did not have wide experience as a company director.

16. (f) Mr. Duncan did not attend the critical Board Meeting, being in Japan at the time, and the meeting was in fact attended by his alternate director, Mr. Balhorn. Mr. Balhorn voted in favour of the allotment, but His Honour found as a fact that Mr. Duncan also approved of it.

16. (g) Mr. Anderson is a retired employee of Millers, who had been a joint Managing Director for a time after the death of Sir Roderick Miller. p.442 and p.1003

16. (h) Mr. Cameron is a member of a Sydney firm of Chartered Accountants, and he had been appointed to the Board of Millers during 1971, after the death of Sir Roderick Miller, apparently by reason of his financial expertise. He became a member of the Finance Committee appointed by the directors shortly after Sir Roderick Miller's death. p.44 l.28

III. The Takeover Struggle

17. By early 1972 it was obvious to all concerned that Millers was going to be taken over by some other public company. The only real question was when and by whom it would be taken over.

18. Between January and May 1972 negotiations for the acquisition of the Romanda shares in Millers took place, and some further reference to these will be made below in the context of the relationship between Ampol and Bulkships. On 22nd May 1972 Ampol acquired the Romanda shares for $2.27 per share, and on the same day

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p.1218

announced an intention to make a take-over offer in respect of the remaining shares in the capital of Millers at the same price.

19. At the time Ampol made its offer it held 2,681,641 shares (29.8% of the issued capital) in Millers, and Bulkships held 2,257,100 shares (25.1% of the issued capital), making a total combined shareholding of 54.9%. On 15th June 1972 a formal takeover offer was made by Ampol.

p.1243

p.1257

20. On the 23rd June 1972 the Millers Board met and considered the Ampol offer. All Millers directors (including Sir Peter Abeles) considered it too low and the board decided to recommend to the shareholders rejection of the offer.

21. Meanwhile discussions were going on between Howard Smith and what has been described as "the Management team" of Millers. "The Management team" included Mr. Conway, the legal officer of Millers, who was highly praised by Street J. as a person of undoubted integrity, and Mr. Koch, the General Manager of Millers. The only member of "the Management team" who was also a Director of Millers was Mr. Taylor, There is no suggestion that any of the other directors of Millers were aware of the discussions until, at the most, a day or so before the meeting of the 6th July 1972.

p.1147 l.22

p.1290

22. On the 16th June 1972, Directors and Executives of Howard Smith approached the Millers Management team on the basis that Howard Smith would be interested in making an offer to acquire the two tankers ("Amanda Miller" and "Robert Miller") which were currently under construction for Millers.

23. Ampol, Bulkships and Howard Smith all had an interest in the Millers

tankers, for they were all involved in shipping activities including the operation of tankers on the Australian coast. One of the bases upon which Howard Smith initially suggested that the tankers should be sold to it was that it would be "a travesty", in the light of the history of Sir Roderick Miller's activities, if the tankers fell under the control of an oil company rather than an independent operator such as Howard Smith.

24. Discussions as to the possible acquisition of the Millers' tankers by Howard Smith were fruitless, but in the course of the meetings the Millers' Management team suggested to Howard Smith that it might make a competing takeover offer for "the whole shooting box". Howard Smith initially indicated considerable reluctance to do this, pointing out that Ampol and Bulkships between them held more than 50% of the company's issued capital already. The question whether those two companies were acting in combination was discussed, and it was suggested by Mr. Conway to the Howard Smith directors at that stage that he did not believe they were.

25. Ultimately, on the 22nd June 1972, Howard Smith announced its intention to make a takeover offer in competition with the Ampol offer, and at a price of $2.50 per share (or an alternative offer of shares in Howard Smith, with cash, worth on that date $2.76 per Miller share). On the 18th July 1972 it delivered to Millers the statement required by Part A of the Tenth Schedule to the Companies Ordinance 1962 and on the 17th August 1972 it despatched offers to the shareholders of Millers. The offers were to remain open until the 17th November 1972 but the closing date was subsequently extended to 19th December 1972. p.1255

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## IV. Millers' Financial Position.

26. To facilitate an understanding of the relevant events it is necessary to summarise the evidence as to Millers' financial position, and more particularly the understanding which each of the directors had of that situation. Although the learned Judge set out to form his own
p.1167 opinion as to the true financial situation, it is the Appellant's submission that to embark upon such a task was a fundamental error in His Honour's reasoning. The critical question was what was the understanding of each of the directors as to that financial situation, even if one must limit it, as for present purposes the Appellant is content to limit it, to their honest belief based upon reasonable grounds and information furnished to them by responsible officers of the company, and reasonably believed, as to the company's position. The Appellant will submit that in the end no director is properly to be expected to do more than base his judgment on such information, nor can he properly do less. The evidence relating to Millers' financial situation as known to the directors is summarised below.

27. A great deal of evidence about the financial position of Millers in June 1972 was given and a great deal of time at the hearing was devoted to an examination of such evidence and submissions thereon by both Ampol and Millers. In the end the conclusion which Street J. reached was substantially as submitted by Millers rather than as submitted by Ampol. The Appellant is not concerned to challenge His Honour's findings as to the financial position of Millers but submits that his views as to what was an appropriate business course to adopt are irrelevant. In addition, it is necessary to draw attention

from time to time to certain aspects of the evidence to which His Honour does not refer in his judgment. It is convenient to quote here what His Honour said about Millers' financial position.

28. His Honour said:

"A tremendous amount of detailed evidence was directed to establishing that Millers was, as at 6th July 1972, in a financially straitened position... p.1167 l.22 to p.1168 l.35

It is clear on the evidence that Millers was, as at 6th July 1972, in a position of tight liquidity. It did not have within its own funds sufficient money to cover its present and foreseeable financial commitments. It had, however, been in a position of tight liquidity for many months before 6th July 1972. There is a history of a series of financial crises; but at the same time there is a trend of improvement during the months preceding the meeting of 6th July.

The primary cause of the position of tight liquidity was the capital commitment involved in the construction of the two 66,000 ton tankers. The construction of the first of these tankers had almost been completed during the lifetime of the late Sir Roderick Miller, and the construction of the second had been commenced shortly after his death. The planning of the tankers had been essentially the province of Sir Roderick Miller. He had followed during his lifetime a policy of not issuing shares to cover the construction costs. He had preferred to cover the construction costs by loans....

> I have no hesitation in finding that as at 6th July 1972 Millers did have a capital need, and, indeed, a capital need of no mean order. This capital need had, however, existed for some time past. Millers' policy in Sir Roderick Miller's lifetime had been to meet such capital need from borrowings rather than from an issue of shares."

29. The Appellant submits that -

> His Honour's findings of fact overlook one important additional factor which was established by the evidence but which His Honour did not mention in his reasons for judgment, and which was no doubt well known to the directors on the 6th July 1972. It appeared from the evidence of Mr. R.I. Nicholl, whose firm had acted as Sir Roderick's solicitors for many years, that the reason why, during Sir Roderick's lifetime, a "policy" had been pursued of not raising finance for the tankers by the issue of share capital was not that anyone considered that such a policy was an objectively desirable one, but that Sir Roderick Miller was himself in a fairly tight financial situation and could not have afforded to take up in his family company or otherwise sufficient shares to maintain his position of voting strength in the company.

30. Further, not only was Millers under-capitalised, but that fact was obvious and widely known, and had been the subject of comment, for example, by Millers' bankers on previous occasions.

31. His Honour went on, dealing with the matter of liquidity:

p.1169 Ll.1-4 "It is clear that the alarms and

strains of such a policy were constantly before, and well known to, and understood by, the directors. These strains were still very much present on 6th July 1972."

32. As illustrations of the sort of matter to which His Honour was referring it might be mentioned that during 1971 Millers had been served with a formal notice of demand, failure to comply with which is prima facie evidence of insolvency. Further, Millers was subject to frequent threats of legal proceedings by the Commonwealth Government in respect of moneys owing for progress payments on the tankers that were being constructed. These tankers, the "Amanda Miller" and the "Robert Miller" were being constructed under subsidy arrangements which were common in Australia. Under these arrangements a Commonwealth authority places an order for the building of a vessel and sells it for less than cost to the ultimate owner. The owner, however, is responsible to put the Commonwealth in funds to meet progress payments to the shipbuilder. As recently as the 30th June 1972, efforts of some desperation had to be made to enable the Company to meet a substantial commitment to that Authority on that date.

p.1765 Ll.32-47
p.1766 l.6
p.1767 l.5-11
p.1769 Ll.26-31
p.1779 l.32 to
p.1780 l.1-10

33. On this matter, His Honour said:

"In short, I am satisfied that as at 6th July 1972 there was a need for capital. I am satisfied that this need had been recognised for many months past and that a policy had been followed of meeting it by loan capital rather than by share capital. I am satisfied that progress was being made in meeting this

p.1172 Ll.11-21

need by this policy. I am not satisfied that the company's financial affairs were at crisis point due to unavailability of capital, or that there was a pressing need to obtain cash funds by a share issue".

34. The Appellant submits that -

p.1171 l.38

His Honour's suggestion that there had been some deliberate or conscious "policy" of raising loan capital rather than share capital was unfounded and contrary to the evidence. So far as the situation during the lifetime of Sir Roderick Miller is concerned, that has been dealt with above.

So far as the situation after the death of Sir Roderick Miller is concerned, the evidence was all one way. There was no reasonable prospect of obtaining any substantial amount of share capital. The matter had been considered from time to time but it appears to have been rejected almost out of hand. The reason was simple. During 1971, and up until a takeover battle became imminent, the price at which the Company's shares were quoted on the Stock Exchange was such that it was out of the question to hope to make any substantial placement of shares at a worth while premium. There was no evidence to support any finding of a conscious and deliberate preference, on the part of the Millers' Board, for loan capital. On the contrary, the evidence was that Millers' financial advisers had not regarded the making of a share issue as being a real possibility.

V. The Ampol-Bulkships Combination.

35. His Honour said :

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"The negotiations leading up to the acquisition by Ampol of its holding of 2,681,641 shares originated in the early part of 1972 and continued until May. The course of these negotiations and some concurrent negotiations initiated by Sir Peter Abeles, were investigated in evidence and were the subject of submissions in argument. There is insufficient material upon which to base any finding of concerted activity, such as is alleged by Millers. I am not satisfied that, in the negotiations culminating in Ampol purchasing these 2,681,641 shares, there was any collaboration between Ampol and Sir Peter Abeles for Bulkships. There are straws in the wind that suggest there may, during the course of the negotiations, have been some exchange of confidences between Ampol and Bulkships concerning the future of Millers. But these fall short of providing a basis upon which I am prepared to make any affirmative finding. I state this view after giving full weight to the reliance placed by Counsel for Millers upon the scintilla doctrine and the inferences it is entitled to have drawn in its favour by reason of the failure of Ampol and Bulkships to call evidence from any of their officers." p.1134 Ll.18-41

36. What His Honour referred to as "straws in the wind" and "scintilla" were the following facts :

(a) During January 1972 Ampol made an offer to acquire the Romanda shares for $2.11 per share. The persons who were dealing on behalf of Romanda in the matter were, principally, Mr. R.W. Nicholl (father of Mr. R.I.

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Nicholl), Mr. A.N. Taylor and Lady Miller. Messrs. Taylor and Nicholl were directors of Romanda. Mr. Nicholl was one of the Executors of the Will of the late Sir Roderick Miller and Lady Miller was a principal beneficiary.

(b) Subsequently Sir Peter Abeles on behalf of Bulkships offered $2.40 per share for the Romanda shares.

(c) Negotiations went on until early May when, on the one day, Sir Peter Abeles withdrew the Bulkships offer of $2.40 per share, and the Ampol offer was increased to $2.27 per share. That offer was subsequently accepted.

p.1705 (d) Over this period, or at about this time, Ampol's Solicitors prepared a document (which was never in fact executed) which provided in substance for the joint acquisition of Millers by Ampol and Bulkships and for the spreading or division of the assets of that company between Ampol and Bulkships along certain lines.

p.1220 (e) In May Ampol made its takeover offer for the company, and in June, in response to the competing Howard Smith offer,

p.1268 Ampol and Bulkships issued the "joint announcement" referred to below, in which they announced their intention to act jointly in relation to the future operation of Millers.

37. Referring to the attitude with which the directors of Millers viewed the acquisition by Ampol of the Romanda shares, and the activities of Ampol and Bulkships, His Honour said, in relation to a time which was about the middle of May 1972 :

"There was evident, even at this early stage, an attitude in the Millers' Boardroom which pervaded with increasing intensity, the whole of the subsequent events. This was an attitude of concern, even apprehension, as to the intentions of Ampol and Bulkships regarding Millers - an attitude which tended to identify Millers and the best interests of Millers with the 'minority shareholders' and the best interests of the 'minority shareholders'. It grew out of the suspicion of the directors that Ampol and Bulkships were acting in concert, and a fear that such concerted action would be detrimental to Millers. The Directors, at this board meeting, perceived what they regarded as the prospect in the future of Ampol and Bulkships versus the rest. As the narrative will disclose, this prospect had crystallised in their minds to an established fact by the time of the board meeting of 6th July." p.1135 l.31 to p.1136 l.3

38. The matters to which His Honour was referring in the above passage may briefly be summarised as follows :

(a) The fear which was developing in the mind of the Millers' directors was that there existed between Ampol and Bulkships a combination the ultimate purpose of which was to take over the company and, in a winding up or otherwise, dismember it by dividing its assets up between them or selling them.

(b) The apprehension on the part of the directors did not (as His Honour specifically found) relate to any personal desire on their part to retain their position on the Board. On the other hand, the directors regarded what they suspected, and ultimately believed, to be the intentions of Ampol and Bulkships,

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as being inimical both to the interests of Millers as a corporate entity, and to the interests of all the shareholders in Millers except Ampol and Bulkships.

(c) On the 5th June 1972 Sir Peter Abeles in a conversation with Taylor foreshadowed a joint Ampol-Bulkships takeover, dismemberment of the Millers organisation and staff redundancy at a senior level (although Taylor's own position was said to be secure).

p.459 Ll.10 to 22

p.459

(d) Over the period there developed on the part of Sir Peter Abeles an attitude of increasing truculence evidenced by his request to Taylor some time between the 23rd and 27th June 1972 that he obtain the resignations of three of the directors and by his threats on 5th July 1972 to force the resignation of other directors and "to blow the place wide open".

p.466 Ll.16-21

p.472 Ll.42-43

39. It is submitted that -

In the ultimate assessment of the bona fides of the Millers' Directors, which is the matter upon which this litigation ultimately turns, what is relevant is not His Honour's finding as an objective fact that, from the point of view of legal evidence there is no justification for a Court to conclude that there was a combination on the part of Ampol and Bulkships during May 1972, but, rather, His Honour's finding of fact that the Directors genuinely believed there was such a combination and, further, that they believed that it was a combination for a purpose harmful to the interests of Millers as a corporate entity and

harmful to all the other shareholders of Millers.

VI. The Ampol-Bulkships Joint Announcement. p.1268

40. The reaction of Ampol to news of the Howard Smith offer was not to increase its own offer. On the contrary, it joined with Bulkships, on the 27th June 1972, in the publication of the following press statement, which emerged as a statement from the Chairman of Ampol and the Chairman of Bulkships (Sir Ian Potter) :

> "Following discussions that took place today, agreement has been reached for the two companies to act jointly in relation to the future operation of R.W. Miller (Holdings) Limited. Accordingly, they have decided to reject any offer for their shares whether from Howard Smith Limited or from any other source. Ampol Petroleum and Bulkships Limited, between them, control in excess of 55% of the issued shares of R.W. Miller (Holdings) Limited." p.1268

41. It is submitted that the following features of that "joint announcement" are noteworthy:

(a) The agreement that is referred to goes beyond a mere agreement to act jointly in relation to the takeover battle. The statement records an agreement to act jointly in relation to "the future operation of" Millers.

(b) One of the obvious purposes of the statement is to warn Howard Smith off the course. What the makers of the statement are plainly telling Howard Smith is that it can never hope to become anything other than a minority shareholder in Millers, no matter how much it is prepared to offer for Millers' shares.

Further, Howard Smith is being told that there is in existence a combination or agreement between the two majority shareholders as to the manner in which the future business of Millers will be conducted.

(c) Finally, the shareholders in Millers are being put on notice of the fact that they might as well accept the Ampol offer (which, incidentally, is viewed by all the directors of Millers including Sir Peter Abeles as too low) (see paragraph 3(c)) otherwise they will be "locked in".

p.1306 l.20 to p.1307 l.6

VII. Howard Smith's Application for the Allotment.

42. In considering the following course of events it is important to distinguish between the activities of the Millers' "Management team" on the one hand, and the knowledge and conduct of the Millers' directors (none of whom, with the exception of Mr. Taylor, was engaged in management) on the other.

43. The Millers' Management team was plainly anxious to encourage and promote the success of the Howard Smith offer, but there was obviously grave doubt that the offer could or would go forward in the light of the Ampol-Bulkships joint announcement.

44. On the 4th July there occurred a meeting between the Millers' Management team and directors and executives of Howard Smith in the course of which various possibilities were discussed. One possibility that was suggested by Howard Smith was that it might be allotted 3,000,000 shares in the capital of Millers at $2.00 per share on certain terms and conditions, but this suggestion was

rejected by the Millers' representatives on the ground that the offer was too low.

45. Later on the 4th July Mr. Walker, a member of the Millers' Finance Committee, spoke to Mr. Conway. It was of Mr. Conway that His Honour said :

> "He was a witness whose honesty, and the reliability of whose evidence, was plainly to be seen." p.1138 l.34

Mr. Conway described the conversation in the following manner :

> "He gave me some facts and figures as to Millers' financial position and pointed out to me that from a short term liability point of view the Company was urgently in need of cash and so far as I can recall I said: 'Well, surely, in a situation like this, there is some justification for issuing shares'." p.712 Ll.40-44

46. The events of the 5th July, leading up to the proposal for allotment, are described at length in His Honour's judgment, and the evidence as to them was not the subject of any significant dispute. They may be summarised briefly as follows : p.1145 l.38 to p.1148 l.40

(a) On the morning of the 5th July the Millers "Management team" met with Mr. Aston, a Solicitor who was advising the Company on the takeover situation. p.1145 to p.1148

(b) Messrs. Aston and Conway advised those present that an allotment of shares to Howard Smith would be justified if it were such that it would raise the amount which would be "necessary to safeguard the Company's financial position as it stood at that time".

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p.1146 l.18

(c) On that basis it was calculated that at a price of $2.30 per share it would be necessary to issue 4,152,000 shares in order to produce $9½m., being the amount required to safeguard the Company's financial position.

(d) A proposal on this basis was put by Mr. Conway to Mr. Maxwell of Howard Smith.

(e) During the day, while the matter was being discussed at Millers, Mr. Nicholl arrived with certain reported decisions of the High Court of Australia, which he discussed with those present. The three lawyers present agreed, and informed the others, "that it was quite legal for a company to make a placement of shares in a situation where the money was immediately required to meet the company's financial requirement."

p.1147 Ll.29-33

(f) During the afternoon Mr. Maxwell told Mr. Conway Howard Smith proposed to make an offer for 4,500,000 shares at $2.30 per share and later be brought around a form of a letter to that effect which Howard Smith proposed to deliver to Millers' Board the next day. Messrs. Conway and Maxwell discussed the form of the letter and Mr. Conway suggested one alteration.

p.1147 l.48 to p.1148 l.11

(g) That evening Mr. Conway told Mr. Balhorn of the Howard Smith proposal in general terms. No intimation was given to Sir Peter Abeles, Mr. Cameron or Lady Miller, of the proposal. None of Messrs. Balhorn, Nicholl and Anderson knew of the actual details of the Howard Smith offer nor was any of them aware that Sir Peter Abeles, Mr. Cameron and Lady Miller had no knowledge of it at all.

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## VIII. The Meeting of 6th July 1972

47. The meeting was attended by Mr. Taylor (Chairman), Lady Miller, Sir Peter Abeles, Mr. R.I. Nicholl, Mr. Balhorn (as alternate for Mr. Duncan), and Messrs. Anderson and Cameron. p.1290

48. Also present were :

(a) Mr. Conway, the legal officer of Millers.

(b) Mr. Aston, a Sydney Solicitor who had been retained by Millers to advise the Board.

(c) Mr. Koch, the General Manager of Millers.

(d) Other persons who attended the meeting in a secretarial capacity.

49. It is important to put the part played by Messrs. Conway, Aston and Koch into proper perspective. Each of those gentlemen played an important role at the Directors' Meeting of the 6th July 1972. Each of them emerged as a powerful advocate of the proposed allotment. None of them, however, was a director, nor is the motivation of any of them legally relevant. What is of vital importance, however, is the effect of their advocacy upon the minds of the various directors and, in particular, the non-executive directors.

50. As soon as the meeting commenced, the Chairman announced that an application had been made by Howard Smith for an allotment of 4,500,000 shares in the Company at a premium of $1.30 per share, upon certain terms and conditions contained in a document which was before the meeting. The proposal was discussed at length, and details of the discussion will be considered below. One particular matter which gave rise to dispute at the meeting was that the Chairman

limited discussion at the meeting by Sir Peter Abeles, and ultimately refused him the right to vote. This was done on the ground of an alleged conflict of duty and interest, Sir Peter Abeles having first refused an invitation to disqualify himself.

51. Ultimately the question of the proposed allotment was put to the vote, and the Chairman, and Messrs. Nicholl, Balhorn and Anderson voted in favour of the resolution.

52. Mr. Cameron and Lady Miller voted against the resolution.

p.70 l.41
p.95 Ll.13-17
p.95 l.22

53. Mr. Cameron said in evidence that he voted against the resolution because he did not think the capital to be raised by the allotment was really needed by the Company, and he did not consider that he had been given adequate time to consider the proposal. He said, however, that his views on the matter were not very firm, that he did not impugn the honesty of the other directors, and that he conceded that the other directors could honestly and fairly have come to the decision which they ultimately did reach. He also said that he believed the meeting had been given proper guidance by the lawyers who attended it as to the standards which the directors ought to apply to the question before them.

54. Lady Miller did not give evidence at the hearing. It appeared from the records of the meeting, however, that the reasons which she advanced for voting against the proposed allotment were that it would result in the suspension of the listing which the shares held on the Stock Exchange, and that she did not think she had been given adequate time to consider the proposal. Lady Miller was represented by Counsel at the hearing, and in the course of his address Counsel was asked by His

Honour to state his client's attitude towards the main issue in the case, that is, the validity of the allotment. Lady Miller's Counsel, in response to His Honour's request, said

> "We ... join the controversy to support the submissions put on behalf of the majority of the Board. We dispute the contention that the Board of Directors acted otherwise than bona fide."

## C. REASONS FOR THE MAKING OF THE ALLOTMENT

### I. The Reasons put by Howard Smith to the Millers Board

55. Howard Smith's application for the allotment was in fact made by a letter dated the 6th July 1972. His Honour attached great importance to the terms of that letter. The letter gives two reasons which, according to Howard Smith, might be regarded by the Millers' Directors as good reasons why they should make the allotment. Those two reasons are expressed in a letter as follows : p.1273

(a) "This combination by the two largest shareholders of your Company would in the present circumstances effectively deprive the very large number of minority shareholders of R.W. Miller (Holdings) Limited of the opportunity of securing a substantially higher price for their shares. My Board would be most reluctant to proceed with a bid which, even if every shareholder other than Ampol or Bulkships accepted, could only result in Howard Smith Limited being the largest individual shareholder in a company the future operations of which would be controlled by a combination of two smaller shareholders. p.1274 Ll.1-25 and p.1275 Ll.32-40

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We believe that your Board is conscious of the injustice being suffered by your smaller shareholders and we submit for your consideration a proposal which, if it meets with the approval of your Board, would enable Howard Smith Limited to proceed with its intended offer thereby restoring to your minority shareholders the right to sell their shares to the highest bidder, and would give Ampol Petroleum Limited and Bulkships Limited a similar opportunity."

(b) "Notwithstanding the current circumstances I believe that the opportunity of placing such a large parcel of shares at a substantial premium is likely to be of considerable benefit to your Company. The infusion of $10,350,000 cash is likely to ease the financing problems your Company has faced in recent years, and enable you to rearrange your borrowings with the prospect of interest savings."

56. Much was made by the Plaintiff, and by His Honour, of the priority and relative degrees of emphasis said to be given to the above two considerations.

II. The Reasons Advanced by the Millers' Management Team to the Board

57. At the Board Meeting the members of the Millers' Management team assumed the role of advocates of the allotment.

p.1290 58. Mr. Koch, the General Manager, expounded at length the Company's difficult financial position, and its need for capital. In a lengthy and reasoned argument he put figures to the Board which demonstrated that the Company had short term financial commitments of the order of $10 million and he commended the allotment

to the Directors on the specific ground that the Company could ill-afford to pass up the opportunity of such a large infusion of share capital.

59. During the course of the hearing Senior Counsel for Ampol made a sustained attack upon the validity of the reasoning put forward by Mr. Koch in his address to the Board, and the accuracy of the figures contained in it. What is of significance, however, is that whilst a great deal of time at the hearing of the action was occupied by criticism of Mr. Koch's argument, there was practically no criticism of it at the Board Meeting. In particular, Mr. Cameron, who was the acknowledged financial expert on the Company's Board, a member of its Finance Committee and one of the directors who voted against the resolution, did not criticise Mr. Koch's proposition or correct anything he had to say, and His Honour made no finding of fact to the effect that any of the Directors doubted the accuracy of Mr. Koch's figures or the legitimacy of his process of reasoning. Indeed, it is a significant indication of His Honour's approach to the case that he took great pains to reach his own conclusion as to Millers need for capital, but failed to advert to the effect upon the Directors' minds of Mr. Koch's speech at the Board meeting. His Honour's view as to the correctness of Mr. Koch's report is irrelevant. What is significant is the weight attached to it by the other Directors.

60. The position, then, is that the allotment was powerfully advocated on financial grounds at the Board Meeting by the Company's General Manager, and it appears from the evidence that the Directors who voted for the resolution

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accepted his arguments at face value. Messrs. Conway and Aston, who were respectively the Company's legal officer and an independant legal consultant, dealt with the following matters :

(a) They told the Directors that they were obliged by law to exercise their powers bona fide for the benefit of the Company and for the shareholders as a whole and that they could not justify the exercise of their powers for the benefit of themselves or some only of the shareholders.

(b) They dealt with a matter which was of considerable concern to some of the Directors, that is to say, the fact that the allotment would be in breach of the rules of the Sydney Stock Exchange and could result in "de-listing" or, more accurately, "suspension". They recognised this as a real possibility, but said that it would not inevitably follow. One point which Mr. Conway made in relation to the matter of "de-listing" was that it was inevitable that in the near future the Company was going to be de-listed anyway. (No doubt he said this because once a takeover occurred there would be insufficient spread of shareholding for the Company to retain listing).

61. One particular matter which was stressed by His Honour was the use, particularly by the Millers' Management team, of expressions such as "justify" and "fortify" in relation to the allotment and the relevance of the Company's financial position. The view apparently taken by His Honour, was that the way the matter was put was that for reasons related to the exigencies of the take-over

struggle the persons concerned dearly wanted an excuse to make an allotment in favour of Howard Smith, and found it in the Company's well known and obvious need for funds. There is, undoubtedly, strong support for this way of looking at the matter. There is, however, another way of looking at it, and it can be best seen through the eyes of Mr. Conway. Mr. Conway was a lawyer, and a person of honesty and absolute integrity. He had no axe to grind.

62. Mr. Conway was indignant about the joint announcement, and saw the Ampol-Bulkships combination as inimical to the interests both of Millers as a legal entity and of all the shareholders in Millers with the exception of Ampol and Bulkships. He wanted the Howard Smith takeover offer to go forward so that the shareholders who were otherwise "locked in" would have an opportunity of selling out at a higher price than that which was being forced on them by Ampol and Bulkships. He was also aware of Millers' financial problems and its need for capital, a need which there had been no opportunity of fulfilling in the past. He saw the proposed allotment as serving the double purpose of fulfilling the Company's need for capital and enabling the Howard Smith takeover offer to proceed, with all the consequences that entailed. In that sense he regarded the Company's financial needs as providing a "justification" for the making of an issue of shares which, for a variety of reasons, he personally wanted the Company to make. There is nothing dishonest or improper about that, although there may be problems involved in assigning to him, within some formulations of the law on this subject, a "motive" or a "purpose" or "object". p.1268

III. <u>The Reasons Advanced by the Majority Directors for their Decision</u>.

63. It emerged clearly at the hearing,

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P.1290

and indeed was obvious enough from the records of the meeting of the 6th July 1972 and the surrounding circumstances, that the Directors who voted in favour of the resolution were moved by a variety or mixture of considerations, rather than by one single consideration. Leaving aside for the moment arguments about the difference, if any, between "motive" and "purpose" such as were advanced for the plaintiff at the hearing, and accepted by His Honour, so much was common ground.

64. As the context was waged at the hearing, between Ampol and Millers, the Directors were examined and cross-examined at length in a search for what was, in terms of the existing case law on the subject of the exercise of directors' power, "the primary purpose of the allotment". The Directors said, in a variety of ways, and with varying degrees of emphasis, and conviction, that their primary purpose in voting in favour of the allotment was to raise money for the Company and thereby satisfy its need for capital.

65. Certain passages, although not necessarily entirely representative passages, from the Directors' evidence in this regard are quoted by His Honour in his Reasons for Judgment.

D. THE MAIN ISSUE AT THE TRIAL

66. The main issue at the trial was raised by Ampol's challenge to the allotment on the ground that the Directors who voted in favour of the allotment were not acting bona fide for the benefit of the Company as a whole, and that therefore the allotment, having been made for an ulterior and improper purpose, was invalid.

67. Subsidiary challenges to the validity

of the allotment were also made on the following grounds :

(a) It was alleged that Mr.Balhorn, who was Mr. Duncan's alternate director, failed to exercise any independent discretion or judgment in the matter and acted merely as a cipher for Mr. Duncan. Accordingly, so it was claimed, his vote was ineffective and the proceedings of the meeting were vitiated. His Honour rejected this allegation as a matter of fact. p.1154 Ll.3-4

(b) There was also a claim that the proceedings of the meeting were vitiated by the wrongful exclusion of Sir Peter Abeles from full participation in the discussion, and from voting. It was this claim which gave rise to the cross-claim, which was, in short, an application by Millers for discretionary relief in case the ground for attack should be made out. His Honour did not find it necessary to deal with this claim, but Howard Smith's submissions in relation to it will be made below.

68. If Ampol's primary case against Millers were made out a further question arises as to the consequences for Howard Smith of that conclusion. In addition to supporting Miller's contention that the allotment was properly made and was therefore valid, Howard Smith raised a defence based upon the fact that it had acquired legal title to the shares the subject of the allotment, that even if the allotment were invalid on the ground suggested by Ampol it was voidable and not void, and that Ampol was not entitled in the circumstances to have the allotment set aside.

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69. Notwithstanding detailed arguments that were put to him on matters of fact and law, His Honour ultimately decided the case on the basis that, as was contended by Ampol at the hearing, it raised for determination a relatively simple issue of fact.

70. The appellant does not accept His Honour's formulation of the issues, either of fact or law, which arose for determination in the case, and indeed submits that it was in the formulation of the issues that His Honour committed an initial error.

His Honour formulated the issue as being the following question of fact :

> Was the primary purpose of the majority of directors to satisfy the Company's need for capital or was their primary purpose to destroy the majority holding of Ampol and Bulkships?

His Honour found that it was the latter although his mode of expressing that conclusion varied substantially in different parts of his judgment. This finding then, according to His Honour, gave rise to a question of law which he formulated thus :

> "If a majority bloc of shareholders denies success to what is thought by the directors to be an attractive takeover, can the benefits of the takeover be obtained for the other shareholders by the directors issuing shares so as to destroy the majority?"

His Honour said that the answer to that question was in the negative, and that therefore the plaintiff was entitled to succeed in the action.

E. HIS HONOUR'S FINDING OF FACT

71. Certain of His Honour's findings of

fact have been set out and discussed above.

72. One important finding of fact made by His Honour, in favour of the defendants, had the consequence that a principal ground upon which the conduct of the Directors was challenged, may be removed from further consideration. His Honour completely rejected the allegation that the majority Directors were motivated in any way by a desire to retain their position on the Millers' Board or by any other purpose of personal gain or advantage. The evidence made it clear that most of the Directors held the view that in the circumstances they would shortly lose their positions on the Board whatever happened. His Honour said:

> "I discard the suggestion that the Directors of Millers allotted these shares to Howard Smiths in order to gain some private advantage for themselves by way of retention of their seats on the Board or by obtaining a higher price for their personal shareholding. Personal considerations of this nature were not to the forefront so far as any of these Directors was concerned, and in this respect their integrity emerges unscathed from this contest." p.1132 l.43 to p.1133 l.7

73. His Honour rejected the contention of the Directors that their "primary purpose" in voting for the allotment was to gain for the Company the infusion of capital which the allotment involved. For present purposes, the Appellant is content to make the following observations with respect to that finding of fact : p.1176 l.30

(a) Although His Honour rejected the assertion that the purpose as stated was a primary purpose of the Directors, he appears to have accepted that it was a

subsidiary purpose, and he certainly did not find to the contrary of the proposition that it was a purpose without which the Directors would not have been prepared to make the allotment.

(b) His Honour did not make any finding to the contrary of the proposition that the Directors acted honestly in the sense that they believed that they were legally entitled to act as they did and, indeed, that they would not have made the placement had they not genuinely believed the Company had a real capital need and that the infusion of capital would greatly benefit the Company as a commercial entity. His Honour made no finding that the majority of directors did not honestly accept the legal and financial advice which they were given by the Company's executives at the Board meeting.

(c) One of the principal arguments advanced in His Honour's reasons for judgment as a ground for rejecting the directors' contention involves a serious misapprehension or misunderstanding of the evidence on the part of His Honour. In pointing out that the professed purpose of the Directors was inconsistent and contrary to what His Honour called "the context" His Honour saw as an important part of the context what he said was a long standing policy on the part of Millers of satisfying its financial requirements by way of loan rather than equity capital. As stated in paragraphs 29 and 34 above, there was never any such policy and the fact that the financial requirements had been satisfied by loan capital rather than

p.1172 Ll.11-16

share capital was a matter of necessity, and never of choice.

(d) His Honour found that the assertion of the Directors as to their primary purpose carried a lack of conviction but he was at pains to disclaim any finding that any of the Directors was deliberately or consciously misstating his purpose or motivation. In every case His Honour said that the Director as a result of the preparation for the litigation, answering interrogatories, and self analysis involved, could by the time he came to give evidence well have believed that his primary purpose was as he stated it, and that there were substantial elements of unconscious reconstructions rather than recollection and of honest self-justification involved in the directors' evidence. Accepting that, the Appellant will submit that the whole enquiry upon which Ampol and His Honour himself embarked involving, as it did, an acceptance of the proposition that there was a relevant distinction between 'purpose' and 'motive' and that there had to be something which could be described as a 'primary purpose' was, in the circumstances of the present case, misconceived. His Honour overlooked the fact that, in many circumstances, individual persons, including directors, are influenced or moved by more than one consideration and would not have adopted some course of action or acted in some particular way but for the combination of circumstances and considerations.

74. The alternative (and, apparently the only alternative) view of the Directors' primary purpose as argued by Ampol was that of reducing the

proportionate shareholding of Ampol and Bulkships in Millers with a view thereby to facilitating the Howard Smith takeover. In argument at the hearing the Appellant protested against this submission and contended that such a characterisation reflects the way in which Ampol and Bulkships saw the conduct of the Millers' directors as affecting them rather than as the way in which the directors viewed their own conduct and objectives.

75. His Honour having posed the above two alternatives as the competing (and only possible competing) findings, reached the following conclusion :

p.1183 l.30 to p.1184 l.2

"The conclusion that I have reached is that the primary purpose of the four directors in voting in favour of this allotment was to reduce the proportionate combined shareholding of Ampol and Bulkships in order to induce Howard Smiths to proceed with its takeover offer. There was a majority bloc in the share register. Their intention was to destroy its character as a majority. The directors were, and had for some weeks been, concerned at the position of strength occupied by Ampol and Bulkships together. They were aware that in the light of the attitude of these two shareholders Howard Smiths could not be expected to proceed with its takeover offer that these directors regarded as attractive. They issued the shares so as to reduce the interest of these two shareholders to something significantly less than that of a majority. This was the immediate purpose. The ultimate purpose was to procure the continuation by Howard Smiths of the takeover offer made by that Company."

It is to be noted that even within the framework of the alternatives he saw as being open to him, His Honour's expression of the "purpose" of those involved fluctuated at various parts of his judgment between assigning primacy to the desire to keep the Howard Smith takeover offer alive or to the desire to reduce the proportionate shareholding of Ampol and Bulkships. There are various internal inconsistencies in His Honour's findings on this point. Thus, at one point His Honour stated that certain evidence pointed strongly to three of the directors having the intention primarily directed to keeping on foot Howard Smith's takeover offer by means of destroying the proportionate strength of the combined Ampol-Bulkships shareholding. Later in his judgment, His Honour made the explicit finding set out above.

F. HIS HONOUR'S CONCLUSION.

76. Having made the above findings His Honour went on to ask himself what he regarded as the question of law posed for decision in the case, that is to say whether majority directors "had it within their power to issue shares for the direct purpose of destroying an existing majority bloc." His Honour found that the answer to that question was in the negative. What force His Honour gave to the word "direct" in this context is not clear.

77. His Honour said :

> "But it is to my mind unacceptable to assert, as the defendants do, that if a majority denies success to what is thought by Directors to be an attractive takeover the benefits of the takeover can be obtained by the Directors issuing shares so as to destroy the majority. That is what the defendants seek to justify in this case."

p.1190 Ll.1-8

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With respect to His Honour that is certainly not what the defendant Howard Smith sought to justify in the case nor was any such assertion made during argument by Counsel for the Appellant.

78. His Honour then went on to consider the question of Howard Smith. In substance, he held that in consequence of the negotiations prior to the 6th July and of the terms of its own letter of that date Howard Smith was "fixed with notice that Millers Board were predominantly influenced by an inadmissible purpose".

p.1191 l.48 to p.1192 l.2

79. His Honour then concluded directly that, although the allotment was voidable not void, Howard Smith could not bind the Company to it. The Plaintiff therefore succeeded in the action.

G. THE BREACH OF STOCK EXCHANGE RULES.

80. His Honour appears to have attached great importance to the fact that the challenged allotment was in breach of the rules of the Sydney Stock Exchange. The precise significance to His Honour of the breach is not clear, but he said of the Directors' decision in the face of the breach :

p.1188 Ll.40-43

> "This serves to underline the imprudence of their action, even though of itself it does not establish invalidity."

81. The breach in question does not, as a matter of law, either alone or in combination with any other circumstances, affect the validity of the allotment one way or the other, and His Honour erred in law in suggesting that it did. Nor was the "prudence" of the Directors' action a matter that arose for His Honour's determination.

On that aspect of the matter, however, it is important to remember that since Millers was virtually certain to be taken over in the near future the Directors considered its days as a listed company to be numbered in any event.

82. The Directors in question acted as they did on legal advice, in full knowledge of the possible consequences, but honestly believing that they would be discharging their duty by facing up to the possibility of suspension of the shares in the circumstances.

H. APPELLANT'S SUBMISSIONS OF LAW ON THE MAIN QUESTION.

83. The power of the directors of a company to issue shares is a fiduciary power. A Court will not interfere with or set aside an exercise of the power unless it is satisfied that the power has been exceeded or abused.

84. At the outset in dealing with a challenge such as that made in the present case it is necessary to look to the ambit of the power which is confided to the directors by the Articles of Association. In the present case Articles 4 and 110 are particularly relevant. They confer a wide discretion on the directors.

85. The ultimate enquiry is as to the bona fides of the directors.

In Hindle -v- John Cotton Ltd. (1919) 56 Sc. L.R. at 630-631 Viscount Finlay said :

> "Where the question is one of absence 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 interest of the company or were acting from some bye-motive, possibly of personal advantage, or for any other reason."

See also in Re Smith -v- Fawcett Ltd. (1942) 1 Ch. 304.

86. Most of the cases in which issues of shares by directors have been set aside were, in fact, cases where the directors were held to have been acting from the "bye-motive" ..... of personal advantage", and, in particular, for the purpose of entrenching their own position (cf. Fraser -v- Whalley, 1864 2 H. & M.10; 71 E.R. 361, Punt -v- Symons, 1903 2 Ch. 506; Piercy -v- Mills, 1920 I Ch. 77; Ngurli Ltd. -v- McCann, 90 C.L.R. 425). Such a purpose is wholly impermissible and "corrupting" in the sense that its very presence vitiates the exercise of the power. There was, of course, no such purpose in the present case.

87. It is of critical importance that a trial Judge should bear in mind that he is not in any sense acting as some kind of tribunal of appeal from the decision of the directors. He is not at liberty to substitute his own conclusions on relevant factual problems for theirs, his enquiry being as to their state of knowledge and belief, not as to the correctness of their beliefs and understandings.

Referring to an exercise by directors of a power to refuse registration of share transfers Isaacs, J. said in Australian Metropolitan Life Assurance Co. Ltd. -v- Ure, 33 C.L.R. at 231 :

"Acting entirely within the scope of their power, honestly basing their action on their

own business opinion, they were exercising a function with which no Court can interfere, and over which no Court has any jurisdiction of review or appeal."

88. It is neither helpful nor relevant to make fine distinctions between "motive" and "purpose" or between "immediate purposes" and "ultimate purposes". Such distinctions, which appear to have their origin in revenue law, are alien to the task upon which a Court of Equity is engaged when it is considering a challenge to the exercise of a fiduciary power, particularly one entrusted in wide terms to company directors.

89. Where directors are found to have acted in what they believed to be an interest or interests they were entitled to serve by their actions their exercise of power can only be set aside if it be found that either :

(a) the interest or one of the interests they were serving was an inadmissible or "corrupting" interest (such as self-interest);

OR

(b) they have so misconceived their function that they cannot be said to be acting substantially for the purpose of serving any interest which it is legitimate for them to take into account.

90. The test which is frequently applied to cases such as the present, that is to say whether the directors were acting "bona fide for the benefit of the company as a whole" is not easy to apply to this case. The motives and purposes of the directors were both complexand, in a sense, developed over the course of consideration of the proposals. Furthermore, the "interests of the

company as a whole" are not easy to define. The company as a commercial entity was plainly going to benefit from the share issue and this was a substantial ground on which the advocates of the proposal supported it. If, on the other hand, one looks to the "individual hypothetical member" (cf. Greenhalgh -v- Arderne Cinemas Ltd., 1951 Ch. 286) further problems arise. All shareholders benefited, including Ampol and Bulkships, in their capacity as shareholders. (See Peters American Delicacy Co. -v- Heath 61 C.L.R. 457 per Latham C.J. at 481 and per Dixon J. at 511 to 513).

91. The interests which the directors in the present case were serving may be stated as follows :

(a) they were endeavouring to keep the Howard Smith offer open and thus in turn -

(i) securing to the shareholders a fair price for their shares;

(ii) warding off what they saw as a combination harmful to the interests of Millers;

(b) they were taking the opportunity of obtaining a large and much-needed infusion of capital into Millers.

92. In relation to sub-paragraph (a) above it is necessary to bear in mind that the situation was one in which it was reasonable for the directors to conclude that some takeover or other was inevitable. It is submitted by the Appellant that both considerations in sub-paragraphs (a) and (b) above are legitimate interests for the Directors to serve or legitimate purposes for them to pursue.

In this context it is material to note that the relevant legislation obliges directors to take more than

a passive role in a takeover situation (cf. Companies Ordinance ss. 180A et seq.). In Savoy Corporation Ltd. -v- Development Underwriting Ltd. (1961) 80 W.N. (N.S.W.) 1021. Jacobs, J. rejected as -

> "unreal in the light of the structure of modern companies and of modern business life ..... the view that directors should in no way concern themselves with the infiltration of the company by persons or groups which they bona fide consider not to be seeking the best interests of the company".

93. His Honour's whole approach to the present case was affected by the following fundamental errors :

(a) the acceptance of a relevant distinction between "motive" and "purpose";

(b) the search for a single, "primary", "immediate" purpose;

(c) a consideration of the relevant facts with too much emphasis on what His Honour thought about them and too little emphasis on what the directors thought about them.

94. In the light of the principles set forth above His Honour, on the facts found by him, should have resolved the main question in favour of Millers and Howard Smith.

95. In any event, His Honour in considering the separate position of Howard Smith should have held that that company was, in the light of the relevant legal principles, entitled to accept that the Millers' directors were acting properly and within power and that Howard Smith was a bona fide purchaser for value of the shares without notice of any irregularity or defect in the

allotment.

J. THE ISSUE CONCERNING MR. BALHORN

96. The nature of this challenge to the allotment is set out in paragraph 67 (a) above.

The appellant submits the matter is concluded against Ampol by His Honour's findings of fact.

K. THE EXCLUSION OF SIR PETER ABELES

97. The allegations upon which the plaintiff's claim was based are in paragraphs 25 and 27 of the Statement of Claim. Ampol claimed that the proceedings of the meeting were vitiated because Sir Peter Abeles was wrongfully excluded from discussion and voting and alleged that Howard Smith knew of such exclusion when it received the challenged allotment and paid for the shares. His Honour found that Sir Peter Abeles was wrongfully excluded but did not find it necessary to deal with the consequences of that exclusion. However, if the Appellant succeeds in its principal case, this point will not arise.

p.2055 98. (a) In interrogatories (Ex. HS1) Howard Smith sought particulars of the allegation that it had knowledge of the alleged exclusion of Sir Peter Abeles from discussion or voting. Ampol was unable to give such particulars.

(b) At the hearing Ampol failed to establish any knowledge on the part of Howard Smith by the alleged exclusion at any material time.

(c) It was never suggested to any of the Miller witnesses in cross-examination that Howard Smith was told of the decision to

exclude Sir Peter Abeles, or told that such exclusion had occurred.

(d) The only time the possibility was even mentioned was in the cross-examination of Conway. The witness was being asked about his discussion with Maxwell of Howard Smith at the Miller offices on the afternoon of July 5th.

"Q. During the course of this discussion was there raised any reference to the decision taken to exclude Sir Peter Abeles from discussion and voting on the allotment? p.762 Ll.29-32

A. No."

That discussion took place at about 5.45 p.m.

99. The objective events of the 6th July insofar as Howard Smith was involved in them were as follows : At about 9.40 a.m. Mr. Maxwell handed Messrs. Conway and Taylor a letter of application and a form of agreement relating to the proposed allotment. The meeting was held on a lower floor, but Mr. Maxwell remained in an upstairs office. After the resolution was passed the agreement and share scrip were executed under the common seal of Millers and Mr. Conway took them upstairs and handed them to Mr.Maxwell in exchange for Howard Smith's cheque. The share certificate (Ex. W) bore the common seal of Millers, affixed and countersigned in the manner provided by the Articles. The certificate on its face asserts that Howard Smith is the registered holder of the shares (see also Companies Ordinance 1962 s.92). The share register entry had been made in advance of the meeting. p.1306 l.23 to p.1307 l.10 p.1307 l.15 to p.1308 l.25

Indeed the orders His Honour made were framed on the basis that Howard Smith became the registered holder of the shares.

The question which then arises is whether, in those factual circumstances, the (assumed) fact that the proceedings of the Miller Board were in some way vitiated by a wrong ruling of the Board's Chairman in relation to discussion and voting by one of the Board members produces the result that as between Millers and Howard Smith the allotment was not legally binding on Millers.

100. Howard Smith was an outsider dealing with Millers. It applied for an allotment of shares in Millers on certain contractual conditions. It received a share certificate and deed executed, in an apparently regular fashion, under the seal of the Company in pursuance of what purported to be a resolution of the Company's Board of Directors. It was entered on the share register as holder of the shares. It paid over about $1m. in cash and undertook to pay about $9m. at some future time.

p.1307 l.15 to p.1308 l.25

101. The appellant submits that the case falls squarely within the Rule in Turquand's Case (The Royal British Bank v. Turquand 5E. & B.248 (119 E.R. 474)and 6 E. & B. 327 (119 E.R. 886)), according to which an outsider who deals with a company is entitled to assume that all internal regulations of the company have been complied with. (cf. Mahoney v. East Holyford Mining Company 1874 L.R. 7 H.L. 869 especially per Lord Hatherley at pp. 893-5, Lord Chelmsford at pp. 889-890 and 892 and Lord Penzance at pp. 899-900 and 902).

102. It is submitted that what went on in the Millers' boardroom on the 6th July, as to discussion and voting, was so far as Howard Smith was concerned a matter of "indoor management" or "internal management" of Millers and Howard Smith was entitled to assume that the

resolution pursuant to which the Company's common seal was affixed to the share certificate and deed was passed after due observance of the rules of discussion and voting which governed the conduct of the Board meeting.

103. At the hearing Ampol argued that the case was covered by a qualification to the general rule by reason of the fact that Howard Smith had knowledge of suspicious circumstances putting it on enquiry (cf. A.L. Underwood Ltd. v. Bank of Liverpool and Martins (1924) 1 K.B. 775). However, the alleged "suspicious circumstances" all related to or arose out of the main ground of challenge to the validity of the allotment and had no direct connexion with anything relating to the actual conduct of the meeting at which the resolution for the allotment was passed. This approach, the Appellant submits, overlooks the need to identify, for the purposes of the qualification of the Rule, the matter of which the person seeking to invoke the Rule is alleged to be put on enquiry. There was nothing to put Howard Smith on enquiry as to irregularities in the procedure followed at the Miller's Board meeting.

104. The Appellant also relies on the provisions of Section 51 A of the Conveyancing Act 1919 of the State of New South Wales which in favour of a purchaser in good faith deems a deed executed in the manner in which the share certificate in this case was executed to be duly executed and to take effect accordingly.

105. Alternatively to the above, Howard Smith submits that by reason of the matters set forth in paragraphs 35 to 41 above, and in the circumstances of the case, Sir Peter Abeles found himself in such a conflict of duty and interest that the Chairman of Directors was justified in excluding him from voting at the meeting and taking part in the discussion.

## L. CONCLUSION

106. The Appellant submits that the appeal should be allowed, His Honour's orders set aside, and the suit dismissed for the following amongst other

### REASONS

(1) That His Honour should have held that, on the evidence, the directors of Millers, in voting in favour of the allotment in question, were honestly acting in the discharge of their powers in interests which they were entitled to serve.

(2) That His Honour should have held that no sufficient ground had been made out for the setting aside by a Court of the honest exercise by the directors of their discretionary power.

(3) That His Honour failed to pay sufficient regard to the consideration that what was in question was the beliefs and understandings of the directors on factual matters, not the correctness of such beliefs and understandings, and moreover erred in substituting his own view of the financial situation of Millers, the commercial realities and business prudence of the proposed allotment, for the view of the Directors honestly formed on relevant financial and legal advice. His Honour did not advert to the bona fides of the Directors in acting as they did in changing from short term borrowing to increased share capital, nor did he advert to the significance of the fact that the allotment of 4,500,000 shares at $2.30 per share was calculated to produce a cash sum commensurate with the Company's obligations and needs for cash.

(4) That His Honour founded his decision upon irrelevant and inappropriate distinctions between the motives and purposes, and immediate and ultimate purposes, of the directors.

(5) That in so far as His Honour based his decision on the following findings of fact :

(a) that the primary purpose of the directors in voting in favour of the allotment was to reduce the proportionate shareholding of Ampol and Bulkships in Millers;

(b) that the allegation of certain Millers' officers and directors as to their purpose was contrary to a long-standing policy of preferring loan capital to equity capital

it was contrary to the evidence and the weight of the evidence.

(6) That His Honour should have found, if relevant, that the primary or dominant purpose of the directors who voted in favour of the allotment was to place the Company's finances on a sound basis.

(7) That His Honour erred in proceeding upon the footing that there must exist some "primary purpose" which was a single purpose and in failing to take account of the fact that the purposes actuating the majority of the Directors were at least twofold and that they would not have acted as they did in the absence of the purpose of obtaining a substantial financial advantage for the company.

(8) That His Honour should have found that the Directors were actuated by two purposes, namely the purpose of keeping open Howard Smith's offer for the benefit of all shareholders (or, alternatively,

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all shareholders other than Ampol and Bulkships,) and for the protection of Millers as a corporate entity, and for the purpose of improving the financial position of Millers and placing it on a sound basis for the future. His Honour should also have found that, although moved by the former purpose, the Directors would not have acted as they did unless the Company was in need of further share capital and that the issue of further shares for the purpose of improving the financial position of Millers was in the interests of the company as a whole. His Honour should further have found that the issue of shares for those two purposes together was within the powers of the Directors and was valid and effective.

(9) That His Honour erred in attaching significance, or undue significance, to the breach of the Rules of the Stock Exchange constituted by the allotment and in failing to advert to the significance of the general situation in which Millers found itself, i.e. that it was commercially certain it would be taken over.

(10) That His Honour erred in finding that Howard Smith had notice of the impropriety of the purposes of the Millers' directors in making the allotment.

(11) That in the circumstances the exclusion of Sir Peter Abeles from discussion and voting at the relevant directors' meeting did not constitute sufficient ground as against Howard Smith for the setting aside of the allotment.

(12) That Howard Smith, as the legal

holder of the shares, was an allottee for value without notice of any irregularity in the allotment and had a legal title which was not defeasible by reason of any irregularity in the internal affairs of Millers and, in particular, not defeasible by reason of any irregularity in the conduct of the meeting nor in the motives or intentions of the Directors.

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K. A. AICKIN

A. M. GLEESON

No. 9 of 1973

IN THE PRIVY COUNCIL

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O N  A P P E A L
FROM THE SUPREME COURT OF NEW SOU
WALES EQUITY DIVISION

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B E T W E E N :

HOWARD SMITH LIMITED Appellan

- and -

AMPOL PETROLEUM LIMITED and OTHERS
Responde:

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# CASE FOR THE APPELLANT

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