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Legal Aspects of the New Zealand Stock Exchange
Listing Rules

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This paper examines two broad aspects of the Listing Rules of the New Zealand Stock Exchange: one, their status as a contract, and the implications of that for their enforcement, and two, the discretion of the Stock Exchange to interpret and modify the Listing Rules to suit its ends. The underlying theme of the paper is that users of the Listing Rules should question the legitimacy of the purported effect of some of the listing requirements. For example, it is contended that rulings on the interpretation of the takeovers provisions required to be included in a listed company's constitution are not binding on shareholders or the company, because they are effectively alterations to the constitution and therefore require the approval of shareholders. Similarly, although the Listing Rules purport to reserve the NZSE an absolute and unfettered discretion to, for example, delist a company it is likely that the powers of the NZSE are subject to some sort of judicial review.	6
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I INTRODUCTION

The Listing Rules ("the Rules") of the New Zealand Stock Exchange ("the NZSE") occupy an important position in the New Zealand securities regulation regime. However, they do not have the force of law, are not administered or enforced by a specialised government body, and their administration and enforcement is not subject to ordinary administrative law constraints. Rather, the Rules form part of an extraordinary contract administered by a private owned and funded entity.

This paper has two broad purposes. The first, is to discuss the nature of the obligations imposed by the Rules, and the enforceability of those obligations both in practice and in hypothetical legal proceedings. It is submitted that the NZSE's heavy reliance on the threat of delisting a company and the ability of shareholders to enforce the Rules has a number of serious limitations. Although, a requirement for the company to comply with the Rules in its constitution has probably improved the ability of shareholders to enforce the Rules, there are other significant barriers to enforcement, for example litigation costs risk and information disadvantages, which impede shareholder litigation.

The second is to examine the nature of the NZSE's broad powers to issue rulings on the interpretation and application of the Rules, the extent to which shareholders and listed company's are "bound" by those rulings, and any limits on the NZSE's discretion. It is submitted that the NZSE's rulings are not binding on shareholders, and are only legally binding on listed companies if the ruling is issued before the breach of the Rules occurs. It is also argued that, in light of recent developments in the scope of public law judicial review, the Court of Appeal might be persuaded to reconsider its opinion that the decisions of the NZSE are not amenable to judicial review. However, the grounds for seeking such a review, and the relief able to be obtained in such proceedings, is likely to be limited.

The underlying theme of this paper is that when dealing with the Rules, assume nothing. Apparently settled principles relating the Rules and the NZSE are susceptible to question.

This paper does not examine the substantive merits of any particular listing requirement, or argue the merits or otherwise of securities regulation. It is assumed that some form of securities regulation is necessary. Equally, this paper does not directly address the issue of giving the Listing Rules the force of law, or retaining the contractual nature of the Rules and enacting specialised statutory provisions for their enforcement.

The next section contains an introductory statement on two basic elements of this paper: the company constitution, and a stock exchange. Section III introduces the NZSE and its history, and the Rules. Section IV questions the traditional classification of the Rules as a binding, enforceable contract. Section V examines the scope of the Rules, namely who is bound to comply with them, and who can enforce that obligation. Section VI examines the enforcement powers of the NZSE, and concludes that the NZSE is heavily reliant on the threat of delisting, with the limitations associated with that remedy, to ensure listed companies comply with the Rules. Section VII looks at aspects of the three mechanisms available for shareholders to enforce the Rules. Section VIII is the first of two sections concerning the second focus of this paper - the discretionary rulings powers of the NZSE. It examines the nature of these rulings, and the formulation of rulings. The effectiveness of a ruling to prevent a shareholder from seeking to enforce the Rules is questioned. Section IX contends that the operations of the NZSE are arguably subject to judicial review, contrary to settled case law. However, the restraints imposed by the courts are unlikely to exceed those imposed by the law of equity or contract.

Finally, section X contains a broad summary of the paper's main conclusions.

II PRELIMINARIES

A The Constitution

Any company incorporated or re-registered under the Companies Act 1993 ("the 1993 Act") may, but is not required to have a constitution.¹ The primary purpose of the constitution is to allow shareholders to create their own rules concerning the internal governance of the company, subject to the requirements of the 1993 Act. In addition, constitutional authorisation is required to "opt in" to various otherwise illegal transactions like share buy-backs, and the provision of insurance for directors by the company. The constitution does not affect the validity of transactions between the company and third parties that do not have notice that the constitution or the Act has not been complied with.²

The provisions of the constitution are given statutory force under section 31(2) of the 1993 Act which states that:

¹ See section 26 of the Companies Act 1993.

² See section 18 of the Companies Act 1993. Interestingly, section 18 appears to invoke a constructive knowledge rule by the words "ought to know" rather than merely "know".

“Subject to this Act, the constitution of a company is binding as between-

(a) The company and each shareholder; and

(b) Each shareholder-

in accordance with its terms.”

The equivalent documents under the Companies Act 1955 (“the 1955 Act”) were the articles of association and the memorandum of incorporation. The articles of association were expressed to constitute a contract which was enforceable as a deed between the company, and shareholders, and each shareholder *inter se*.³ The Law Commission expressed considerable dissatisfaction with this approach.⁴ It appears from this, and in the absence of a reference in section 31(2) to a contract or deed, that the company and shareholders are placed under a statutory duty, rather than a contractual duty, to comply with the provisions of the constitution. Furthermore, under section 134 of the 1993 Act directors have a general duty not to act, or agree to the company acting, in a manner that contravenes the constitution.⁵

There are a range of specific remedies, including specific performance, for enforcing the provisions of the constitution. In summary, these are:

(a) Shareholders or directors may apply to the court for an injunction to prevent the company contravening its constitution. Similar relief can be obtained by shareholders and the company against directors.⁶

(b) A shareholder may apply to the court for an order requiring the company to perform an act required by the constitution.⁷ Similar relief can be obtained against a director on application to the court by the company or a shareholder.⁸ The court will grant such an order where it considers it is “just and equitable” to do so.

³ See section 14 of the Companies Act 1955.

⁴ See Law Commission Report No 9 *Company Law Reform and Restatement* (Law Commission, Wellington, 1989), paras 154-158, 39-40.

⁵ See section 134 of the Companies Act 1993.

⁶ See section 164 of the Companies Act 1993.

⁷ See section 170 of the Companies Act 1993.

⁸ See section 170 of the Companies Act 1993.

- (c) A shareholder has either a personal action or a derivative action against directors who breach their duty to act, and not agree to the company acting, in breach of the constitution.⁹

There are no specific provisions for enforcing a shareholder's obligations under the constitution.

A company's constitution may contain such provisions as it "wishes to include"¹⁰, provided that constitution may only restrict the rights, privileges, powers granted to a company by the 1993 Act¹¹. The scope of the constitution is further limited by section 31(1), which proscribes:

"The constitution of a company has no effect to the extent that it contravenes, or is inconsistent with, this Act."

A number of sections are expressed to be applicable "notwithstanding the constitution of the company", for example, section 106 which requires special resolution approval of shareholders for major transactions, amalgamations, and alterations by shareholders to the constitution. In contrast a number of other sections are specifically identified as being "subject to the constitution", for example, section 39 which provides that a share is transferable so that the transferability of shares can be restricted by the constitution. Certain provisions are expressly prohibited, for example, a provision requiring a shareholder to take up more shares in the company.¹²

The rest of the provisions in the 1993 Act do not refer to the constitution at all. However, it does not necessarily follow from section 31(1) that the effect of provisions of the 1993 Act which do not refer to the constitution are not able to be altered by it. Rather, the enforceability of such a constitutional provision turns on the application of section 31(1) in each particular case.¹³

⁹ The uncertainty arises because the Companies Act 1993 does not specify whether the duty to comply with the constitution is owed to the company or to shareholders. It is submitted that the answer will depend on the constitutional provision in question. Guidance can be taken from section 169, which gives a non-exhaustive list of the duties owed by directors to the company and to shareholders.

¹⁰ See section 30 of the Companies Act 1993.

¹¹ Section 16 of the Companies Act 1993.

¹² See section 101 of the Companies Act 1993.

¹³ Dugan R *The Companies Act 1993: Governance Issues for closely held companies* (forthcoming)

B What is a stock exchange?

A stock exchange is essentially an association of sharebrokers who have agreed, as amongst themselves, to trade shares on behalf of their clients in a particular way.¹⁴ A stock exchange performs a critical function in a capitalist economy like New Zealand's. Broadly, it provides a fast and fairly cost effective means of liquidating and transferring assets from one use to another, by enabling investors with complementary investment and risk preferences to transact without ever meeting or even directly communicating. This is because share brokers assume the risk that the parties to the sale contract default. In terms of the Rules, the brokers are held to be principals on the contract. Accordingly, if a client defaults the relevant broker is personally liable to buy or sell the securities. The NZSE monitors its members to ensure they are sufficiently solvent to meet this obligation if it arises. Fairly conventional economic theory posits that, given the presence of such an efficient system for transferring wealth between different uses, assets will gravitate toward the most efficient use, maximising the total wealth of society.

III THE NEW ZEALAND STOCK EXCHANGE

The NZSE operates a national stock exchange in New Zealand. It is the only stock exchange in New Zealand. The NZSE itself has its origins in a number of privately owned, independent provincial stock exchanges which were operating under the Sharebrokers Act 1908. In 1915 they set up what was called the Stock Exchange Association of New Zealand as a central body while continuing their own operations. In 1981, the Sharebrokers Amendment Act was enacted to provide for the incorporation of a single body, the New Zealand Stock Exchange, as a successor to the association and what were by then four trading exchanges. Although established by statute, the NZSE is essentially a privately owned, funded, and operated organisation.

¹⁴ The settlement system employed by the NZSE can be summarised thus: "Settlement of securities transactions conducted through the NZSE is effected through an electronic registration system known as FASTER, which was introduced in 1992. Introduction of the FASTER system streamlined some aspects of settlement, although it did not result in a completely paperless system. A seller of securities is required to deliver a transcript form and script to its broker. The broker then electronically effects a transfer of the securities in the issuer's securities register from the seller to itself and then the purchaser's broker, without the use of a written transfer or the delivery of a script. The purchaser's broker electronically transfers registration of the securities from itself to the ultimate purchaser, again without a written transfer or script. On completion of the transfer the issuer's share registry issues new script to the purchaser. On the transfer of the relevant securities from the seller to the seller's broker, the seller's broker holds the securities on trust for the seller until the seller has received the purchase price. Similarly, on transfer of the securities to the purchaser's broker, the securities are held in trust

The NZSE is subject to minimal government regulation. The Sharebrokers Act 1908 (as amended by the Sharebrokers Amendment Act 1981) requires that every association of sharebrokers register under the Act, and that until registration it may not use the words "Stock Exchange" in its name.

The Rules are rules imposed by the NZSE on companies that have their shares traded on the exchange (listed companies").¹⁵ Listed companies must comply with the Rules to obtain, and maintain, the quotation and trading of its shares on the exchange. The Rules contain a broad range of requirements, for example: pre-requisites for listing¹⁶, restrictions on the form of on-market share transfers¹⁷, continuous disclosure by listed companies¹⁸, and regulations governing takeovers¹⁹, and transactions with related parties²⁰.

IV CONTRACTUAL EFFECT OF THE RULES

The Court of Appeal in *New Zealand Stock Exchange v Listed Companies Association Incorporated and NZ Forest Products*²¹ ("the NZSE decision") held that all listed companies are contractually bound to the NZSE to comply with the Rules. Woodhouse P said:

"It is beyond question, too, that the listing agreement was intended to create a contractual relationship. And clearly the contract which was made was intended to embrace the published listing requirements of the Exchange as part of the terms and conditions it was to operate. Accordingly, the listing agreement entered into by NZ Forest Products is binding and enforceable against it. Obviously similar listing contracts which have not been terminated by one or other of the parties will continue to have binding force and effect."

for the purchaser, subject to the purchaser paying the purchase price." *International Securities Law* (Euromoney, London, 1996) p291.

¹⁵ Entities other than companies are able to be listed on the exchange, for example, unit trusts. Similarly securities other than shares are quoted and traded on the exchange, for example unit trust units. For simplicity, however, all listed entities are herein referred to as companies, and securities traded at the exchange are herein referred to as shares.

¹⁶ See section 5 of the Listing Rules.

¹⁷ See section 11 of the Listing Rules.

¹⁸ See section 10 of the Listing Rules.

¹⁹ See section 4 of the Listing Rules.

²⁰ See section 9 of the Listing Rules.

²¹ (1984) 2 NZCLC 99,159, 99,164.

The contractual effect of the Rules was also assumed by Barker J in the High Court in *New Zealand Stock Exchange v NZ Forest Products Ltd*²² two years earlier. Barker J said:

“I find the exact position of the listing agreement rather puzzling in the light of the 1981 Act. Clearly it was a subsisting contract which the defendant inherited from the SEANZ.”

The Court of Appeal, the High Court, and counsel appearing in both cases appear to have assumed without addressing the issue that, prior to 1981, the Rules formed part of a binding contract between each listed company and the NZSE. The question before the court was whether the Sharebrokers Amendment Act 1981 requires these Rules to be promulgated as regulations. Thus Woodhouse P, after holding that the Sharebrokers Amendment Act 1981 neither requires or enables statutory rules to be made by the NZSE to regulate listed companies, said²³:

“And in this context it is accepted by all counsel that the listing agreement entered into by NZ Forest Products does continue to have contractual force and effect: that the contractual relationship was in no way qualified by the provisions of the 1981 Act. We agree.”

There are number of difficulties with the assumption that the Rules form part of a legally effective contract.

Rule 5.4.2 purports to reserve the NZSE an absolute and unfettered discretion to delist a company.²⁴ It can be argued that such a wide discretion renders the listing contract and the Rules unenforceable at law.²⁵ This is because the courts have held that a promise to do or not to do something at the absolute discretion of the promisor does not evidence an intention to create binding contractual relations.²⁶ The argument is that the NZSE's promise to list the company, in return for the company's promise to comply with the Rules, does not create a binding contract because of the NZSE's wide discretion to delist the company and renege on its promise.

* This analysis assumes that the listing contract is intended to create executory obligations on the company to comply with the Rules and the NZSE to continue to list the

²² (1984) 2 NZCLC 99,051, 99,065.

²³ See above n21, 99,163.

²⁴ The actual wording of Rule 5.4.2 is “...may at any time and in its absolute discretion...”.

²⁵ See P Spender “The Legal Relationship Between the Australian Stock Exchange and Listed Companies” (1995) 13 C&SLJ 240. Spender makes this argument in relation to the listing rules of the ASX.

²⁶ See *Taylor v Brewer* (1813) 1 M & S 29; and J Chitty and AG Guest (ed) *Chitty on Contracts* (27th ed, Sweet & Maxwell, London, 1994) 159; and DW Greig and JLR Davis *Law of Contract* (Law Book Co, Sydney, 1987) 238.

company. However, it can be argued that the NZSE does not undertake to maintain the listed status of a company. This is the effect of rule 5.4.2. Rather, the listing agreement comprises a promise by the listed company to comply with the Rules if, and for as long as, it is listed. This promise is binding on the company as soon as the NZSE provides consideration to support it by actually listing the company and allowing its shares to be traded on the exchange. Listing by the NZSE may constitute sufficient consideration to bind the applicant company even though the NZSE may not have been bound to list the company.²⁷

Furthermore, it can be argued that the NZSE's discretion to delist a company is not unfettered. The reviewability of decisions of the NZSE is discussed below in section IX.

Alternatively, it can be argued that the listing contract is unenforceable because the terms of the contract are not sufficiently certain. The foreword to the Rules requires listed companies to comply with the spirit as much as the letter of the Rules. This requirement creates difficulties if it enables the NZSE to take action if it feels the Rules have been breached in spirit. What the spirit of the Rules requires in any given situation is left to be determined by the NZSE. Arguably, therefore, the contract is uncertain because it is unclear to each listed company as to how the NZSE will interpret the Rules in any given situation.²⁸ Another problem is that certain Rules purport to bind non-parties to the listing contract, for example subsidiaries of the listed company, and shareholders.²⁹

These arguments are not addressed in the judgments in the High Court or the Court of Appeal in the *NZSE* decision.

Australian courts have held that the listing rules of the ASX, which purport to confer a similar powers to delist companies, determine the "spirit" of the listing rules, and waive their operation are contractually binding.³⁰ However, these issues were not addressed in those decisions either.

The force of these arguments is unclear. At the end of the day, a court is likely to be influenced as much by commercial nature of the transaction as legal argument. It is likely that given the commercial considerations and the decisions in both the High Court and

²⁷ See *Cambridge Nutrition Limited v BBC* [1990] 3 All ER 523, 538. Per Ralph Gibson LJ.

²⁸ P Spender, see above n25, 257.

²⁹ See Rule 1.1.5 of the Listing Rules which purports to require subsidiaries of the listed company to comply with the Rules.

³⁰ *Kwikasair Industries Ltd v Sydney Stock Exchange Ltd* (1968) ASLR 30,701.

Court of Appeal in the *NZSE* decision, a court would confirm that the Rules comprise a legally enforceable contract.

V SCOPE OF THE RULES

The scope of the Rules to bind parties other than listed companies, for example, shareholders and directors of listed companies and other companies association with the listed company, is delimited by the law of contract. Only the parties to the listing contract in question, in this case the NZSE and the listed company, are obligated to comply with its terms and conditions.

As a consequence, the Rules cannot effectively regulate certain aspects of the New Zealand securities market closely related to listed companies but not directly involving them, for example, insider trading, and takeovers.

In contrast, under legislation, the Australian Securities Commission, Australian Stock Exchange ("ASX"), shareholders, and persons aggrieved by a breach are given standing to obtain orders requiring a listed company to comply with the listing rules, although the listing rules themselves retained their contractual status. Orders can be obtained against the listed company, any director or secretary of the company, and any holding company, subsidiary company, or any subsidiary of a holding company, of the listed company.

A Rules included in the constitution

Section 4 of the Rules requires all listed companies to adopt certain provisions into their constitutions ("section 4 provisions") namely: one of three optional sets of rules regulating takeovers of the company ("takeovers provisions"); a procedure for 90 per cent majority shareholders to compulsorily purchase the remaining shares and for minority shareholders to require a 90 per cent majority shareholder to acquire their shares ("compulsory acquisition provisions"). Listed companies must also adopt certain provisions dealing with breaches of the takeovers provisions adopted by the company under this section ("enforcement provisions"). Broadly, the section provisions impose restrictions on "restricted transfers", basically share transactions which may involve a transfer of control. Two of the optional sets of takeovers provisions impose "notice and pause" requirements on offerors. The third option requires any restricted transfer to be accompanied by an offer to all shareholders of the company on equal terms, unless the transfer has been approved by shareholders. The enforcement provisions deal with what

happens if a shareholder breaches the takeover provisions, including preventing the shareholder from voting the shares, and empowering the company to sell the shares.

* The NZSE has issued sample constitutional provisions that may be adopted by listed companies ("the sample provisions"). The listed company is also bound in contract to comply with the section 4 provisions.

As terms of the company's constitution, the section 4 provisions are binding the listed company, its shareholders, and its directors have a general duty not to act, or agree to the company acting, in a manner that contravenes the constitution under section 134 of the 1993 Act.³¹ While most stock exchange listing rules restrict the content of listed companies' articles or constitutions, section 4 is novel because it requires listed companies to incorporate parts of the Rules themselves into their constitutions. This is probably so uncommon because a special resolution of shareholders is needed to alter those provisions.³²

B Requirement in constitution to comply with rules

Under rule 3.1.1(c), all listed companies' constitutions must contain a provision requiring the company to comply with the Rules for as long as that company remains listed on the exchange ("the compliance provision"). The purported effect of this provision is to allow shareholders to remedy a breach of the Rules by the listed company or directly (or either a personal or derivative action) against directors of the company via the provisions in the 1993 Act for remedying breaches of the constitution.

C Are directors of listed companies bound by the Rules?

As noted above, directors are under a statutory duty not to agree to the listed company breaching the Rules. It is interesting to consider the position of directors under the purely contractual rules. In the absence of anything else, a director of a listed company is not contractually obliged under the Rules to procure compliance by the company with the Rules because there is no privity of contract between the NZSE and the director. As a consequence, the NZSE requires that all directors of listed companies sign a written

³¹ See section 134 of the Companies Act 1993.

³² See T Shreves "Secondary Market Regulation in New Zealand" in G Walker and B Fisse (eds) *Securities Regulation in Australia and New Zealand* (Oxford University Press, Auckland, 1994) 447.

acknowledgement promising to procure compliance by the relevant listed company with the Rules.³³ The ASX proposed to introduce a similar measure in 1982.³⁴

However, this acknowledgement is unlikely to improve compliance with the Rules. This is because the acknowledgement is unlikely to impose binding obligations on signatory directors. The NZSE does not appear to provide any consideration to support the directors' undertaking and render it enforceable at law. Further, the acknowledgement is not executed in the form of a deed, which would render the acknowledgement binding notwithstanding the lack of consideration. Finally, although rule 2.2.2 requires that listed companies procure similar acknowledgements from new directors of listed companies, there is evidence that the NZSE does not police this rule. Consequently, it is likely that a significant number of directors of listed companies have not executed an acknowledgement.

VI ENFORCEMENT POWERS OF THE NZSE

The NZSE in the foreword to the Rules emphasises private enforcement of the Rules, rather than enforcement by itself, on the basis that the stock market works better when "buyers and sellers are fully responsible for the quality and consequences of their decisions to buy and sell". An emphasis on private enforcement rather than enforcement by a regulatory agency like the NZSE is consistent with other modern consumer protection legislation in New Zealand, for example, the Consumer Guarantees Act 1993, the Securities Amendment Act 1988, and the Companies Act 1993. This approach to enforcement of securities regulation in New Zealand was heavily favoured by the Ministerial Working Group on Securities Law Reform in 1991.³⁵

However, number of commentators have pointed out the significant barriers to private enforcement through legal proceedings, for example: the costs involved in bringing and action, the risk of incurring party-party costs, and the problems of obtaining the information

³³ See rule 2.2.2 of the Listing Rules.

³⁴ Exposure Draft of *Proposed Listing Rule Amendments and Other Issues* released in October 1992. Rule (3J)(37) required every director and secretary of a listed company to enter into an undertaking to the ASX "In the course of acting as a Director/Secretary I shall use my best endeavours to procure compliance with the Listing Rules by the company". However this was not taken up when Rules subsequently amended in 1 July 1993. Magarey comments (14-15) that unlikely to add more if directors personally liable as companies liable to comply with rules under statute.

³⁵ Also commonly referred to as the Report of the Group of Eight and the Roche Report.

needed to base a legal action.³⁶ The Ministerial Working Group on Securities Law Reform considered that until these barriers were removed or reduced, private enforcement rights are unlikely to result in a large number of private enforcement actions or improved compliance. There is evidence to support this prediction. Recent studies indicate that the overwhelming majority of actions to enforce the listing rules of the ASX are brought by the Australian Securities Commission and not private individuals.³⁷ The number of actions brought annually by the ASC suggests that compliance has not been usefully increased by empowering shareholders to enforce the Rules.

In the United States, enforcement of listing rules by the stock exchanges themselves is encouraged. Shareholders of listed companies may sue any stock exchange under the Securities Exchange Act 1934 for damages for any loss caused by the stock exchange failing to enforce its listing rules.³⁸ Similar to New Zealand, the listing rules of stock exchanges in that jurisdiction only have contractual force. However, United States jurisdictions do not have a statute similar to the Contracts (Privity) Act 1982 ("the Contracts (Privity) Act"), and therefore, shareholders are prevented by the doctrine of privity from directly enforcing listing rules of United States stock exchanges.

Notwithstanding the comments in the foreword to the Rules, there is a perception that the NZSE is extremely active in policing and enforcing the Rules. This is consistent with the concerns expressed recently by the Chairman of the Panel, Mr Kevin O'Connor, that the Panel is increasingly faced with the prospect of legal challenge.³⁹ There is no evidence of a widespread belief that the NZSE feels significantly constrained from delisting a large listed company.

A Regulatory structure of the NZSE

The NZSE typically delegates its powers administer and enforce the Rules to the Market Surveillance Panel ("the Panel"). The formation of the Panel was prompted by

³⁶ See P Fitzsimons "The New Zealand Stock Exchange: Rights and Powers" and B Gaynor "Securities Regulation in New Zealand: Crisis and Reform" in Walker and B Fisse (eds) *Securities Regulation in Australia and New Zealand* (Oxford University Press, Auckland, 1994) 534.

³⁷ See I M Ramsay "Enforcement of Corporate Rights and Duties by Shareholders and the Australian Securities Commission: Evidence and Analysis" (1995) 23 ABLR 174; and R Simmonds "The Enforcement of Corporations Law and Securities Regulation in Australia: A Framework for Analysis and Reform" (1995) 25 WALR 49.

³⁸ See P Fitzsimons, above n36.

³⁹ See "Exchange panel shows concern at legal threats" (The Dominion, Wednesday 24 September 1997) 11.

criticisms that the Board of the NZSE, which was comprised entirely of members of the NZSE, was incapable of effectively policing the Rules because of the vested interest of members of the NZSE in maintaining and expanding the number of companies listed on the exchange. It was thought that, as a result, the NZSE may not enforce the Rules as zealously as the public interest requires and may interpret the Rules in favour of listed companies.⁴⁰ Another problem the NZSE faced at the time was threats by certain large listed companies to shift off shore, placing the NZSE under pressure to take a more facilitative approach to interpreting the Rules.

The Panel is intended to function as an independent panel of experts, not dominated by members of the NZSE, to deal with enforcement and interpretation of the Rules. A majority of the seats on the Panel must not be members of the NZSE.⁴¹

The establishment of the Panel was generally viewed positively by commentators.⁴² One commentator has, however, questioned the independence of the Panel because the NZSE appoints the members of the Panel and the NZSE retains the ultimate decision on whether a matter is referred to the Panel.⁴³

B Suspending trading or delisting

The NZSE's principal means for securing compliance by listed companies with the Rules is the threat of delisting a non-complying company. Alternatively, the NZSE may temporarily suspend trading in a listed company's securities, rather than taking the ultimate step of delisting, pending compliance by the company with the Rules. Suspension gives rise to similar considerations as delisting.

Delisted company's shares are no longer able to be traded on the exchange. Delisting, therefore, has very serious consequences for the company. Delisting would substantially reduce the value of the company's shares because of the increased difficulty and cost of obtaining buyers for the shares outside the stock exchange mechanism. The resulting fall in

⁴⁰ See New Zealand Ministerial Committee of Inquiry into the Sharemarket *Report of the New Zealand Ministerial Committee of Inquiry into the Sharemarket* (Wellington, 1989).

⁴¹ See Appendix 3 of the Listing Rules which establishes and covers the administration of the Panel.

⁴² See B Gaynor above n36 and PD McKenzie "Reforming Securities Regulation in New Zealand" in G Walker and B Fisse (eds) *Securities Regulation in Australia and New Zealand* (Oxford University Press, Auckland, 1994) 447.

⁴³ P Fitzsimons above n36, 546.

value of the company's share capital may cause the company to breach debt covenants, would reduce its ability to borrow, and increase its cost of borrowing.

Perhaps most importantly, shareholders of the company would be likely to remove incumbent directors⁴⁴, and perhaps seek other remedies against those directors under the 1993 Act for breach of directors' duties. In *FAI Insurances v Pioneer Concrete (No 3)*⁴⁵, Needham J found that an allotment of shares in breach of the Rules provided prima facie evidence of a breach of the proper purposes duty by directors of the company. Furthermore, directors are likely to suffer significant ignominy from being involved in a company that is delisted due to the actions of the directors, undermining the security of current directorships and limiting future employment prospects. Therefore, there is substantial incentive for a director of a listed company to ensure that the company complies with the Rules.

The main criticism of delisting a company for breaches of the Rules is the resulting harm to shareholders of the delisted company. As noted above, delisting increases the cost and difficulty selling the shares, therefore reducing the value of those shares. This effect is particularly significant for small minority shareholders because the value of their small shareholdings may be less than the costs involved in selling the shares off-market rather than through the stock exchange's electronic matching system. In some cases, the harm caused by delisting may be greater than the damage caused by the breach of the Rules which initiated the decision to delist in the first place.

Delisting a large listed company would also have a significant impact on the incomes of members of the NZSE, and could possibly affect the value of other shares. As a result, large listed companies are likely to have more scope to infringe the Rules. On the other hand, large listed companies are more likely to comply with the Rules. The reason is that large companies generally enlist experienced, professional directors whose livelihoods depend on a number of directorships. These directors are generally unwilling to jeopardise their positions, and potential future employment, by being censured by the NZSE for allowing a company to breach the Rules, and are more likely to be aware of their potential liability exposure to shareholders for agreeing to a course of action which results in delisting.

⁴⁴ See section 156 of the Companies Act 1993, which allows shareholders of a company to remove directors by ordinary resolution.

⁴⁵ (1986) 13 ACLR 492.

That said, the necessity to weigh up the cost to shareholders, members, and others of delisting a company against the cost of the initial breach imposes a serious limitation on the ability of the NZSE to enforce the Rules based solely on its unfettered discretion to delist a non-complying company.

Another limitation is that in some circumstances, the threat of being delisted may not constitute a threat at all, for example, if the transaction alleged to be in breach of the Rules contemplates delisting anyway, like a management buy-out or going private transaction. This limitation is tempered in part by the NZSE's discretion to refuse any subsequent listing application by those involved in an earlier breach of the Rules.

C Investigate suspected breaches, publish report, and censure

The NZSE may investigate possible breaches of the Rules by requiring the production of relevant documents or other information under the Rules. The NZSE may publish a report based on the findings of that investigation, or issue a public statement censuring a listed company or its directors in relation to a breach of the Rules. The adverse publicity associated with censure is a significant incentive for directors to ensure that the listed company complies with the Rules.

Ultimately, however, the ability of the NZSE to compel a listed company to produce all relevant information is dependent on the ability of the NZSE to compel the listed company to comply with the Rules. A further limitation is that the NZSE cannot demand information from other market participants that are not listed or are not members of the exchange. In, particular this limits the NZSE power to investigate allegations of insider trading which may not involve the listed company itself.

All listed companies are required to pay a bond to the NZSE upon listing to which the NZSE may resort to cover any expenses.⁴⁶ The NZSE charges a listed company full costs for any investigation it conducts, which can in itself be a deterrent from breaching the Rules.

D Contractual remedies available to the NZSE

It would be difficult for the NZSE to obtain an order for specific performance of the Rules by the listed company, or injuncting the company from breaching the contract.

⁴⁶ Currently the NZSE requires NZ\$75,000.

The Rules exhibit a number of factors that a detrimental to an application for specific performance of a contract. For one, the Rules lack "mutuality" because the Rules are not capable of supporting an order for specific performance against both a listed company and the NZSE.⁴⁷ In *Kwikasair Industries Ltd v Sydney Stock Exchange Ltd*⁴⁸ Street J held that the Court would not impose an injunction against the ASX with respect to its obligations (if any) under the listing rules, on the grounds that equity would not grant specific performance of an immediately terminable agreement. The same logic would prevent a listed company from obtaining an injunction (prohibitory or mandatory) against the NZSE under the Rules. There is authority that a court will deny specific performance for want of mutuality, however, later cases suggest that mutuality merely raises a question over the courts discretion to be exercised according to all that has happened up to time for judgment.⁴⁹

The NZSE may also be prevented from obtaining specific performance because the rule in question may involve continuous or successive acts, for example the continuous disclosure requirements in section 10 of the Rules, and consequently require the supervision of the court. A requirement for supervision by the courts does not necessarily preclude specific performance, but weighs heavily against the courts exercising its discretion.⁵⁰

Alternatively, and presuming the breach of the Rules was sufficiently serious or involved a substantial detriment to the NZSE, the NZSE could cancel the listing contract and seek damages for the breach.⁵¹ However, any damages awarded to the NZSE in such an action are likely to be nominal, because the NZSE is unlikely to have suffered any significant loss as a result of the breach of the Rules. The persons most likely to have suffered loss are shareholders. It appears that damages for a breach of the listing rules of the ASX are likely to be purely nominal.⁵²

⁴⁷ For explanation of this requirement see G Jones and W Goodhart *Specific Performance* (2 ed, Butterworths, London, 1996) 38.

⁴⁸ (1968) ASLR 30,701 (Supreme Court of New South Wales); D Brewster "Judicial enforcement of the Listing Rules of the Australian Stock Exchange" (1991) 9 C&SLJ 313, 319.

⁴⁹ G Jones and W Goodhart *Specific Performance* (2 ed, Butterworths, London, 1996) 39; *Price v Strange* [1978] Ch 337, 354 per Goff LJ.

⁵⁰ See above n49, 44.

⁵¹ See sections 4 and 6 of the Contractual Remedies Act 1979.

⁵² *Designbuild v Endeavour* 5 ACLR 1980 610, 635. Fernell J said at 635 "...the undoubted, and, in my view, unexaminable, discretion of the exchange (see *Kwikasair Industries Ltd v Sydney Stock Exchange*

The NZSE's ability to obtain interim relief is hampered by the necessity to give an undertaking as to damages for any loss suffered by the listed company as a result of the injunction if the court subsequently lifted the injunction.⁵³

Perhaps because of these difficulties, there are no reported decisions involving legal action by the NZSE to enforce the Rules. The NZSE is heavily reliant on the threat of delisting to secure compliance by listed companies with the Rules.

VII ENFORCEMENT OF THE RULES BY SHAREHOLDERS

A Contracts (Privity) Act 1982

At common law, only the parties to a contract may seek to enforce that contract.⁵⁴ In the absence of anything else, therefore, only the NZSE has standing to commence legal proceedings to enforce the Rules. The effect of this principle in New Zealand has been modified by the Contracts (Privity) Act. Under section 8 of that Act, persons upon whom a contract confers or purports to confer a benefit are able to enforce that contract as if they were a party to it. The proviso to that section provides that:

“Provided that this section shall not apply to a promise which, on the proper construction of the deed or contract, is not intended to create, in respect of the benefit, an obligation enforceable at the suit of that person.”

Rule 2.1.1 acknowledges shareholders of listed companies as beneficiaries of the Rules, so that the Rules “purport to confer” a benefit on shareholders and are able to be enforced by shareholders under the Contracts (Privity) Act. Rule 2.1.2 prevents shareholder's from enforcing the Rules so as to limit the right of the NZSE to exercise its powers under the Rules as it sees fit in particular its discretion to make rulings in respect of the Rules and to change or revoke any of the rules or entitle any person to pursue any proceedings or enforce a provision of the Rules which is the subject of a current ruling other than in accordance with that ruling.

Ltd [(1968) ASLR 30,701]), whether with or without cause, to ‘suspend’ or ‘delist’ a company provides a far more powerful means of securing observance of the Official Listing Requirements than would a mere promise to observe them - for damages for breach of such a promise may well be nominal, and ‘specific performance’ of the promise, in the absence of a power such as is now conferred on the court by s31 of the Act, [Securities Industry Act 1976] may well be singularly difficult to sustain.”

⁵³ See High Court Rules 236A and 630.

It is arguable that other participants in the securities market, for example, other listed companies or share brokers, also have standing under the Contracts (Privity) Act to enforce the Rules as persons upon whom the Rules confer a "benefit". "Benefit" is defined broadly to include any advantage. A person must be designated by name or reference to a class to have standing under the Contracts (Privity) Act. Although there is no equivalent to rule 2.1.1 for third parties other than shareholders, the NZSE, in the foreword to the Rules, defines the purpose of the Rules as being "to facilitate the efficient operation of the market in the interests of securities issuers, buyers, sellers, and brokers". It is certainly open for brokers and former shareholders (as sellers) to argue that the Rules identify them as a class of persons who the Rules are intended to benefit, and that therefore they have standing under the Contracts (Privity) Act to enforce them.

It is doubtful whether rule 2.1.1 significantly enhances the enforceability of the Rules. It can be argued that the Rules do not evidence a sufficiently clear and unqualified promise intended to be enforceable by a third party, a shareholder.⁵⁵ This is because a shareholder's ability to enforce the Rules is subject to the NZSE's discretion to waive any particular requirement.

No doubt, the requirement for a clear and unqualified promise would be met if the NZSE formally ruled that a listed company had breached a requirement and that shareholders were entitled to enforce the Rules under the Contracts (Privity) Act, because such a ruling forms part of the Rules.⁵⁶ However, is the NZSE to be taken to have waived or varied compliance with a particular rule if it has not issued such a ruling and not sought to enforce that requirement itself?

The courts in New Zealand have not addressed this issue. Australian courts have refused to enforce the listing rules of the ASX in proceedings brought by a shareholder on the assumption that the ASX has impliedly waived the requirement by failing to enforce the listing rules itself⁵⁷, or have granted an interim injunction pending the decision of the ASX

⁵⁴ See discussion of *Price v Easton* (1833) 4 B & Ad 433, and *Tweddle v Atkinson* (1861) 1 B & S 393 in JF Burrows, J Finn, SMD Todd and GC Cheshire *Cheshire and Fifoot's Law of Contract* (8th NZ ed, Butterworths, Wellington, 1997).

⁵⁵ See PD McKenzie "Takeovers - The New Zealand Experience" in JH Farrar (ed) *Takeovers, Institutional Investors, and the Modernization of Corporate Laws* (Oxford University Press, Auckland, 1993).

⁵⁶ See rule 1.6.2 of the Listing Rules.

⁵⁷ *FAI Insurances v Pioneer Concrete (No 2)* (1986) 10 ACLR 801, 814.

on whether or not to issue a waiver.⁵⁸ On the other hand, sections 5 and 6 of the Contracts (Privity) Act anticipate contracts that confer benefits on third parties and which make express provision for variation and discharge of that contract. It can be argued, therefore, that although the Rules probably do not impose unqualified obligations on listed companies, the Contracts (Privity) Act anticipates that promises able to be varied or even discharged via some mechanism in the contract be enforceable by the third party beneficiary.

A further barrier may be the questionable contractual effect of the listing contract, noted above. Following that argument, the Rules do not constitute a promise contained in a contract or deed and are therefore not able to be enforced by shareholders under the Contracts (Privity) Act.

Another potential problem is that under the Contracts (Privity) Act any variation and discharge of the Rules is only valid if all third party beneficiaries to the contract (principally shareholders) either:

- (a) have not materially altered their position or that of another party in reliance on the Rules; or
- (b) are aware of the ability of the NZSE to vary (or discharge) the Rules before materially altering their position in reliance on the Rules; or
- (c) consent to the variation or discharge.

Whether these restrictions apply in any given situation is a matter of fact that would need to be established in each instance. It would be hard for a shareholder that had relied on a provision of the Rules to prove it was not aware of the NZSE's powers of waiver or variation the Rules. However, if these restrictions applied to a particular provision of the Rules, any variation or discharge of that rule by the NZSE would be invalid without the consent of all beneficiaries who have relied on the rule unaware of the provision allowing the NZSE to so vary or discharge. Such rulings would not be contractually binding on the listed company (although this mere fact would probably not prevent the NZSE from enforcing the ruling by threatening delisting). Furthermore, rule 2.1.2 precludes anyone from seeking to enforce the Rules under the Contracts (Privity) Act other than in

⁵⁸ *Devereaux Holdings Pty Ltd v Pelsart Resources NL* (1985) 9 ACLR 879; also see D Magarey "Enforcement of the Listing Rules of the ASX" (1995) 13 C&SLJ 6, 15-17.

accordance with any ruling issued by the NZSE. Therefore, although that the ruling may not be effective to vary the Rules as provided in rule 1.6.2, a shareholder is unable to bring an action under the Contracts (Privity) Act at odds with the ruling.

Other commentators have pointed out the significant costs barrier to shareholders seeking to enforce the Rules and that shareholders are unlikely to have access to the information required to commence, or to threaten to commence, legal proceedings.⁵⁹

Even assuming a shareholder could mount a successful claim, it would be necessary for a shareholder to establish a causal link between the breach of the Rules and any decrease in the share price of the company concerned to be entitled to damages. Given the likely difficulties in establishing such a link, one commentator has noted that the court may only be willing to award nominal damages.⁶⁰

A shareholder would encounter the same difficulties faced by the NZSE if it sought specific performance.⁶¹ A court is likely to require that the shareholder demonstrate direct detriment to the value of the shares before granting injunctive relief or order specific performance of the Rules by the listed company.⁶²

It is worth noting that there have been no attempts by shareholders to enforce the Rules under these provisions.

B Takeovers provisions

Clause 3.6 of the sample provisions purports to limit the remedies for breach by a shareholder of the section 4 provisions to requiring the company to invoke the enforcement provisions, and prohibits any person from seeking an injunction preventing a transaction alleged to be in breach of the section 4 provisions. Clause 3.6 would not preclude a shareholder from bringing an action under a specific provision in the 1993 Act to enforce the section 4 provisions. Having said that, the 1993 Act does not contain specific provisions dealing with breaches by shareholders of the constitution.

⁵⁹ See P Fitzsimons above n36, 534; T Shreves above n32; New Zealand Ministerial Working Group on Law Reform *Report of the New Zealand Ministerial Working Group on Securities Law Reform* (Wellington, 1991).

⁶⁰ See *Mercury Energy v Power NZ Ltd (No 2)* (1995) 7 NZCLC 260,818.

⁶¹ See section VI D above.

⁶² See above n60.

However, it can be argued that a shareholder can apply to the court under section 91 of the 1993 Act to have a person who has purchased shares in the company in breach of the section 4 provisions removed from the share register of the company.⁶³ The argument is that the legal title to shares does not pass if the company's constitution imposes conditions on the transfer of its shares, until those conditions are met. This argument is based on section 39(1) which provides that shares are transferable "subject to any limitation or restriction on the transfer of shares in the constitution".

Furthermore, registration of the transfer does not perfect the transfer of legal title. This argument is based on section 39(2) which provides that shares in a company may be transferred by entry in the company's share register in accordance with section 84. Section 84(1) in turn provides that shares in a company may be transferred "subject to the constitution" by entry in the share register.

Section 89 of the 1993 Act provides that the share register is only prima facie evidence of legal title to the shares. Thus it does not necessarily follow from registration of a transfer in the company's share register that the transferor named in the transfer obtains legal title to the shares. The 1993 Act clearly contemplates the possibility of the legal owner of the shares and the registered holder of the shares be different persons.

* In conclusion, it can be argued that a purchaser that does not satisfy the takeovers provisions in a listed company's constitution does not obtain legal title to the shares even though the transfer has been recorded in the company's share register. Therefore, an "aggrieved person", or shareholder of the listed company, may move the court to rectify the company's share register by removing the purchaser from the share register and reinstating the original transferor of the shares.

The point is that this remedy would be available to a shareholder notwithstanding clause 3.6, because it is a remedy provided for by statute. Arguably, a shareholder could seek an injunction against the company, or its directors, preventing registration of a transfer that breached the takeovers provisions.⁶⁴ It is interesting to note that Australian courts have

⁶³ See section 91 of the Companies Act 1993.

⁶⁴ Transfers of shares in breach of the constitution are not immediately excluded by the 1993 Act from being registered. It appears that the constitution must expressly grant the board the power to refuse to register the shares, for that reason, or specifically state that such transfers are not to be registered.

refused to order rectification of the share register for breach of the listing rules of the ASX.⁶⁵

C Enforcement of other listing rules under the constitution

The effectiveness of the compliance provision has yet to be fully tested. However, it appears to have been assumed in *Mercury Energy v Power NZ Ltd (No 2)*⁶⁶ that the provision was effective to support an application for an injunction under, among other things, section 164 of the 1993 Act to prevent a breach of the Rules. The Court declined to grant the application for an interim injunction on the basis that the applicant, Mercury Energy, failed to demonstrate that it would suffer loss if the injunction were not granted. However, Morris J held that Mercury Energy had established a "reasonably arguable" case for granting of an injunction pursuant to the equivalent of section 164 of the 1993 Act in the amended 1955 Act. It seems therefore that the full range of remedies in the 1993 Act for breach of the constitution may also be available to enforce the Rules via the compliance provision. There is at least sufficient argument to survive a striking out application.

VIII CAN THE NZSE CONCLUSIVELY DETERMINE DISPUTES OVER THE RULES?

Under rule 1.4.2, "any party to a dispute" over the interpretation or application of the Rules may apply to the NZSE for a ruling. Listed companies and shareholders are required to apply to the NZSE to determine any dispute over the Rules before commencing legal proceedings to enforce the Rules.⁶⁷ The NZSE may, either upon being asked for a ruling or acting on its own, determine the dispute by ruling on the matter, refer the matter to the Panel, or allow the dispute to be determined in legal proceedings, at its discretion. In practice, the NZSE refers these matters to the Panel.⁶⁸ If the NZSE rules on the matter, any party to the dispute can request that the NZSE's decision be reviewed by the Panel. The Panel may uphold the NZSE's decision or substitute its own. Although it is unlikely that the NZSE would not accede to a request to refer a matter to the Panel, the ultimate decision is still the NZSE's.

⁶⁵ See *FAI Insurances v Pioneer Concrete (No 2)* above n57.

⁶⁶ See above n60.

⁶⁷ Rule 1.4.3 of the Listing Rules.

⁶⁸ Under rule 2.5.2 of the Listing Rules, the Panel may not review decisions of the NZSE relating to amendments to the Rules, appointment, dismissal, or discipline of officers of the NZSE (other than members of the Panel).

Rulings are governed by rule 1.4. The NZSE may make "rulings" on the interpretation of any provision or term of the Rules "for such periods and on such terms and conditions as the NZSE may determine". Such a ruling forms part of the Rules applicable to the listed company in respect of which the ruling was issued.⁶⁹ Given this, what can be said about the effect of a ruling?

Arguably, if a ruling concluding that a particular course of action would breach the Rules was issued before that action occurred, then a listed company undertaking that action would, by definition, be in breach of the Rules. In defending a legal action by the NZSE or a shareholder to enforce the Rules, a listed company could not argue that it had not breached the Rules because the Rules had been varied to provide that undertaking the course of action at issue would constitute a breach. However, if such a ruling was issued after the action alleged to be in breach of the Rules, the listed company be able to argue the merits of the interpretation adopted by the NZSE when defending court proceedings to enforce the Rules. The fact of breach is not determined by the ruling because the variation of the Rules would have occurred after the action that is alleged to have breached the Rules.

The Rules also allow the NZSE at its absolute discretion to waive, by written notice to the listed company concerned, the application of any provision or provisions of the Rules.⁷⁰ A waiver may be issued on such terms and conditions as the NZSE may determine, and for such period as the NZSE decides. Rule 1.7.2 allows the NZSE to revoke such a waiver. Waivers give the Rules flexibility to allow transactions which do not infringe the "spirit" of the Rules, as determined by the NZSE, but breach the strict letter of the Rules.

The NZSE's broad interpretative powers grant it a large measure of control over listed companies and transactions involving securities traded on the exchange. When the effect of the Rules on a particular transaction is unclear, the parties to the transaction often will approach the NZSE for a ruling to clarify their respective obligations under the Rules. This happens frequently because the Rules are drafted in wide, often ambiguous terms. As a result, transactions are often brought to the attention of the NZSE by the parties themselves where otherwise they might have gone unnoticed.

⁶⁹ See rule 1.6.2 of the Listing Rules.

⁷⁰ See rule 1.7.1 of the Listing Rules.

A Rules included in the constitution

The drafters of section 4 clearly envisaged that the NZSE would retain the same broad powers over the interpretation and application of section 4 provisions as it has over the ordinary contractual Rules. Clause 1.2 of the sample section 4 provisions published by the NZSE provides:

If the NZSE gives any Ruling in respect of the matters dealt with by sections [2, 3 or 4][of this Constitution], that Ruling shall be binding on the Company and all holders of Equity Securities, and shall take effect as if that Ruling were itself incorporated in this Constitution.

“Ruling” is defined in the interpretations section of the sample provisions as: “a decision, determination, ruling, waiver or dispensation by the NZSE given pursuant to the Rules”.⁷¹

Provisions of a constitution that are inconsistent with or contravene the 1993 Act are invalid to the extent of that inconsistency or contravention. Clause 1.2 therefore does not give rulings issued by the NZSE that are inconsistent with, or contravene a provision of, the 1993 Act binding effect under section 31(2); such a ruling is not binding on the listed company or its shareholders under the 1993 Act. The ruling may still be contractually binding on the listed company.⁷² However, the section 4 provisions purport to regulate shareholders, not listed companies, and even though the ruling may be contractually binding on the listed company it will not be binding on shareholders. Furthermore, the courts have refused to injunct a company from altering its articles despite the existence of a contract under which the company has undertaken not to alter its articles.⁷³ It is unlikely, therefore, that the NZSE could obtain a court order requiring the listed company to formally adopt a ruling into its constitution pursuant to rule 1.11.1. The NZSE’s only legal remedy would be damages for breach by the listed company of the listing contract.

Having said that, the NZSE is unlikely to issue a ruling that directly contravened a provision of the 1993 Act, for example, a ruling that directors of listed company’s need not consider the best interests of the company when complying with section 4, directly contrary to section 131 of the 1993 Act.⁷⁴

⁷¹ The requirement for this provision can be found in rule 4.7.2(f); in fact, the wording is identical.

⁷² Subject to analysis above in section?

⁷³ *Allen v Gold Reefs of West Africa Ltd* [1900] 1 Ch 656.

⁷⁴ Section 131 of the Companies Act 1993 requires that directors act in the best interests of the company when performing their duties as directors.

It can be argued that the purported effect of clause 1.2 is to allow the NZSE to alter the constitution of a listed company by issuing a ruling. It is submitted that a ruling purports to “alter” the constitution if:

- (a) the ruling purports to be binding on the company and its shareholders as if it were part of the constitution. This is satisfied by clause 1.2; and
- (b) a court would have interpreted the same term, or provision, differently. In other words, a Ruling alters the constitution if a court considers that it purports to alter the legal effect of that provision. This would need to be determined on a case by case basis by the courts.

Any alteration to a company’s constitution probably requires special resolution approval of shareholders. The constitution is defined under section 29(e) of the 1993 Act to include only those alterations made by special resolution of shareholders under section 32(2), and by the court under section 34.⁷⁵ Therefore, it can be argued that clause 1.2 is invalid in respect of rulings that purport to alter the constitution of a listed company and are not supported by a special resolution of the shareholders of that company. Such rulings would not be binding on shareholders, the company, or directors.

Although it was settled under the 1955 Act that the articles could not take away or limit a company’s power to alter the articles or memorandum by special resolution, there was no authority for the proposition that alterations other than by way of special resolution could or could not be authorised by the articles.⁷⁶ There is authority that alterations having the informal unanimous consent of shareholders create valid and binding articles, notwithstanding the statutory requirement for a special resolution was not formally fulfilled.⁷⁷ However, these cases appear to rely on the general company law principle that

⁷⁵ Section 29(e) of the 1993 Act defines the constitution as: “[...] (e) A document described in paragraph (a) or paragraph (b) or paragraph (c) or paragraph (d) of this section as altered by the company under section 32 of this Act or varied by the Court under section 34 of this Act.”

⁷⁶ Section 24 of the Companies Act 1955 similarly allowed the company, by special resolution, to alter the articles. *Walker v London Tramways Co* (1879) 12 ChD 705; *Allen v Gold Reefs of West Africa Ltd* [1900] 1 Ch 656 at 671, 676. There is a line of cases, beginning with *Ayre v Skelsey’s Adamant Cement Co Ltd* (1905) 21 TLR 464, holding that articles which purported to increase the majority required to approve an alteration to the articles were invalid. However, there is no authority for the proposition that the articles cannot decrease the majority required to alter the articles. R Pennington *Penningtons Company Law* (7th ed, Butterworths, London, 1995) 91, cite this line of cases in support of the proposition that the memorandum and articles cannot enable or require the alteration to be made in any other way than by special resolution.

⁷⁷ *Ho tung v Man On Insurance Co* [1902] AC 232 at 236 (PC) where the shareholders had failed to sign the copy of the articles which were registered at the companies office. The “articles” were then altered by special resolution a number of times, and used by the company for the next 19 years. *Cane v*

incorporators may do any *intra vires* action by unanimous consent,⁷⁸ rather than the proposition that alterations made other than by special resolution but via some mechanism approved in the articles are valid. Furthermore, the 1955 Act defined the articles as “the articles as originally framed or as altered by special resolution...”.⁷⁹ This suggests that only alterations approved by special resolution formed valid articles (subject to the general exception for unanimous shareholder consent outlined above).

* The Law Commission originally envisaged that the constitution might prescribe its own system for altering the constitution.⁸⁰ The equivalent provision to section 32(2) in the draft Act was expressed to be “subject to [the company’s] constitution”. This wording was not carried over into the final version of 1993 Act. Arguably, this indicates an intention that only alterations approved by special resolution of shareholders be valid. This is certainly the view taken by most commentators.⁸¹

There are a number of arguments that the 1993 Act does not require that all alterations to a constitution be approved by a special resolution of shareholders:

- (a) Section 32(2) provides that “shareholders may alter the constitution”; it does not say that “only shareholders may alter the constitution”. Arguably, therefore, a provision in the constitution purporting to allow a third party, in this case the NZSE, to alter the constitution is not inconsistent with the Act.
- (b) Section 106 is expressed only to apply “when” shareholders alter the constitution. The requirement in section 106 for special resolution approval of alterations to the constitution “notwithstanding the constitution” is inapplicable to alterations by persons or entities other than shareholders.

Jones [1980] 1 WLR 1451 where Michael Wheeler QC (sitting as a deputy judge in the High court) held that section 10(1) of the Companies Act 1948 (UK) did not mean that the articles can only be altered by special resolution. That section only laid down a procedure whereby some only of the shareholders can validly alter the articles. He held that the general principle that all shareholders acting together can do anything *intra vires* the company was still applicable and, therefore, articles approved by the unanimous consent of shareholders were valid.

⁷⁸ *Duomatic Ltd Re* [1969] 2 Ch 365; [1969] 1 All ER 161.

⁷⁹ Section 2(1) Companies Act 1955.

⁸⁰ See New Zealand Law Commission *Company Law Reform and Restatement - Report No 9* (Wellington, 1989) 89; and New Zealand Law Commission *Company Law Reform: Transition and Revision - Report No 16* (Wellington, 1990) 158.

⁸¹ M Russell *Morisons Company and Securities Law* (Butterworths, Wellington, 1995) E/10, para 9.9; E Abernethy and P Castle (eds) *Andersons Company and Securities Law* (Brooker & Friend, Wellington, 1991) Vol 1, 77; A Beck, A Borrowdale, L Trotman and D Wishart *New Zealand Company Law and Practice* (CCH New Zealand, Auckland, 1993) 92,035.

(c) Section 29 of the 1993 Act also defines the constitution as including “a document described in section 33 of this Act”. Section 33(1) of the Act refers to the constitution as including section 29(e) alterations “together with all amendments to [the constitution]”. This suggests that the constitution may be altered by means other than the methods listed in section 29(e), that is other than by shareholder special resolution, or by the court. However, for no apparent reason, there is no reference to section 29(e) in section 33(2). It may be difficult, therefore, to draw any firm conclusions from this provision.

(d) Section 34(1) refers to alterations of the constitution “using the procedure set out in the act or *the constitution*” (own emphasis added) which supports the view that the constitution can provide for alternative procedures for altering the constitution.

It is submitted, however, that these drafting points are simply enduring evidence of the original approach taken by Law Commission.

Therefore, rulings by the NZSE would not be conclusive evidence of a breach by a shareholder of the section 4 provisions. The court is able to examine such a ruling to determine whether or not it purports to alter the constitution of the company. This would involve determining the true legal meaning of the provision in question and deciding whether the ruling purports to alter that meaning. Such rulings, if given before the relevant action occurred, are determinative of whether the company has breached its contractual obligation to comply with the Rules.

An alternative or supplementary argument is that clause 1.2 is invalid because it purports to abrogate the court's role in interpreting the provisions of a company's constitution. Although, the 1993 Act does not specifically address the possibility that a third party be appointed to determine disputes over the terms of the constitution, the 1993 Act contains a variety of court-based remedies for breach of the constitution. Indeed, the Law Commission specifically addressed and affirmed the role of the courts in determining civil claims for breach of the constitution.⁸²

⁸² See *Law Commission Report No 9* see above at n80, 34 para 136.

Under the 1955 Act, the courts upheld provisions in articles requiring arbitration of disputes between shareholders and companies.⁸³ Indeed a recent report by the Scottish Law Commission proposes that an arbitration clause for company-member disputes be included in the default articles of association.⁸⁴ However in contrast to the 1955 Act did not contain any specialised provisions for remedying breaches of the articles of association, nor did the 1955 Act impose a statutory duty on shareholders and the company to comply with the articles of association. Under section 4 of the 1955 Act, the terms of the articles of association were simply enforceable as a deed or contract.

In preparing the 1993 Act, the Law Commission expressly departed from the contractual approach used in the 1955 Act, favouring instead to impose a statutory duty on the company and shareholders to comply with the constitution.

American courts have examined the validity of provisions in articles of association which provide for compulsory arbitration of claims under the Securities Exchange Act 1934. The Supreme Court in *Shearson/American Express v McMahon*⁸⁵ compared the alternative dispute resolution procedures sought to be instituted against the remedies provided by statute. The court required the sharebroker's client to show that the legislature intended that the statutory remedial provisions not be abrogated, and that the replacement procedure did not adequately protect their rights.

However, the 1993 Act does not contain any specific provision governing enforcement of the constitution against a shareholder by the company, or another shareholder. Arguably, therefore, clause 1.2 is consistent with the 1993 Act (and therefore valid) to the extent that it purports to abrogate the court's role to interpret provisions of the constitution that impose obligations on shareholders. A large proportion of the provisions required by section 4 impose obligations on shareholders. However, there are a number of provisions that impose obligations on directors of listed companies.

⁸³ *Hickman v Kent or Romney Marsh Sheep-Breeders' Association* [1915] 1 Ch 881. In this case the plaintiff brought an action against the company in connection with his expulsion from the company. Astbury J held that the company was entitled to have the action stayed because the articles amounted to a contract between the company and the member, and referred such matters to arbitration.

⁸⁴ Scottish Law Commission *Shareholders Remedies* (London, 1997) 189, 279.

⁸⁵ 107 S Ct 2332 (1987). This case considered a provision in a brokerage agreement providing for arbitration of any controversy relating to the customer's account, and precluding an action under the Securities Exchange Act 1934.

1 Waivers

At first glance a waiver may appear to be contrary to section 31(2) of the 1993 which provides that the provisions of the constitution are binding "in accordance with [the constitution's] terms". However, a waiver of certain constitutional provisions is not inconsistent with section 31(2), if the constitutional provisions required by section 4 can be interpreted as applying *only if* the NZSE has not issued a waiver. In other words, according to the terms of the takeovers provisions, the restrictions are only to be binding if no waiver has been issued.

It can be argued that waivers of certain provisions purport to alter the constitution, based on case law dealing with the point at which a waiver of contractual rights becomes a variation of that contract. Woodhouse J defined the distinction as follows:⁸⁶

"[A]t least I think it can be said that where the modified version of the original contract involves such changes in the contractual obligations of the parties that its structure is clearly affected, then the change goes beyond any question of waiver and must be regarded as a variation"

The distinction was also described by Goddard J in *Besseler Waetcher Glover & Co v Derwent Coal Co*⁸⁷ as:

"...if as a matter of contract the parties agree that the terms of the original agreement shall be varied, the variation must be in writing. But if what happens is a mere voluntary forbearance to insist on delivery or acceptance according to the strict terms of the written contract, the original contract remains unaffected, and the obligation to deliver and accept the full contract quantity still continues."

The distinction, however, is "a difficult one to apply in practice".⁸⁸ It can be inferred from these cases that a waiver of a substantive requirement of the takeovers provisions, for example, the requirement to give notice of a restricted transfer, can be characterised as an alteration to the constitution, and therefore invalid. On the other hand, a waiver of the time for giving that notice would not be considered an alteration.

⁸⁶ *Watson v Healy Lands Limited* [1965] NZLR 511, 513.

⁸⁷ [1938] 1 KB 408, 416-417.

⁸⁸ See J Chitty above n26, 1088.

B Effect on requirement to comply with the Rules in constitution

Rule 3.1.1(d) requires that listed companies constitutions also contain a provision exempting the company from the obligation under the compliance provision to comply with the Rules if the NZSE has issued a ruling or waiver authorising that action.

It can be argued on the same principles that any alterations to the Rules subsequent to the listed company adopting the compliance provision is not enforceable under the constitution unless the alteration has been approved by a special resolution of shareholders. This is because to hold otherwise would empower the NZSE to effectively alter the constitutions of listed companies, which is contrary to the 1993 Act.

This argument was not raised in *Mercury Energy v Power NZ Ltd (No2)*.⁸⁹ *Harman v Energy Research Group Australia Limited*⁹⁰, the company alleged that it was bound by its articles of association to observe the listing requirements of the Perth Stock Exchange. The articles contained a provision analogous to the compliance provision. Brinsden J in the Supreme Court of Western Australia held that the obligation under the articles of association:⁹¹

“Can only mean an obligation to comply with such of the listing requirements as the Stock Exchange, in its discretion, has required the company to comply with.”

The court held that the company had not breached its articles of association because the stock exchange could be taken to have impliedly waived the requirement to comply with the listing rules. It can be inferred from this decision that a company is bound under a compliance provision in its articles to comply with subsequent alterations to the Rules absent shareholder approval. However, the court did not consider the argument that this would allow the stock exchange to effectively alter listed company's articles. In addition, the case is not directly applicable in New Zealand because the companies legislation pertinent to that case was similar to the 1955 Act.⁹²

C The Panel as an arbitrator

“The relevant meaning of ‘arbitration’ in *The Oxford English Dictionary* is as follows:

⁸⁹ See above n62.

⁹⁰ (1985) 9 ACLR 897.

⁹¹ See above n90, 902.

⁹² The differences between the 1955 Act and 1993 Act in this regard, and the consequences of those differences, are discussed above.

The settlement of a dispute or question at issue by one to whom the conflicting parties agree to refer their claims in order to obtain an equitable decision.”⁹³

Certain operations of the Panel bear a striking resemblance to an arbitration. A recent example demonstrates this point. In early September 1997, the directors of Power NZ Limited alleged that two of its major shareholders, Mercury Energy Limited and Utilicorp, had breached the takeovers provisions in Power NZ's constitution.⁹⁴ Both parties approached the Panel for a ruling on the issue. Presumably, submissions were made to the Panel on the interpretation of the provision in question and the facts.⁹⁵ The Panel ruled that the two shareholders had not breached Power NZ's constitution, and therefore the directors were precluded from invoking the enforcement provisions. In summary, there was a dispute between directors of Power NZ and two other shareholders, and those parties referred the dispute to the Panel in the manner contemplated by the Rules for resolution. Similarly disputes between the NZSE and a listed company over the interpretation or application of the Rules can be referred to the Panel for determination.

It can be argued that the Arbitration Act 1996 applies to the proceedings of the Panel in either of these circumstances if the Rules constitute an “arbitration agreement” within the meaning of the Arbitration Act. “Arbitration agreement” is defined as:⁹⁶

“an agreement by the parties to submit to arbitration all or certain disputes which have arisen or which may arise between them in respect of a defined legal relationship whether contractual or not.”

Do the Rules fit this definition?

As noted above, all disputes in relation to the application or interpretation of the Rules may be submitted to the Panel for resolution, although the NZSE has a discretion not to refer a matter to the Panel.

It is clear that the Rules constitute an agreement between the listed company and the NZSE. This discretion is not critical to whether or not the Rules are an arbitration

⁹³ F Thorp and D Williams *Arbitration Act* New Zealand Law Society Seminar (Wellington, 1997) 58.

⁹⁴ “Exchange probes bid for Power NZ” *The Independent*, 5 September 1997, 1; and “Mercury, Utilicorp NZ cleared to vote” *The Dominion* 11 September 1997 15.

⁹⁵ The Panel is required to call for submissions from the issuer unless the NZSE certifies that the delay would be prejudicial to the shareholders. The Panel may take submissions from any one it considers has a material interest in the matter. See rule 2.6.4 of the Listing Rules.

⁹⁶ Section 2 of the Arbitration Act 1996. The predecessor to this Act, the Arbitration Act 1908 (now repealed), included a further reference to “any question or matter to be decided by one or more persons to be appointed by the contracting parties or by some person named in the agreement”.

agreement. The courts have upheld arbitration agreements which confer a discretion on only one party to refer disputes to arbitration.⁹⁷

It is unclear whether the Rules constitute an agreement between shareholders and listed companies, or shareholders and the NZSE, to arbitrate disputes over the Rules. Shareholders are not strictly parties to the Rules. Shareholders merely have rights to enforce the Rules under the Contracts (Privity) Act. It is not clear whether the Contracts (Privity) Act confers sufficiently strong rights on shareholders to enforce the Rules that they can be said to form part of an "agreement" between the listed company and its shareholders for the purposes of the statutory definition of "arbitration agreement". However, this would not satisfy the usual requirement for a "meeting of the minds" to form an agreement. Arguably, shareholders can be taken to have consented to the jurisdiction of the Panel by purchasing shares in a listed company. It is not clear that this would be sufficient to form an agreement.

The remaining issue is whether the Rules require the Panel to conduct an "arbitration" within the meaning of that term in the Arbitration Act. The term "arbitration" is left effectively undefined by the Arbitration Act.⁹⁸ The Law Commission in its report on the draft Arbitration Act said:⁹⁹

"The term 'arbitration' is not defined in functional terms, and the definition of 'arbitration agreement' similarly refrains from describing the nature of the arbitral process. Although the Quebec legislation comes closer to a definition of 'arbitration' in defining 'arbitration agreement' in terms of a submission 'to decision by one or more arbitrators to the exclusion of the courts' (article 1926.1), we believe that the concept is well enough understood not to require a definition."

⁹⁷ *Pittalis v Sherefettin* [1986] QB 868. See MJ Mustill and SC Boyd *The Law and Practice of Commercial Arbitration in England* (2 ed, Butterworths, London, 1989) 41, fn 17a.

⁹⁸ An arbitration under the Arbitration Act 1996 means "any arbitration whether or not administered by a permanent arbitral institution", (section 2).

⁹⁹ New Zealand Law Commission *Arbitration - Report No 20* (Wellington, 1991) 129, para 200. Although the Law Commission did not define the term, it did point out a number of similarities between arbitration and litigation, namely that: NZLC p59, para 16

- (a) the decision-maker must be impartial, treat the parties equally, and hear the respective cases of the parties;
- (b) the decision-maker's determination is intended to be binding on the parties and enforceable at law; and
- (c) the identity of the decision-maker, the procedure to be followed, and the applicable law all the subject of agreement between the parties.

Guidance can be taken from "documents relating to" the Model Law on International Commercial Arbitration adopted in June 1985 by the United Nations Commission on International Trade Law¹⁰⁰ or the United Nations working group responsible for preparing it.¹⁰¹ However, these documents do not elucidate this point.

English courts have established six criteria for determining whether an agreement contemplates an arbitration or some other form of dispute resolution process.¹⁰² For the Rules to constitute an arbitration agreement under these criteria, it must evidence an intention that:

- (a) **the decision of Panel be binding and enforceable at law.**¹⁰³ The Panel's determination forms part of the Rules and is therefore contractually binding on the listed company and the NZSE. Shareholders are prevented from enforcing the Rules under the Contracts (Privity) Act where the Panel has authorised the action by a ruling.

However, the NZSE can unilaterally vary the Rules at its discretion and effectively overturn the Panel's decision so that it is not ultimately binding on the NZSE.¹⁰⁴ Similarly, as noted above, rulings by the NZSE, and the Panel, in relation to actions brought by shareholders under the 1993 Act may not be binding under the 1993 Act because such rulings arguably constitute alterations to the listed company's constitution.

- (a) **that the Panel act impartially, and fairly to both parties.**¹⁰⁵ The requirement for the NZSE, and by extension the Panel, to act fairly and impartially in making its decisions may be implied by equity or public law.¹⁰⁶

¹⁰⁰ Also known as UNCITRAL.

¹⁰¹ Section 3 of the Arbitration Act 1996. The Act, including the definition of 'arbitration', is modelled closely on the Model Law ('the Model Law').

¹⁰² MJ Mustill and SC Boyd see above n97, 41.

¹⁰³ See *Arenson v Arenson and Casson, Beckman, Rutley & Co* [1976] 1 Lloyd's Rep 179, [1977] AC 405.

¹⁰⁴ Under rule 2.4.3 of the Listing Rules the Panel may exercise all the powers of the NZSE when dealing with matters referred to it under 2.4.1.

¹⁰⁵ MJ Mustill and SC Boyd see above n97.

¹⁰⁶ Judicial review of decisions of the NZSE is discussed below in section IX.

- (b) **the arbitration agreement is enforceable at law.**¹⁰⁷ As noted above, the prevailing view is that the Rules are binding as a contract between the NZSE, and the listed company. A shareholder who is not a party to the Rules but is merely granted standing by statute to enforce the Rules is also probably bound to the "arbitration" clause for any action under the Contracts (Privity) Act. This is because the Contracts (Privity) Act only grants shareholders the right to enforce the contract as if it were a party to it, and therefore subject to the arbitration clause. Moreover, the Contracts (Privity) Act allows the standing of shareholders to enforce the Rules to be modified by express provision.¹⁰⁸

However, it is questionable whether a shareholder is required to approach the NZSE before seeking to enforce the Rules under the listed company's constitution. As noted above, such a requirement is arguably contrary to the 1993 Act and therefore unenforceable.

- (c) **the Panel decide disputes which are already formulated at the time when the matter is referred to the Panel.** The Rules anticipate that the Panel review determinations by the NZSE in relation to disputes over the application or enforcement of the Rules. Often the Panel acts in the first instance because the NZSE typically delegates the matter directly to it. In either case, the requirement for a pre-existing dispute is satisfied.

Other critical factors are that:

- (d) **the jurisdiction of the Panel derives from the consent of the parties rather than some external source.** It is unclear whether shareholders can be taken to have consented to the jurisdiction of the Panel. The Panel is constituted under the Rules which form part of an agreement between each listed company and the NZSE. Can shareholders who are not party to that agreement be said to have consented to its provisions? In a sense the requirement to seek a ruling from the NZSE is imposed upon shareholders by listed companies and the NZSE. It is not clear whether shareholders can

¹⁰⁷ MJ Mustill and SC Boyd see above n97.

¹⁰⁸ See above section VII A which discusses the limitations on power to sue under the Contracts (Privity) Act 1982 and rule 2.1.2 of the Listing Rules.

be taken to have consented to the processes laid out in the Rules by purchasing shares in listed companies.

- (e) **the process is carried on between two parties whose substantive rights are to be determined by the Panel.** A ruling issued by the Panel is intended to be binding all shareholders of the listed company concerned and not simply the shareholders who made submissions to the Panel. Arguably this requirement is satisfied because all shareholders are probably able to make submissions to the Panel.

Other relevant but not critical factors are that:

- (f) the arbitration agreement contemplates that the Panel will receive submissions from both parties, or at least allow submissions to be made. Under rule 2.6.4, the Panel may receive submissions from anyone it considers to have a material interest in the matter, and in most situations from the listed company concerned.
- (g) the wording of the arbitration agreement is consistent with the view that the process was intended to be an arbitration. There is no express disclaimer of the view that the Panel acts as an arbitrator. The NZSE is able to insert such a provision at will.
- (h) the agreement requires the Panel to decide the dispute according to law. Although the Panel is likely to have regard to legal consideration, it is also required to consider the efficiency of the market. At the end of the day, the Panel is not likely to view itself as being constrained by legal considerations when interpreting the Rules if those considerations do not produce an interpretation that maximises the efficiency of the market.

The Rules satisfy all the common law criteria of an agreement to arbitrate all disputes between listed companies and the NZSE over the Rules, except for the requirement that the Panel's decision be binding on both the listed company and the NZSE.

Similarly, it is difficult to characterise the Rules as an agreement to arbitrate any disputes between shareholders and the listed company, or shareholders and the NZSE, under these criteria. The agreement to refer all disputes to the Panel, and the decisions of the Panel, may not be binding on shareholders in relation to an action brought under the listed company's constitution. It is unclear whether it is enough that the Rules clearly

evidence an intention to bind shareholders, or whether the Rules must actually be binding. Secondly, arbitration is characterised by the requirement for the consent of the parties to the process. The problem is determining whether shareholders, by virtue of their rights under the Contracts (Privity) Act or by acquiring share in a listed company can be taken to have agreed to refer disputes over the Rules to the Panel.

It seems unlikely therefore that the Rules would be characterised as an arbitration agreement and the proceedings of the Panel subject to the Arbitration Act. Having said that, the point is not entirely clear. Furthermore, even if the NZSE altered the Rules to expressly denying that the Panel is an arbitrator. The courts have ignored clauses of this nature. If the arrangement in substance meets the definition of an arbitration, then the courts will consider the proceedings to be an arbitration subject to the provisions of the Arbitration Act notwithstanding such a clause.

D Do the rules purport to oust the jurisdiction of the court?

At common law, any contractual provision which purports to destroy the right of one or both of the parties to submit questions of law to the courts are generally held to be invalid. The NZSE justifies the requirement that a ruling be obtained before any action at law to enforce the rules, on the basis of arbitration law cases which permit clauses that require arbitration of any dispute before allowing legal proceedings to be commenced to enforce the underlying agreement.¹⁰⁹ This justification presupposes that the proceedings of the Panel are an arbitration, which is highly questionable.

It can be argued that this requirement does not oust the jurisdiction of the court. Dealing with the potentially ousted rights in turn:

- (a) **Shareholders under the constitution.** The requirement to apply to the NZSE before enforcing the Rules under the 1993 Act is not binding on shareholders because they are not a party to the Rules. Similarly, any ruling issued by the NZSE are arguably ineffective to vary a shareholder's rights under the constitution.
- (b) **Shareholders under the Contracts (Privity) Act.** This requirement may effectively prevent a shareholders from enforcing the Rules under the

¹⁰⁹ So called *Scott v Avery* clauses (named after the leading case, *Scott v Avery* (1856) 5 HL Cas 811).

Contracts (Privity) Act. However, the Act expressly allows the third party's rights under the principal contract to be varied by provision of the parties.

- (c) **Listed company in contract.** Although the requirement for a ruling is binding on a listed company as a matter of contract, it can be argued that the jurisdiction of the court is not ousted because the ruling acts to vary the underlying agreement. Therefore, if a ruling is issued prior to the action alleged to be in breach of the rules (for example, an issue of shares), the jurisdiction of the court is not ousted because the court could not have had any jurisdiction over the matter until the action occurred. Neither the listed company nor the NZSE had any right to seek a remedy in court under the Rules at the time of the Ruling. If, on the other hand, the ruling is issued after the action alleged to be in breach of the rules, the ruling does not "bind" the company in the sense that the listed company is deemed to have breached the rules. The ruling cannot retrospectively constitute a particular action as being in breach of the Rules. Therefore, in legal proceedings by a shareholder or the NZSE to enforce the Rules, a listed company would not be bound to the interpretation set out in the ruling, and would be able to make submissions on the proper interpretation of the Rules.

In conclusion, the rulings powers of the NZSE do not "oust" the jurisdiction of the court. The only situation where the NZSE's rulings are binding in the sense that a listed company is prevented from having the matter determine by a court (that is where a ruling is issued before the action that breaches the Rules) arguably does not involve an ousting of jurisdiction because the contract is varied before the rights of the parties to submit the question to law arises.

IX ARE THE DECISIONS OF THE NZSE CAPABLE OF JUDICIAL REVIEW?

"Judicial review involves interference by the Court with a decision made by a person or body empowered by Parliament or the governing law to reach that decision in the public interest. A litigant may only invoke interference by the Court with such a decision if the litigant pleads plausible allegations which, if substantiated at the trial, will demonstrate that the decision was not reached in accordance with the law."¹¹⁰

¹¹⁰ *Mercury Energy Limited v Electricity Corporation of New Zealand Limited* [1994] 2 NZLR 385 per Lord Templeman.

Most actions for judicial review in New Zealand are made by way of the Judicature Amendment Act 1972, although the common law grounds for judicial review, known as the prerogative writs, remain available. A third avenue for judicial review, so called "private law" judicial review, essentially involves challenging a decision based on traditional private law causes of action, typically breach of contract. The classic example is a decision by an incorporated society that is in breach of its rules or constitution. In *Waitakere City Council v Waitemata Electricity Shareholders Society Inc*¹¹¹ Fisher J held that members of societies could bring an action founded in breach of contract where that society had acted outside the express or implied scope of its own rules. The members, having contracted into the society's rules by joining it, were entitled to obtain a declaration to prevent such a breach of contract. It was clear that this would have been true even if the decisions of the society were not amenable to review under the Judicature Amendment Act or via the prerogative writs.¹¹²

There may be limited grounds for seeking private law judicial review of the NZSE. The Court of Appeal in the *NZSE* decision¹¹³ upheld the ability of the NZSE to vary the Rules, free from the types of limitations applied in *Waitakere City Council v Waitemata Electricity Shareholders Society Inc*.¹¹⁴ Woodhouse P recognised that NZSE's ability to maintain a fair market would be stultified if it were impossible to vary the listing requirements without the express or implied concurrence of individual companies. Woodhouse P referred to the ability of listed companies to immediately terminate the listing contract as one reason for upholding the NZSE's power unilaterally to alter the Rules. However, the Rules have been altered since the Court of Appeal's decision in the *NZSE* decision¹¹⁵ to prevent listed companies from terminating the listing contract at will. Under the Rules currently in force, a listed company may only request that the NZSE terminate the listing contract (which the NZSE may grant, subject to any conditions it sees fit to impose, for example, shareholder approval).¹¹⁶ There is no longer provision for termination by a listed company. Further it is unlikely that the court would imply such a

¹¹¹ [1996] 2 NZLR 735.

¹¹² See also *Finnigan v New Zealand Rugby Football Union Inc (No2)* [1985] 2 NZLR 181; and *Peters v Collinge* [1993] 2 NZLR 554 (HC).

¹¹³ See above 21, at 705.

¹¹⁴ [1996] 2 NZLR 735. Here Fisher J held that amendments to the rules of the society must be within contemplation of the members when they joined, and consistent with the purposes of the society.

¹¹⁵ See above n21.

¹¹⁶ See rule 5.4.1 of the Listing Rules.

provision when the Rules appear to anticipate that voluntary delisting be achieved by a request from the listed company to the NZSE.

Alternatively, it can be argued that the equitable doctrine of fraud on a power requires the NZSE to exercise its powers in good faith and for the purposes for which they were conferred.¹¹⁷ It is useful to note that Australian courts have held in relation to the delisting powers of the ASX that, although the ASX is not subject to judicial review, it is subject to the requirements of natural justice and therefore must afford procedural fairness to a party affected by a discretionary determination.¹¹⁸

In a private law judicial review, the court only grants declaratory relief. The defendant is required to satisfy the usual criteria before substantive relief by way of an injunction may be granted. Having said that, a declaration is usually sufficient to protect the applicants rights.

A Judicature Amendment Act 1972

The traditional basis for judicial review under either the Judicature Amendment Act 1972, or the prerogative writs, is that the body being complained of is a public body exercising authority deriving from the Crown or Parliament.

For applications brought under the Judicature Amendment Act 1972, the requirement is that the body has exercised a "statutory power of decision". That term, in its original meaning, meant a power deriving from statute. However, a 1977 amendment to the Judicature Act expanded the definition to include decisions under the constitution or other instrument of incorporation, rules, or bylaws of any body corporate.

The NZSE was established as a body corporate by section 3 of the Sharebrokers Amendment Act 1981. Section 7(1) of that Act provides that the NZSE shall make rules for the conduct of its members and for the conduct of business on its exchange. Section 4 sets out the functions of the NZSE and provides it with "all such powers as are reasonably necessary or expedient to carry out its functions". Included in the functions are:

¹¹⁷ See P D Finn *Fiduciary Obligations* 1977 para 84.

¹¹⁸ See Beaumont J in *Chapmans Ltd v ASX Ltd (No 2)* (1995) 17 ACSR 524; cf *Kwikasair Industries Ltd v Sydney Stock Exchange Ltd* (1968) ASLR 30,701. The exact nature of this obligation is variable, depending upon the circumstances of the particular case and the nature and subject matter of the proceeding. Although the source of this requirement is unclear because the court held that there was no implied term in the listing contract limiting the ASX's power to delist.

“(b) To promote and specify the conditions and terms for the listing and trading of securities on its exchange .. and

...

(d) To promote the interests of its members and members of the public in relation to the listing, trading, underwriting, and marketing of securities.”

The Court of Appeal in the *NZSE* decision¹¹⁹ held that the Listing Rules were not made, or required to be made, pursuant to section 7(1) of the Sharebrokers Amendment Act. Woodhouse P interpreted section 7 as empowering the NZSE to make rules for the members of the NZSE but not rules regulating the relationship between the NZSE and companies listed on the NZSE. Rather, the relationship between the NZSE and listed companies was governed exclusively by contract, namely the listing agreement which incorporated by reference all of the Rules, including the rule on suspension of listing. The Court of Appeal inferred that, in order to constitute a “statutory power of decision”, the NZSE’s power to enter listing contracts had to be specifically conferred by statute. It was not sufficient to ground an application for judicial review under the Judicature Amendment Act that the contracting power fell within the NZSE’s statutory function pursuant to section 4. Woodhouse P said at 707:

“Parliament could never have intended that any corporate body recognised by statute or owing its existence to a specific or general statute such as the Companies Act could have all its commercial operations subject to constant judicial review.”

As a consequence, the court held that a decision of the NZSE to delist a company was not reviewable under the Judicature Amendment Act.

The *NZSE* decision has been cited with approval on a number of occasions in support of the proposition that a body does not become subject to judicial review simply because it owes its existence to statute. The Court of Appeal in *Mercury Energy Limited v Electricity Corporation* applied this line of reasoning in holding that Electricorp’s decision to cancel its supply contract with Mercury Energy was not justiciable.¹²⁰

That aspect of the Court of Appeal’s decision was overturned by the Privy Council on appeal. Lord Templeman held that the contracting actions of Electricorp, a body established by the State Owned Enterprises Act 1986, were in principle amenable to judicial review both under the Judicature Amendment Act 1972 and under the common

¹¹⁹ [1984] 1 NZLR 699.

¹²⁰ [1994] 1 NZLR 551, 560.

law. The Privy Council inferred that Electricorp's power to determine contracts was a "statutory power of decision" notwithstanding the State Owned Enterprises Act did not specifically grant contracting powers. It was sufficient that contracting to supply bulk electricity fell within the sphere of activity designated to Electricorp by statute.

Lord Templeman made no reference to the *NZSE* decision. However, it is directly contrary to the statements of Woodhouse P in that case. It can be argued that, as a result of the Privy Council's decision, the scope of the Judicature Amendment Act is expanded to catch bodies established under statutes which merely confer a function or sphere of operation rather than restricted to specific statutory powers.¹²¹ Further support for this proposition can be found in comments by Cooke P in two Court of Appeal decisions of the same name.¹²² In both decisions, the second time in direct response to comments made by Woodhouse P in the *NZSE* decision, Cooke P took the opportunity to assert that a statutory body can be in a different position from a private citizen when it comes to the exercise of contractual rights:¹²³

"I have no doubt that in connection with the exercise of contractual rights a statutory body can be in a different position from a private citizen. For instance, as to the entering into or cancellation of a contract, the statute expressly or implicitly may require certain considerations to be taken into account or may exclude others. If so, statutory powers of decision will be involved. ... Unfettered discretion is wholly inappropriate to a public body. Apart from any other express or implied restraint, the requirement of good faith is invariable."

However, the Privy Council in *Mercury Energy v Electricity Corporation*¹²⁴ then went on to indicate that courts should be slow to interfere in decisions of bodies such as Electricorp which, though established by statute, had a pronounced commercial flavour. Lord Templeman stated:

"It does not seem likely that a decision by a state-owned enterprise to enter into or determine a commercial contract to supply goods or services will ever be the subject of judicial review in the absence of fraud, corruption, or bad faith."

In light of the Privy Council's decision, there may be fresh grounds for arguing that the NZSE exercises a "statutory power of decision" and therefore may be amenable to judicial

¹²¹ M Chen "The Reconfiguration of the State and the Appropriate Scope of Judicial Review" J Boston *The State Under Contract* (Bridget Williams Books, Wellington, 1995).

¹²² *Webster v Auckland Harbour Board* [1983] NZLR 646; and *Webster v Auckland Harbour Board* [1987] 2 NZLR 129.

¹²³ See above n122, at 31.

¹²⁴ See above n120.

review under the Judicature Amendment Act. However, it appears that such an action will only lie if there is evidence of fraud, corruption, or bad faith.

B Common law

The Court of Appeal in *New Zealand Stock Exchange v Listed Companies Association* left open the question of whether the delisting of a company might be reviewable by way of the prerogative writs, though it noted that there were "considerable difficulties with that rather amorphous suggestion".¹²⁵

Two subsequent English Court of Appeal decisions concerning the justiciability of decisions of the London City Panel on Takeovers and Mergers ("City Panel") can be invoked in support of the proposition that the NZSE may be subject to judicial review on the common law grounds.¹²⁶ *R v Panel on Takeovers and Mergers, ex parte Datafin plc* ("*Datafin*") involved a disputed takeover of a printing company. The Datafin camp alleged that their rivals had breached the takeover rules instituted and administered by the City Panel, however the City Panel dismissed the allegations. Datafin sought judicial review of the City Panel's decision.

The City Panel was not established under statute or by executive power, but was set up as a self regulatory body by market participants. Furthermore, the rules of the City Panel do not have the force of law, or even contractual force. Nevertheless, it was accepted that the Panel wielded significant power. Companies in breach of the rules of the City Panel could be delisted. Persons who failed to observe the rules could be prevented from trading on the exchange.

The Court of Appeal held that the decisions of the City Panel were capable of judicial review notwithstanding that they did not have any basis in statutory or prerogative power. Rather than focusing on the source of the power of decision, the Court of Appeal concentrated on the nature of the function being performed by the City Panel. It was accepted that bodies performing "public" duties or exercising powers that could be characterised as "public" may be subject to judicial review, even though the powers had no basis in statute or prerogative power. The court concluded that the City Panel was performing a "public" duty on the basis that it:

¹²⁵ See above n21, at 707.

¹²⁶ *R v Panel on Takeovers and Mergers, ex parte Datafin plc* [1984] 1 All ER 564; and *R v Panel on Takeovers and Mergers, ex parte Guinness plc* [1989] 1 All ER 509.

- (a) performed a regulatory role in that it had been incorporated to control commercial activity in this area;
- (b) was able to affect the interests of citizens, regardless of whether or not they had consented to the jurisdiction of the City Panel; and
- (c) although not established by the government, formed an integral part of the governmental regulation of the market, to the extent that the government was said to rely of the City Panel enforcing its rules. The courts have applied a kind of "but for" test here which in this case asked "but for the existence of the City Panel, would the government have to step in to regulate that area?". An affirmative answer indicates that the body is performing a public duty.

The Court of Appeal was also influenced by the fact that the substantial powers of the Panel were not able to be controlled by private law remedies of contract or tort. The Court of Appeal later reaffirmed its decision in *Datafin in R v Panel on Takeovers and Mergers, ex parte Guinness plc*¹²⁷ ("Guinness").

The *Datafin* and *Guinness* decisions can be invoked in support of an application for judicial review of the NZSE on the basis that the NSZE weilds a "public power" and performs a public duty. The NZSE, like the City Panel, performs a critical regulatory role that "but for" its existence would have to be regulated by some other body, possibly governmental. The NZSE's power to delist a company means it is able to affect the interests of citizens, and the wider economy.

There is also academic support for the policy argument that a stock exchange is a body of such position and power that its listing decisions ought to be reviewable.¹²⁸ It could also be argued that the legal position should be reviewed in the light of section 27(2) of the New Zealand Bill of Rights Act 1990.¹²⁹

¹²⁷ See above n126.

¹²⁸ See D Brewster "Decisions under the Australian Stock Exchange Listing Rules: Review Under the Administrative Decisions (Judicial Review) Act" (1991) 9 C& SLJ 377. Australia's listing rules have greater statutory recognition than the New Zealand rules, even though they continue to be regarded as deriving their authority principally from contract.

¹²⁹ Section 27(2) of the New Zealand Bill of Rights Act provides that "Every person whose rights, obligations or interests protected or recognised by law has been affected by a determination of any Panel or other public authority has the right to apply, in accordance with law, for judicial review of that determination."

A recent Australian decision held that the decisions of the ASX were not amenable to judicial review under the Australian equivalent of the Judicature Amendment Act. However, the court expressly left open the possibility that the ASX might be subject to judicial review via the prerogative writs.¹³⁰

Recent English case law has required more evidence of direct involvement by the government or other public body in the exercise of the "public function", for example, establishment by statute, rather than simply applying the "but for" test applied in *Datafin* and *Guinness*. In *R v Disciplinary Committee of the Jockey Club, ex parte His Highness the Aga Khan*¹³¹ the Court of Appeal denied an application for judicial review of the Jockey Club, a private sporting body, notwithstanding striking similarities between the functions of the Jockey Club and the City Panel. However, it is submitted that, given the statutory basis of the NZSE, the "but for" type analysis applied in *Datafin* and *Guinness* is not required to establish this link.

However, in contrast to *Datafin* and *Guinness* it may be possible for listed companies in New Zealand to control unconscionable conduct by the NZSE via a private law action for breach of contract, or some other equitable obligation. Therefore, there may not be the same pressing need to subject the NZSE to public law, as well as private law constraints.

Furthermore, the Court of Appeal in *Datafin* and *Guinness* indicated that, although it is able to review the City Panel's interpretative decisions, the court is more likely to give declaratory rather than substantive relief. Furthermore, the court indicated that relief would be limited to future cases, and that it would not grant any substantive relief to parties in relation to the instant proceedings. The only exception to this self-imposed constraint is where the City Panel had acted unfairly. It can be argued that extending public law judicial review to the NZSE is unnecessary, because identical remedies may be obtained in private law judicial review.

C Conclusions

The comments of the Privy Council in *Mercury Energy v Electricity Corporation*¹³² and Cooke P in the *Webster v Auckland Harbour Board*¹³³ provide at least a basis for

¹³⁰ *Chapmans Ltd v ASX Ltd (No 2)*, above n118.

¹³¹ [1993] 2 All ER 853.

¹³² See above n120.

¹³³ See above n122.

arguing for a reconsideration of the approach of the Court of Appeal in the *NZSE* decision. Alternatively it could be argued that, even if the *NZSE* decision was correct in holding that the *NZSE*'s decisions on its listing rules are not reviewable under the Judicature Amendment Act they are nonetheless less capable of review by prerogative writ based on *Datafin* and *Guinness*.

Notwithstanding the above, the prospects of succeeding with such arguments cannot be put very high. The *NZSE* decision is directly on point. The Privy Council's comments in the *Mercury Energy v Electricity Corporation*¹³⁴ are clearly relevant, but the case can readily be distinguished by reference to the historical antecedents of the bodies in question: Electricorp (now ECNZ) is an offshoot of a former Government department whose existence has always been regulated by statute and the prerogative, whereas the *NZSE* has a pedigree as a private body exercising its powers by contract well before the statutory recognition it was given in the Shareholder's Amendment Act 1981. Moreover, the comments by Donaldson MR in the *Datafin* and *Guinness* cases were essentially obiter dicta (and therefore not binding) in as much as the court decided on both occasions that there had been no defect in the exercise of the powers under consideration. Cooke P's comments in *Webster v Auckland Harbour Board*¹³⁵ decisions were also clearly dicta.

A further consideration to be taken into account is the lesser judicial activism that has been apparent across the board in recent Court of Appeal decisions and more particularly in relation to such matters as judicial review. There have been direct comments by some judges that it is less appropriate in today's deregulated environment for the courts to intervene as readily as they were disposed to when the Government was more heavily and directly involved in the economy.¹³⁶

It is also important to note the limitations placed by the court in *Datafin* and *Mercury Energy v Electricity Corporation*¹³⁷ on the relief available in judicial review of a commercial organisation. It is likely that the same results can be achieved via an action for breach of contract or trust, a so called "private law" judicial review.

¹³⁴ See above n120.

¹³⁵ See above n122.

¹³⁶ See Richardson J *Economics and the Law: the Courtroom Reality* New Zealand Law Society Seminar (1990); cited with approval by Williams J in *Maddaver v Umawera School Board* [1993] 2 NZLR 478, 507-8).

¹³⁷ See above n120.

X CONCLUSIONS

It is not intended here to summarise the various conclusions drawn, or left “undrawn”, in this paper. The object of this paper was not to draw any overriding conclusions about the Rules, or the NZSE, but merely to test a number of aspects of the Rules for validity. The overall impression is that, when examined closely, various aspects of the Rules do not have the effect they purport to have.

A clear example is the power of the NZSE to issue rulings on the section 4 provisions. Another example, is the NZSE’s ability to determine disputes by issuing a ruling after the breach has occurred. Both, it can be argued, are ineffective to determine the dispute. The remaining question then is: does this reduce the ability of the NZSE to enforce the Rules? Arguably not, because the NZSE relies on the threat of delisting and not remedies in contract to procure compliance. However, although it may seem trite to say it, it does reduce the ability of the NZSE to determine disputes. Shareholders not bound by the rulings of the NZSE could choose to resolve disputes over the Rules in court, rather than via the faster and cheaper method provided by the NZSE. As a result, the benefits of the self-regulatory system are threatened.

Finally, it is submitted that, although there are good grounds to support an application for judicial review of the NZSE, a case on the point is unlikely to arise. This is because of the nugatory remedies available to applicant’s for review of commercial type bodies.

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