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PRE-EMPTIVE RIGHTS ARTICLES

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PART I

INTRODUCTION

This paper is concerned with pre-emptive rights. These are designed to keep control of companies in existing hands by restricting the transfer of shares to their present members.

Directors commonly have various powers to refuse registration of a transfer. Articles 23 - 25 of Table A [(1)] provide a limited right to refuse registration of a transfer. Most private companies have provisions in their articles that empower the directors to refuse a transfer either without reason or for the reason stated.[(2)]

Pre-emptive rights provide a greater degree of regulation by restricting the right of transfer (and sale) to other members of the company. Although pre-emptive rights articles may differ in wording, it will usually be possible to distinguish the following features:-

(1) A prohibition on transfer to non-members while any other member is willing to purchase the shares.

(2) A shareholder will be required to give notice to the company of his desire to sell or transfer the shares.

(3) A procedure by which the shares are to be offered to the other shareholders.

(4) Compulsory transfer of the shares if a purchaser is found.

(5) A method to determine the value of the shares in the case of disagreement.

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(1) See third schedule to Companies Act 1955

(2) In Britain section 28 (1)(a) of the Companies Act requires private companies to have restrictions on transfers in their articles

(6) A power given to some named officer to execute a transfer if the vendor/shareholder makes default in doing so.

(7) Permission for the shareholder to sell his shares to outsiders if no other shareholder wishes to purchase them.

This summary follows closely the standard form pre-emptive rights article set out in Dale & Sclater.[1] Comparison may be made with the pre-emptive rights article considered in Lyle & Scott v Scott's Trustees.[2] This case will receive detailed attention in this paper. An abbreviated version of the latter article is as follows:-

> " ... no registered shareholder of more than one per centum of the issued ordinary share capital of the company shall, without the consent of the directors, be entitled to transfer any ordinary share for a nominal consideration or by way of security and no transfer of ordinary shares by such a shareholder shall take place for an onerous consideration so long as any other ordinary shareholder is willing to purchase the same at a price which shall be ascertained by agreement between the intending transferor and the directors and, failing agreement, at a price to be fixed by the auditor of the company ... Any such ordinary shareholder who is desirous of transferring his ordinary shares shall inform the secretary in writing of the number of ordinary shares which he desires to transfer ..."

A pre-emptive rights article as above should be distinguished from the type of article that was under consideration in Gold v Penny.[3] The articles here had the format of the usual

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(1) Private Companies in New Zealand: (1968) p.87-88 See Appendix I

(2) (1959) A.C. 763 A full version of the article is set out in Appendix I post.

(3) (1960) N.Z.L.R. 1032; cf. the precedent in Anderson & Dalglish: "The Law Relating to Companies in New Zealand" (2nd Ed.) 1957, p.810,811.

pre-emptive rights article but the shareholders had no real right of pre-emption. The shares were to be sold to members of the company OR anyone else whom the directors approved.[1]

It is now proposed to examine some aspects of pre-emptive rights articles in more detail.

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(1) The article is set out in Appendix II

PART II

THE MEANING OF "DESIROUS OF TRANSFERRING" AND "DESIROUS OF SELLING" AS USED IN PRE-EMPTIVE RIGHTS ARTICLES

Some pre-emptive rights articles, as in Lyle & Scott Ltd.v Scott's Trustees[1] provide that when a shareholder is 'desirous of transferring' his shares, he must inform the company. In other articles, e.g. Gold v Penny[2] the equivalent wording is 'desirous of selling'. The meaning of each of these expressions will be considered in turn.

A. "DESIROUS OF TRANSFERRING"

As has already been mentioned, in Lyle & Scott Ltd. v Scott's Trustees[3] the pre-emptive rights clause provided (inter alia) that any ordinary shareholder -

> "who is desirous of transferring his ordinary shares shall inform the secretary in writing of the number of ordinary shares which he desires to transfer."

The respondents in this appeal accepted an offer to purchase their shares in the appellant company. The offer was made through a firm of solicitors acting for an undisclosed principal who later turned out to be Mr. Hugh Fraser, a millionaire businessman. The offer had become unconditional upon the acceptance of 75% of the ordinary shares then in issue. The vendors agreed to deliver forms of proxy in favour of the purchaser and authorise him to use them. They were further required to deliver up their share certificates in respect of their shares in the company which they had agreed to sell and to sign the relative transfers when called upon to do so in exchange for the price. The purchase price was, in fact, handed over in exchange for the share certificates and completed forms of proxy were delivered. However, at Fraser's request, no void or defective transfers were actually delivered at this stage.

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(1) (1959) A.C. 763
(2) (1960) N.Z.L.R. 1032
(3) (1959) A.C. 763

Thereupon, the company initiated an action to seek a declaration that the respondents were, in fact, 'desirous of transferring' the shares and that they were bound to inform the secretary of the company of this fact in accordance with the articles. A further order was sought to compel the respondents to inform the secretary accordingly.

Both the Lord Ordinary and the First Division of the Court of Session held that although a breach of the articles had occurred by the shareholders entering into the agreement with Fraser, the Company must fail to obtain its remedy as the shareholders had not done an overt act. The giving of notice to the company could be such an act.[1]

The House of Lords took a different view. Their Lordships held that a person who has agreed to sell his shares (and has received the purchase price) must be deemed to be 'desirous of transferring' his shares and, consequently, was bound to implement the articles by informing the secretary of the number of shares to be sold. The respondents were further ordered, the agreement still standing, to inform the secretary accordingly.

The basic argument of the respondents was that the 'transfer' and 'transferring' in the last part of the article only applied to a complete transfer by acceptance of deeds of transfer. Consequently, it was argued that as long as one is not desirous of having a transfer registered a person is entitled to agree to sell his shares without the article coming into operation.

Viscount Simonds did not wish to be categorical about the meaning of 'transfer'. However, in a passage that deserves to be quoted in full he gave his reasons for holding that the appeal must succeed:-

"For since it is the admitted fact that they entered into the agreement for sale of their shares and have received

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(1) See: Rice: "The Effectiveness of a Pre-emptive Rights Clause in a Company's Articles" (1959) 23 Conveyancer & Property Lawyer, 42

and retain the price, it follows that, whether or not they have yet done all that they ought as vendors to do, they hold the shares as trustees for the purchaser. They are bound to do everything that in them lies to perfect the title of the purchaser. They cannot compel the company to register him as the holder of the shares, but everything else they must do, and it is straining credulity too far to suppose that everything else would not already have been done, if it had not been hoped to gain some tactical advantage by delay. In my opinion, it is not open to a shareholder, who has agreed to do a certain thing and is bound to do it, to deny that he is desirous of doing it. I wish to make it quite clear, for it goes to the root of thd matter, that I regard Scott's trustees as desirous of transferring their ordinary shares unless and until their agreement with Mr. Fraser has been abrogated. Of this at least one acid test would be the return by them of the price they have received."[1]

Later on Viscount Simonds came back to the same point when he said:-

"What he (the shareholder) cannot be permitted to do is to adhere to his contract and in the same breath assert that he does not desire to transfer his shares. It may well be that he thus places himself in a position of disadvantage vis-a-vis the purchaser with whom he has contracted. But it cannot be denied that he has done so with his eyes open."[2]

One matter should be mentioned in connection with the first passage quoted above. Viscount Simonds bases his judgment on the finding that the respondents must be 'desirous of transferring' when they become trustees for the purchasers upon them entering into the agreement for sale and purchase. At present it is not altogether clear whether any equitable interest can pass if a contract is entered into in defiance of such registration provisions in the

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(1) ibid 774

(2) ibid 775-776

articles. There is even some authority for the view that such an agreement is a nullity. Both these areas are dealt with later in this paper,[1] but for present purposes it will suffice to examine the possibility of a finding that the respondents are 'desirous of transferring' if it should be held that either no equitable interests arise under such a contract and/or the contract is a nullity.

In the first situation, the vendor/shareholder is still presumably bound to do everything to perfect the title of the purchaser while the contract is still in existence. If the writer's supposition is correct, then it is submitted that the reason for finding that a vendor is desirous of transferring must remain. The reason for preventing a person denying that he is 'desirous of transferring' will be especially strong if he exhibits an intention to retain the purchase price which may have changed hands. As Viscount Simonds pointed out[2] a shareholder may abandon his desire by terminating the existence of the overt act signifying the existence of the desire. The example he gave was the abrogation of the contract of sale and purchase; the "acid test" would be the return of the purchase price.[3]

Even assuming that the contract is a nullity, it still may be possible to find grounds for holding that a shareholder must be deemed to be desirous of transferring. It was assumed in Lyle & Scott v Scott's Trustees that the vendor/shareholder could annul the contract.[4] Presumably the purchaser could also repudiate the agreement. If, however, the parties act on the assumption that the agreement is still in existence and show no sign of repudiating it, the vendor could be said to be 'desirous of transferring' because of the inconsistency of the parties adherence to the purported agreement with the vendor's denial of his intention to divest himself of his shares. As a practical matter a purchaser would be unlikely to continue an arrangement that can never achieve any legal effect. If, in such a case, he was still anxious to obtain control or a voice in a company, he would seek some other method of obtaining this result.

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(1) See Part IV

(2) ibid 774-775. See also @ 780 per Lord Reid; 786 per Lord Keith

(3) ibid 774

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(1) See Part IV

(2) ibid 774-775. See also @ 780 per Lord Reid; 786 per Lord Keith

(3) ibid 774

(4) See Stevenson v Wilson (1907) S.C. 445 @ 455 per Lord President. This ground for repudiation was doubted by Tamberlin in (1960) 3 Sydney Law Review, 560 @ 564-565

Lord Tucker delivered a brief but similar judgment to that of Viscount Simonds. His Lordship pointed out the existence of the agreement for sale and purchase of the shares and continued:-

> "They thereby bound themselves to take every step which is required from the holder of a share who desires to transfer to another the legal and equitable title to his share. They have received from Mr. Fraser the agreed purchase price and the the contract still subsists. By so doing they have, in my view, beyond question taken an overt act signifying their desire to transfer their shares within the meaning of article 9 of the articles of association of Lyle & Scott Ltd."[1]

The speech of Lord Reid dealt specifically with the meaning of the words "transferring" and "transfer" in the relevant parts of the pre-emptive rights article under consideration. He rejected the limited meaning that was sought to be given to the words by the respondents.[2] He held that "tranfer" should not be taken to be limited to the actual process of registration of an interest of transfer:-

> "Transferring a share involves a series of steps, first an agreement to sell, then the execution of a deed of transfer and finally the registration of the transfer. The word transfer can mean the whole of those steps. Moreover, the ordinary meaning of "transfer" is simply to hand over or part with something, and a shareholder who agrees to sell is parting with something."[3]

Lord Reid looked at the context in which the word "transfer" was used:-

> "I have already referred to the obvious purpose of article 9; to give the other shareholders an option to purchase shares

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(1) ibid 782

(2) ibid 778

(3) ibid 778

which any shareholder desires to part with. To be effective it must come into operation before that shareholder agrees to sell to anyone else, and the last part of the article clearly contemplates this." (1)

Lord Reid thus takes a different approach to Lord Simonds. The latter did not express a concluded opinion upon the meaning of the word "transfer". He was clearly of the view that in any circumstances the present transaction would infringe the pre-emptive rights article - the vendors were committed to a course that would lead ultimately to the registration of a transfer. The fact that the parties purposely did not execute a transfer did not alter the situation. While Lord Reid finds alternative grounds for his judgment he would also agree with this conclusion:-

"But in my judgment, a person who has agreed to sell with a view to a transfer at some future date cannot be heard to say that he is not desirous of transferring the shares merely because it suits him and the purchaser to delay execution and presentation of the transfers." (2)

The purpose of the article in Lord Reid's opinion is to give other shareholders an option to purchase the shares concerned. While his Lordship did not consider the point it would seem that an option to purchase would in his view come within the contemplation of the article. The shareholding giving the option is 'parting' with something. His course of action will in certain circumstances lead to a transfer of shares. A contract of first refusal appears to fall into a different class. The shareholder has not obliged himself to transfer, sell or part with his shares.

Lord Keith also specifically considered the question of the correct meaning of "transfer" within the last part of the pre-emptive

(1) ibid 778
(2) ibid 779

rights article. He thought that it was used in a broad sense of "dispose of or sell". He then went on to express the opinion that even if transfer was to be given a restrictive meaning it did not follow that a shareholder does not express his desire until the instrument of transfer is presented for registration.[1] Here the respondents had done everything but execute a formal instrument of transfer. They had even executed proxies in favour of the purchasers' solicitors. He went on:-

> "I am clear that there is here a clear breach of the positive part of the article requiring an intending transferor to inform the secretary in writing of the number of shares he wishes to transfer and an invasion of the rights of the shareholders under the article ... Standing a completed and unrepudiated contract of sale and acceptance of the purchase money the defenders cannot be heard to say that they are not desirous to transfer their shares because they chhose for some reason or other to hold up completion of the document of transfer or wish to sell only to a particular person." [2]

This case is an interesting example of judicial concern to find a solution to remedy what would otherwise be an unfair result.[3] The Scottish Courts were concerned that the granting of relief to the company would be, in effect, to order a compulsory sale of the respondents shares.[4] While they had held that there was no "overt act" exhibiting a desire to transfer the shares [5] the House of Lords were not prepared to give such a restrictive interpretation to the article. While the giving of notice would be a clear method of showing that one was desirous of transferring it was not the only

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(1) ibid 785

(2) ibid 786

(3) See casenote by Tamberlin in 1960 3 Sydney Law Review, 560 @ 563

(4) See (1959) A.C. 763 @ 779 per Lord Reid

(5) See 1958 S.C. 230 @ 244 per Lord President; see also Lord Sorn @ 250.

method by which a desire to transfer shares could be established.[1] Viscount Simonds said:-

> "I cannot, for instance, accept the view of the Lord President that there has been no overt act which could enable the company to require the defenders to follow out the procedure in the article, nor do I find it easy to reconcile this part of his judgment with his decision that Scott's Trustees had infringed the article by transferring or purporting to transfer their shares to Mr. Fraser. What more conspicuous overt act, evincing the desire to transfer, could there be than this?"[2]

Lord Reid responded in a similar manner to the argument that the desire to transfer had not been evinced by any overt act:-

> "But if the respondents' admitted actions were in breach of their obligations, I do not see that it matters whether or in what sense they were "overt". I would not hold a desire to transfer proved by some equivocal words or acts. But here it is impossible that the respondents could have done what they did unless they desired to transfer: there is no suggestion of any other reason why they should have contracted with Mr. Fraser."[3]

The relief granted in the House of Lords made it clear that the respondents were only obliged to give notice to the secretary of the company if the agreement still stood. However, their Lordships were not prepared to interpret the pre-emptive rights article in such a way that the respondents were the sole arbiters of whether they were desirous of transferring their shares.

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(1) See (1960) 3 Sydney Law Review @ 563

(2) ibid 775

(3) ibid 779

This is clearly expressed in the judgment of Lord Reid. It had been argued that the pre-emptive rights article was a means of selling shares and not a provision compelling transfer. He gave qualified acceptance to this proposition. It was true that no action could be taken against the person who merely said that he wished to sell his shares or did something which exhibited this intention. Such behaviour without more was beyond the purview of the court. It was, however, different if what is done amounts to a breach of the shareholders obligations under an article:-

> "Unless some action can then be taken to assert the other shareholders' rights under the article there is a wrong without a remedy."(1)

Lord Keith of Avonholm was equally candid in the reasons for interpreting the article so as to provide the appellants with a remedy here. He rejected the view taken by the Lord Ordinary of the First Division of the Court of Session that it is for the respondents alone to decide whether they would set the machinery in motion under Article 9 by informing the company secretary of their intention to sell:-

> "There must reside in the courts some power to enforce observance of the article, unless the rights of the shareholders are to be defeated, and the appropriate step at this stage, in my opinion, is to ordain the defenders to give notice to the secretary of their desire to transfer the number of shares which they have contracted to sell to their purchaser."(2)

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(1) ibid 779

(2) ibid 786

In the result, the remedy given avoided the respondents being bound to sell their shares should they decide to rescind their contract.

Lyle & Scott Ltd. v Scott's Trustees was discussed by the New Zealand Court of Appeal in Gold v Penny[1] which was decided in the following year. The so called pre-emptive rights article here was considerably different from that considered in the former case.[2] As Gresson P. said in the Court of Appeal, the 'rights of pre-emption' conferred by the article in question here did not give a right of first refusal to the shareholders (or anyone else) and thus the term was a misnomer.[3] There were a number of distinguishing features in this case [4] but the Court of Appeal did not cast doubt upon the correctness of the decision of the House of Lords in Lyle & Scott Ltd. v Scott's Trustees.

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(1) (1960) N.Z.L.R. 1032

(2) see Appendix II

(3) see (1960) N.Z.L.R. 1032; 1046. Also see 1058 per Cleary & Hutchison J.J.

(4) ibid 1061 per Cleary and Hutchison J.J.

B. "DESIROUS OF SELLING"

Some articles provide for a transfer notice to be given to a company whenever a shareholder is 'desirous of selling'. In Lyle & Scott Ltd. v Scott's Trustees both Lord Reid and Lord Keith of Avonholm were of the opinion that the word transfer as used in the pre-emptive rights article discussed in that case was used in the sense of "to dispose of or sell" or "to hand over or part with something".[1] Clearly an agreement to sell is an unequivocal act showing a desire to sell and a desire to transfer.[2]

The question arises as to what other conduct would be sufficient to exhibit a desire to sell. In Lyle & Scott Ltd. v Scott's Trustees Lord Reid said:-

> "I would not hold a desire to transfer proved by some equivocal words or acts."[3]

Lord Reid said that it was impossible in that case that the respondents could have done what they did unless they desired to transfer their shares. Later he says:-

> "No action can be taken against a shareholder who merely says that he wishes to sell or does somethings which shows that that is his intention. But, when he goes further and does something which is a breach of his obligations under the article, the position appears to me to be quite different."[4]

Lord Reid would, therefore, distinguish between an unequivocal act showing that the shareholder is 'desirous of transferring' and something short of this. The same principle applies (mutatis mutandis) to the sufficiency of a desire to sell. While the desire of selling must be established by unequivocal acts, Lord Reid did not consider it mattered whether the acts were overt or not.[5]

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(1) (1959) A.C. 763 @ 785 per Lord Keith

(2) ibid 775 per Viscount Simonds

(3) ibid 779

(4) idem

(5) ibid 779

The writer finds it difficult to visualise the exact nature of the acts which could be unequivocal unless embodied in a sale and purchase agreement. It is submitted that negotiations for the purchase of shares without more would not be sufficient. An option to purchase shares is a difficult problem.[1] No sale is achieved until the option is exercised. If the person giving an option is regarded as being 'desirous of selling' the company or shareholders could obtain the same remedy as the company in Lyle & Scott v Scott's Trustees obtained. The person giving the option would be bound to set the procedure under the pre-emptive rights article in motion in the event of the continued existence of the option. There does not appear to be any injustice involved in compelling the vendor shareholder to comply with the articles without waiting for an acceptance of the option by the proposed purchaser. By giving an option the shareholder has shown the intention to sell. In the writer's opinion the fact that the substantive contract may never eventuate should not be treated as a relevant consideration.

The discussion so far concerning options to purchase shares has proceeded upon the assumption that the option has been given for consideration or is by deed. An option given without consideration and which is not by deed cannot be enforced. It can be withdrawn with impunity at any time. Whether the courts would treat this as showing an unequivocal desire to sell shares is open to doubt. The vendor is not bound to take all steps to complete the contract. In Lyle & Scott Ltd. v Scott's Trustees Lord Simonds & Lord Tucker in particular relied upon the fact that the vendors in that case were bound to do everything to complete the contract and perfect the title of the purchaser. This is not the situation here.

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(1) See Halsbury: Laws of England 4th Ed. Vol.9 Para. 235

In the present circumstances the shareholder would not be *bound* to carry out his contract. No consideration has passed. He may intend to do so and there would no doubt be evidence of his acts exhibiting this intention. However, in the absence of a binding contract *Lyle & Scott Ltd. v Scott's Trustees* is distinguishable in this regard. It is submitted that the continued existence of an unenforceable option should not result in a shareholder being compelled to comply with the pre-emptive rights articles. While in *Lyle & Scott Ltd. v Scott's Trustees* there was an obvious inconsistency between the respondents' claim that they were not 'desirous of selling' and the continued existence of an executed contract, in the present situation the shareholder has not given any consideration.

The writer finds support in this conclusion in an article in the Sydney Law Review,(1) where the problem of what acts will unequivocably indicate an intention to sell is discussed.

> "In solving such a problem it may be that the courts would have to draw a finer distinction between the legal factum which would bring the article into operation and the mere abstract "wishing" or "intending" to sell which would not."(2)

One other type of arrangement that is clearly outside the contemplation of the pre-emptive rights article is a contract of first refusal.(3) The view has already been expressed that such a contract would not exhibit a desire to transfer even upon Lord Reid's understanding of the term. The same reasoning is applicable here. Such a contract does not exhibit any present desire to sell. It simply binds a person to sell to a particular person should he ever wish to sell.

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(1) (1960) 3 Sydney Law Review 560 @ 564

(2) ibid 564

(3) See Halsbury: 4th Ed. Vol 9 Para. 236

PART III

REVOCATION OF THE NOTICE OF INTENTION TO SELL AND/OR TRANSFER SHARES

In the previous part of this paper, it has been mentioned that while the respondents in Lyle & Scott v Scott's Trustees [1] were held to be desirous of transferring their shares and thus could be compelled to give the requisite notice to the company, they were entitled to say that they were no longer desirous of selling their shares if they annulled their contract with Fraser.

This part of the paper is concerned with the question whether the notice to the company can be revoked once it has been given. This did not arise directly for decision in Lyle & Scott v Scott's Trustees but it was the subject of comment by some of their Lordships. However, reference should first be made to the earlier Scottish cases of Smith v Wilson [2] and Stevenson v Wilson. [3] Both these cases arose out of the same complex situation. Wilson was a trustee in sequestration and advertised for sale some shares in J.M. Smith Ltd. As appears from the later case, Stevenson agreed to buy the shares. One of the conditions upon which the contract was founded was that the company did not have to accept any transferee.

The articles provided that any holder of ordinary shares who wished to sell them had to offer them to the company at the price at which he wished to sell and the company had to take them at that price or intimate the offer to other shareholders who could lodge offers within fourteen days.

Wilson offered the shares to the company before taking any further steps pursuant to his conditional contract with Stevenson. He then withdrew his offer before any one of the shareholders had written to the company offering to purchase the shares. The Lord

(1) (1959) A.C. 763

(2) 1901 9 S.L.T. 137

(3) 1907 S.C. 445

Justice Clerk[1] held that Wilson was entitled to withdraw his offer at any time before it was accepted. He further pointed out that if the defendent attempted to effect the sale of the shares to Stevenson without complying with the articles, the company could refuse to register the transfer.

Stevenson did not pay the price for the shares.[2] Wilson sued for payment and obtained an order for payment. The transfers were executed but the company refused to register them. Stevenson then brought the second reported action. The company had refused to pay dividends on the shares to Stevenson and Wilson had refused to receive them and pay them to Stevenson.

The First Division of the Court of Session upheld the judgement of the Lord Ordinary to the effect that so long as Wilson did not annul the bargain by returning the purchase price, he must fulfil his obligations as trustee. The Lord President said:-

"When there is a stipulation in the articles of the company which allows the directors of the company to refuse at their own hand any particular transferee, then A and B, who are contracting, do so with their eyes open, and knowing that it may be the case that B will not be accepted as transferee. It still becomes the duty of B, if he cannot get the defenders to register him, to find a transferee whom the defenders will register in order to free A, and I think, if he is entirely unable to do that, A can bring the bargain to an end. But I think he could only do so in the ordinary way by annulling the bargain - that is, giving the money he had got from B and bringing matters to their entirety.[3]"

In Lyle & Scott v Scott's Trustees[4] Lord Reid used the cases just mentioned to support the propositions that firstly any notice that was to be given by the respondents was not irrevocable and

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(1) 1901 9 S.L.T. 137

(2) See 1907 S.C. 445, 454

(3) ibid 455

(4) (1959) A.C. 763

secondly they could annul their bargains with Mr. Fraser.[1] He rejected an interpretation of the pre-emptive rights article that would prevent the respondents from avoiding a compulsory sale of their shares:-

> "That article requires a notice to be given by any shareholder who desires to sell his shares, but it does not make such a notice irrevocable. No doubt it becomes irrevocable when the procedure following on it results in a contract between the shareholder giving the notice and another shareholder who has made an offer for the shares ....But until that stage is reached it appears to me that it is open to the shareholder who gives the notice to withdraw it..." [2]

Viscount Simonds said that he did not dissent from the view expressed in Smith v Wilson [3] that notice to a company may be "timeously" withdrawn.[4] Lord Keith also considered Smith v Wilson [5] and Stevenson v Wilson.[6] He did not doubt their correctness but pointed out that the specific questions arising in the present case were not dealt with in thos cases.

In Beynon v Acme Engineering Limited et al [7] a shareholder gave notice of his intention to sell his shares to a company in accordance with the particular pre-emptive rights article concerned. The next day he withdrew his notice. The company solicitors took the view that the notice was irrevocable. The board of directors continued to act in accordance with the pre-emptive rights articles and authorised one of its members to execute the transfer. The plaintiff thereupon sought an injunction to restrain the company and the members of its board from further dealing with his shares.

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(1) ibid 781
(2) ibid 780
(3) 1901 9 S.L.T. 137
(4) (1959) A.C. 763 @ 775
(5) 1901 9 S.L.T. 137
(6) 1907 S.C. 445
(7) (1945) N.Z.L.R. 729

Myers C.J. pointed out that while it was not uncommon for a pre-emptive rights article to provide that the notice to the company is to be irrevocable, the present articles did not contain any such provision. He contrasted the earlier case of Edmonds v T.J. Edmonds Ltd.[1] where he thought that there must have been a provision in the articles in that case that the 'transfer notice' was to be irrevocable except with the sanction of the directors. The writer has not been able to find any mention of an express provision to this effect in the Reports of Edmonds v T.J. Edmonds Ltd[2] but it may be said that the articles raise an implication of irrevocability.

Myers C.J. did not refer to the earlier case of Smith v Wilson[3] but came to the same conclusion. He held that there was no implication of irrevocability arising from the Acme Engineering Ltd. articles and, therefore, the notice was revocable:-

> "It follows, however, in my opinion, that where there is no provision express or by necessary implication that the notice shall be irrevocable, the position is simply that of an ordinary agency, and if that is so, it seems to me that ... the notice ... was clearly revocable."[4]

In the Beynon case Myers C.J. held that on the facts there was no concluded contract made at a meeting of the shareholders held to discuss the plaintiff's notice. If such a contract existed it would not have been in accordance with the pre-emptive rights articles although his Honour was not adverse to the argument that the irregularity could be waived by the assent of all shareholders.

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(1) (1937) N.Z.L.R. 135 (S.C.) and 527 (C.A.)

(2) ibid

(3) 1901 9 S.L.T. 137

(4) (1945) N.Z.L.R. 729, 733

Since there was no concluded contract in breach of the articles, the main question involved in the Lyle & Scott case did not arise for decision here.

In conclusion, it may be said that a notice to the company be "timeously withdrawn" in the absence of any express or implied provision in the company's articles.[1] It is too late if any contract is concluded with other shareholders. Furthermore, in accordance with the obiter statements of the House of Lords in Lyle v Scott v Scott's Trustees [2] a shareholder will not be permitted to assert that the notice is revoked or withdrawn if they have not terminated their contract which is formed in breach of the articles.

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(1) see also Cohern & Sons Pty. Ltd. (1969) 2 N.Z.L.R. 593 NSWAR

(2) (1959) A.C. 763

Useful case on its facts
Revocation at 11th hour permissible

PART IV

THE POSITION INTER PARTES WHEN A TRANSACTION IS IN BREACH OF PRE-EMPTIVE RIGHTS ARTICLES

The House of Lords' decision in Lyle & Scott v Scott's Trustees[1] held that if the vendors of shares adhere to an agreement made in breach of the articles, they can be compelled to give notice to the company of their desire to transfer them. A company or (in some circumstances) its shareholders may sue to enforce the pre-emptive rights articles against other shareholders.

It is now proposed to consider the position inter partes. The company will not always insist on its rights. It may already be in the control of the person who is attempting to purchase shares in breach of the pre-emptive rights article.

The first case that should be mentioned is the decision of the House of Lords in Hunter v Hunter.[2] Their Lordships were (amongst other things) concerned with the validity of a transfer by way of security in breach of the pre-emptive rights article of the company concerned. The lower courts had not been unanimous in their views as to the effectiveness of the transfer.

Viscount Hailsham L.C. thought that the tra-saction in breach of the articles could have been regularised by the assent of all shareholders.[3] Lord MacMillan concurred in the Lord Chancellor's opinion.[4] A passage in Lord Russell of Killowen's opinion tends to support the view of Viscount Hailsham. On the other hand, Lord Atkin took an opposing view:-

> "The effect of Article 17 in my opinion is to provide the means and the only means by which a member of the company can form an agreement for the sale of shares, which can only be constituted by the act of a secretary as agent for seller and purchaser declaring a contract to be concluded at the price

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(1) (1959) A.C. 763

(2) (1936) A.C. 222

(3) ibid 248

(4) ibid 264

fixed by the auditor. That was not done in this case, and in my opinion no rights arose between the bank and Harry Hunter under any contract of sale either equitable or legal." [1]

Hunter v Hunter [2] was discussed in the Irish case of In Re Hafner; Olhausen v Powderley. [3] Black J. at first instance preferred the view that the transaction in question was valid between the parties although it was in breach of the pre-emptive rights articles. He thought that Hunter v Hunter probably turned upon the special nature of a mortgagee's power of sale. [4] Hunter's case dealt with a 'special set of facts' [5] and did not purport to overrule earlier authority [6] to the effect that a transfer in breach of the articles remains effective between the parties. He did not need to finally decide the point, and the Supreme Court on appeal hardly touched upon it. O'Sullivan C.J. in delivering the judgment of the Supreme Court did say, however, that the directors in this case could waive their pre-emptive rights.

In the later decision of Hawks v McArthur [7] Vaisey J. agreed with Black J. in the previous case that Hunter v Hunter must be read as limited to the situation where there is a sale by a mortgagee. He continued:-

> "I find the very greatest difficulty in seeing how I ought to apply the decision in Hunter v Hunter to the facts of this case. On general principles, in such circumstances as those of the present case where a man who has an interest in shares in a company receives something for the sale of those shares and executes under seal a transfer of those shares for that

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(1) ibid 261

(2) (1936) A.C. 222

(3) (1943) I.R. 426

(4) (1943) I.R. 426, 454

(5) ibid 456

(6) e.g. Casey v Bentley (1902) 1 I.R. 376; Hawkins v Matty 3 Ch. App. 188; R. v Londonderry & Coleraine Rly. Co. 13 Q.B. 998; R. v Wing 17 Q.B. 645

(7) (1951) 1 A.E.R. 22

purpose, I cannot bring myself to suppose that Hunter v Hunter constrains me to hold that everything done in that transaction is a complete nullity." [1]

He, therefore, held the transfer in contravention of the pre-emptive rights article resulted in the purchasers obtaining an equitable interest.

It is now necessary to turn to the leading New Zealand decision of Gold v Penny. [2] Here the respondent on appeal became a shareholder in a company on the basis of a promise by the appellant to repurchase the shares from the respondent "in the event of the respondent at any time becoming dissatisfied with his position with or investment of capital in the company."

After the company was formed the respondent commenced work with it but about six weeks later his employment was terminated and he called upon the appellant to repurchase his shares. The appellant refused to do so.

Article 10 (a) of the company (the so-called pre-emptive rights article [3]) provided that no share was to be transferred unless and until the 'rights of pre-emption' conferred by that article were complied with. On the day of the Supreme Court hearing, the managing director of the company produced a notice expressing the respondent's desire to transfer his shares to the appellant. The notice appointed the directors the agents of the respondent for the purpose and stated that the proposed transfer was pursuant to an earlier oral agreement. The notice did not, however, comply with the requirements of the pre-emptive rights article. [4] Upon receipt of this notice, the directors by resolution approved the proposed transfer and agreed to accept the transfer to the appellant for registration.

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(1) (1951) 1 All E.R. 22, 27

(2) (1960) N.Z.L.R. 1032

(3) see (1960) N.Z.L.R. 1032, 1058 per Cleary & Hutchinson J.J.

(4) ibid 1038 per Hardie Boyes J.

Hardie Boys held that the existence of an oral agreement had been proved, and entered judgment for the plaintiff decreeing specific performance. One arguement raised for the appellant was that the oral agreement for purchase was ineffective because of the pre-emptive rights article.

Cleary & Hutchison J.J. in a joint judgment delivered by Cleary J. turned to the recent decision of Lyle & Scott v Scott's Trustees [1] After mentioning the precise point of decision they continued:-

> "...disregarding anything that might arise from the fact that the respondent made his agreement with the appellant before the company was formed, it would mean that, at all events from the time the respondent called upon the appellant to buy the shares the respondent was a member who desired to sell and was obliged to give a transfer notice to the directors." [2]

In the present case - unlike Lyle & Scott v Scott's Trustees - the company had not complained about the breach of its articles. The directors, in fact, took steps to approve the transaction. The Court of Appeal, therefore, had to consider the question whether the agreement was a nullity. If this was so, it would not be competent for the directors to regularise the transaction. The Court of Appeal was not directly concerned with the further question of whether any rights passed under the agreement. This was passed over :-

> "Assuming for present purposes that no beneficial interest in the shares could pass under an agreement in conflict with the articles - a matter that has not been authoritatively decided - the question remains whether such an agreement is a nullity." [3]

Cleary J. and Hutchison J. referred to the difference of opinion between Viscount Hailsham and Lord Atkin in Hunter v Hunter

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(1) (1959) A.C. 763

(2) ibid 1060

(3) ibid 1060 per Cleary & Hutchison J.J.

and mentioned that the passage in Lord Atkin's judgment which has already been cited, [1] may only have been directed to the question whether there are any legal or equitable rights arising.[2] They also referred to the judgment of Myers C.J. in Beynon v Acme Engineering Ltd.[3] where the varying opinions expressed in Hunter v Hunter were mentioned although the Chief Justice did not need to express a final view on the point.

Cleary & Hutchinson J.J. preferred the views expressed by Viscount Hailsham. It was competent for the directors to regularise the transactions although they though that what was done may have been partly a waiver and partly compliance with the articles. Their Honours considered that it was 'unreasonable' that an agreement in breach of the articles could not be enforced even if all those having rights under the articles agreed :-

> "The purpose of pre-emptive provisions in articles is to restrict the shareholder's power to dispose of his shares until the pre-emptive provisions have been complied with and exhausted. This purpose may be achieved, and the rights of the company and the shareholders may be secured without holding that an agreement made in breach of the term of the articles is void ab initio and incapable of subsequent regularisation." [4]

Gresson P. took a different approach. He mentioned the differing judicial opinion expressed in Hunter v Hunter and the fact that the relevant part of their Lordships' speeches was strictly obiter. He cited Re Hafner [5] for the following proposition :-

> "The position may be that if a shareholder sells his shares without complying with the provisions of the articles of association restricting transfer the purchaser becomes

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(1) (1936) A.C. 222; 261

(2) (1960) N.Z.L.R. 1032; 1061

(3) (1945) N.Z.L.R. 729

(4) ibid 1061

(5) (1943) I.R. 426

the equitable owner of the shares, though a mortgagee of the shares may not be entitled to sell the equitable interest." [1]

Gresson P. thought that the distinguishing feature of the present case was that the restriction in the articles was on both selling and transferring, and consequently the agreement was subject to the articles before an "unexceptional" contract could be made. His Honour would thus appear to draw a distinction between articles restricting 'transfer' and articles restricting both selling and transferring. There is a difficulty with this approach. We have the authority of Lords Reid and Keith in Lyle & Scott v Scott's Trustees for the view that the word 'transfer' in pre-emptive rights articles should be interpreted to include a sale and purchase agreement. Moreover, all of their Lordships would agree that if a shareholder agrees to sell his shares, he is 'desirous of transferring' and must give notice to the company. Thus whether the restriction is on both selling and transferring or merely on transferring, any equitable rights that could arise would be negated. It is submitted that the distinction does not have a satisfactory basis except in one regard. Sometimes the articles will specifically restrict the execution and registration of a transfer and nothing else. Here the word 'transfer' is used in its narrow meaning.

The joint judgment of Cleary & Hutchinson J.J. does not raise this distinction. Their Honours applied the dicta of Viscount Hailsham in Hunter v Hunter [2] to the present situation where the restriction is expressly upon both selling and transferring.

In summary of the decisions that have been considered in this part of the paper, three definite approaches emerge:-

(1) An agreement for sale and purchase or transfer in breach of pre-emptive rights is a nullity and ineffective for all

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(1) (1960) N.Z.L.R. 1032, 1047

(2) (1936) A.C. 222

purposes between the parties thereto. This approach is supported by Lord Atkin in Hunter v Hunter.[1]

(2) The agreement for sale and purchase or transfer is not a nullity but cannot have any effect inter partes unless and until it is assented to by all the directors or shareholders, as the case may be, who have rights under the articles. In support of this approach, the dicta of Viscount Hailsham L.C. and Lords Macmillan and Russell in Hunter v Hunter can be cited. The joint judgment of Cleary & Hutchinson J.J. in Gold v Penny [2] also tends to support this approach, as does the judgment of Myers C.J. in Benyon v Acme Engineering Ltd.[3]

(3) The sale and purchase agreement or transfer is effective inter partes to pass equitable rights in the purchaser. These rights are liable to be defeated if the company or its shareholders enforce the provisions of the pre-emptive rights articles. This view is taken in Re Hafner,[4] Hawks v McArthur [5] and (to the extent already mentioned) by Gresson P. in Gold v Penny.

The second approach has the greatest amount of support in New Zealand. As pointed out by Cleary & Hutchinson J.J. in their joint judgment in Gold v Penny, the purpose of the pre-emptive rights articles can be achieved without holding that an agreement made in breach of them is a nullity. If the third approach above is adopted, any equitable rights arising are always subject to the contingency that a company may enforce the articles. The equitable rights would not become absolute until the

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(1) (1936) A.C. 222; 261
(2) (1960) N.Z.L.R. 1032
(3) (1945) N.Z.L.R. 729
(4) (1943) I.R. 426
(5) (1951) 1 All E.R. 22

shareholders or directors having rights under the articles assented to the sale and purchase agreement. Gold v Penny is authority for the view that this assent may be given even on the day of an action for specific performance; the equitable rights necessary to support an action for specific performance will arise, at the latest, when this assent is given.

PART V

TRUSTS OF SHARES AND PRE-EMPTIVE RIGHTS ARTICLES

A suggested method of avoiding the operation of the pre-emptive rights articles in a company's articles of association is for the shareholders concerned to enter into a deed of trust with "the purchaser". It is proposed to turn firstly to the issue of whether a person is 'desirous of selling' or'desirous of transferring' his shares if he enters into a deed of trust or declares himself to be holding shares on trust for another. Then some aspects of the law in relation to trusts of shares will be discussed. This will help to evaluate the effectiveness of trusts as an avoidance device.

A. The Applicability of Pre-emptive Rights Articles to Deeds of Trust and Declarations of Trust

The judgments of Viscount Simonds and Lord Tucker in Lyle & Scott Ltd. v Scott's Trustees do not offer much help in deciding whether a deed of trust comes within the pre-emptive rights article. They based their judgments upon the principle that a vendor is bound to do everything that lies in him to perfect the title of the purchaser.

Lords Reid and Keith did, however, deal with the meaning of 'desirous of transferring' as already mentioned.[1] Lord Keith said:-

> "I think a shareholder who has transferred or pretended to transfer the beneficial interest in a share to a purchaser for value is merely endeavouring by a subterfuge to escape from the pre-emptory provisions of the article. A share is

(1) See Part II A ante

of no value to anyone without the benefits it confers. A sale of a share is a sale of the beneficial rights that it confers and to sell or purport to sell the beneficial rights without the title to the share is, in my opinion, a plain breach of article 9."[1]

The above passage would seem to apply (mutatis mutandis) equally as much to a deed of trust as it does to an outright sale of an equitable interest. L.S. Sealy [2] considers that this statement of Lord Keith's must be read in the light of the facts of *Lyle & Scott Ltd. v Scott's Trustees* where it was planned and agreed that title should be transferred and that it was by virtue of the contract for sale and purchase that the assignment of beneficial rights occurred. This may have been so in *Lyle & Scott Ltd. v Scott's Trustees* but it is submitted that there is nothing in either the passage above or in the rest of Lord Keith's speech that suggests that he intended his observations to be limited to the case in hand.

Some indication of Lord Reid's position on this point may be derived from his judgment. He said:-

> " ... the ordinary meaning of 'transfer' is simply to hand over or part with something; and a shareholder who agrees to sell is parting with something." [3]

A person who declares himself as trustee for another or enters into a deed of trust in connection with shares which he owns is 'parting' with something - the beneficial interest in the shares concerned. It is not altogether clear, however, that the pure trust

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(1) (1959) A.C. 763 @ 785

(2) (1960) C.L.J. 28 @ 29

(3) ibid 778

situation was contemplated to be included in the above words.

The courts have shown themselves willing to construe pre-emptive rights articles liberally and they may well be prepared to follow the lead of Lord Keith especially and prevent the avoidance of such articles by the transfer of beneficial interests. In view of this uncertainty some recently formed companies contain a provision in their pre-emptive rights articles that is expressly designed to prevent dealing in beneficial interests.[1]

An even more fundamental question is raised by the relationship between trusts of shares and pre-emptive rights articles - is a company entitled to regulate the dealing in beneficial interests simpliciter. This question has not yet been directly raised for decision. In <u>Hunter v Hunter</u>[2] the House of Lords held that the beneficial interest in shares could not be disposed of independently of the legal interest. However, it was pointed out by Vaisey J. in <u>Hawks v McArthur</u>[3] that this was a sale by a mortgagee to which special considerations apply. A passage in the speech of Lord Atkin in <u>Hunter v Hunter</u> is relevant in this connection:-

> "The mortgage it is true is an equitable mortgage but of the whole legal interest. It seems to me to be without principle or precedent to construe a power of sale in such cases as including a power to agree to sell either the whole or part of the mortgagor's equitable interest divested of the legal title."[4]

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(1) A pre-emptive rights article containing such a provision is set out in Appendix III

(2) (1936) A.C. 222

(3) (1951) 1 All E.R. 22

(4) (1936) A.C. 222, 261

L.S. Sealy [1] suggests that a company cannot lawfully regulate dealing in beneficial interests in shares as this would be contrary to the principle of company law that a company is not concerned with beneficial interests in shares. He mentioned that McClelland J. in Australian Fixed Trusts Pty. Ltd. v Clyde Industries Ltd. [2] did not consider a further possible objection to the alteration of the articles. This was that the alteration would require the company to become aware of the equitable interests in the shares. [3]

More importantly for present purposes Sealy considered that 'on principle' a company should not be entitled to require notice of trusts. He could find scant authority in support of this proposition. [4] In the absence of any binding decision to the contrary, the writer prefers the view that a company may concern itself with trusts if it chooses to do so. The existence of trusts become highly important in the takeover situation and unless a company can regulate dealings in beneficial interests through pre-emptive rights articles such trusts may provide a convenient means for a takeover.

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(1) (1960) C.L.J. 28, 29

(2) (1950) 59 S.R. (N.S.W.) 33

(3) cf. Section 125 of the Companies Act

(4) (1960) C.L.J. 28 @ 30

B. <u>The Law Relating to Trusts of Shares</u>

In this section we are mainly concerned with the rights of a beneficiary under a deed of trust for shares. The main rights with which we will be concerned are the right to dividends and more importantly the right to dictate the way in which any voting rights are exercised.

A beneficiary would be entitled (in the absence of any express provision in the trust) to demand from the trustees the dividends. The converse is that the beneficiary must indemnify the trustees for any calls made upon the shares. The general principle is stated by Lord Lindley in <u>Hardoon v Belilios</u>:-[1]

> "The plainest principles of justice require that the cestui que trust who gets all the benefit of the property should bear its burden unless he can show some good reason why his trustee should bear them himself."[2]

If such an arrangement as described above was contemplated, then it would be advisable for the beneficiary to obtain executed proxies in his favour because of the present uncertainty as to the extent to which trustees can be compelled to exercise their voting power in favour of the beneficiaries.

<u>Kirby v Wilkins</u>[3] is the first case that needs to be considered. The chairman of the board of the company held a group of shares on trust to use or sell them for the benefit of the company. Some shareholders brought an action to prevent the chairman from voting without a direction from the

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(1) (1901) A.C. 118

(2) ibid 123

(3) (1929) 2 Ch. 444

company. Romer J. rejected this contention:-

> "Where a shareholder holds shares as a bare trustee for a third person, he is no doubt obliged to exercise his voting power in the way that the cestui que trust desires, but unless and until the cestui que trust has indicated his wish as to the way in which the voting power should be exercised, there is no reason why the nominee should not exercise the voting power vested in him as trustee. He holds that voting power upon trust, but, unless and until the cestui que trust intervenes, he must exercise it according to his directions in the best interests of his cestui que trust." [1]

This decision states a general principle that a beneficiary is entitled to direct the trustee to exercise his voting power in accordance with his direction. Some limitations that must be put upon this statement come to mind. There may be a class of beneficiaries in which case it would seem that the class would have to be unanimous. If they were in disagreement an order of the court would be necessary. Most of the difficulties in relation to the general principle have arisen in situations where the trustees have also been directors of the company.

In <u>Butt v Kelson</u> [2] the defendents were trustees of a large proportion of the shares in a company. They had got themselves appointed directors under the provision of the testator's will. The plaintiff who had a life interest in a large proportion of the testator's estate claimed a declaration that he was entitled to inspect all documents which came into the possession of the trustees as directors of the company.

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(1) ibid 454
(2) (1952) 1 Ch. 197

In the High Court, a declaration in terms sought was granted but the Court of Appeal did not agree with the form of the declaration. Romer L.J. gave the leading judgment. He pointed out a number of undesirable consequences that would flow from the granting of the declaration obtained in the court below.[1] It would result in the beneficiary, who was not even on the register of members, obtaining information which would not be available to the ordinary registered shareholder.[2] The information could be highly prejudicial. He further pointed out that the other shareholders might have objections to the beneficiary having unrestricted access to the information.[3]

Romer L.J. considered that the correct approach was put forward by counsel for the appellants. He had submitted that there was a distinction to be drawn between an unincorporated business and a business carried on by a company in which the trustees hold shares. In the first situation, it is well recognised that the beneficiaries could see the documents relating to the business as they are the virtual owners. This principle is one of general application,[4] and applies to all trust documents in the absence of special circumstances.[5]

When the beneficiaries are interested in the shares of an incorporated company the only control over the directors which the beneficiaries can seek to obtain through the courts is a control through the medium of the shares.[6] Romer L.J. summarised the position in the following passage:-

> " ... the beneficiaries are entitled to be treated as though they were the registered holders in respect of trust shares

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(1) ibid 205

(2) ibid 205

(3) ibid 206

(4) see In Re Cowin, Cowin v Gravett (1886) 33 Ch. D. 179

(5) cf. Re Fairbairn (deceased) (1967) V.R. 633

"with the advantages and disadvantages ... which are involved in that position, and that they can compel the trustee directors, if necessary, to use their votes as the beneficiaries, or as the court, if the beneficiaries themselves are not in agreement, think proper, even to the extent of altering the articles of association if the trust shares carry votes sufficient for that purpose." [1]

Since the trust holding in this case gave complete control of the company Romer L.J. considered that subject to three requirements the directors should allow inspection not because they are compelled to do so as directors but as a "short circuit" to an order compelling them to use their voting power to achieve this effect. The three requirements were that the plaintiff must specify the documents which he wishes to see; he must make out a proper case for seeing them and lastly he is not met by any valid objection by the other beneficiaries or by the directors on behalf of the company. The Court of Appeal thereupon gave liberty to apply to the court in relation to any document which he desires to see and to which he is refused inspection.

It is suggested that this order was made upon a dubious basis. The beneficiaries' only rights of control relating to the documents in question were those that could be enforced through the shareholding of the company. Romer L.J. thought that the directors should allow inspection because ultimately they could be compelled to exercise their voting powers to bring about the change desired. It is, however, a different matter to ascribe some sort of legal basis to the "short circuit", and lay down conditions for its exercise. At one point in the judgement already mentioned, Romer L.J. said that the directors should give inspection :-

"... not because they can be compelled to do so as directors but as a short circuit, if one may so describe it to an order compelling them to use their voting powers so as to bring

(1) ibid 207

about what the plaintiff desires to achieve." [1]

By giving liberty to the plaintiff to apply to the court for an order as to inspection, Romer L.J. appears to be granting relief in a situation in which, as he has already asserted, the plaintiff is not strictly entitled to it.

The next case for consideration is In Re George Whichelow Ltd. [2] This was a similar factual situation to Butt v Kelson [3] but here the beneficiaries directed the trustees to exercise their voting power in a certain way. The trustees refused to do this and said that they would exercise their votes in accordance with their discretion. The trustees in this case do not appear to have been directors but the case is important because it refers to the earlier case of Butt v Kelson and is also mentioned in a later Australian case which is yet to be mentioned.

The plaintiffs in In Re George Whichelow Ltd. [4] claimed to be all those who were entitled to the beneficial interest in the trust shares and consequently as a group they could direct the trustees how to vote at a meeting of the company. Upjohn J. rejected the contention that the trustees had received a direction from all those beneficially entitled. The shares were on trust to three married women for life and a remainder to issue. There were children but all were over twenty one. The youngest of the life beneficiaries was fifty two. It was held that as a matter of law it could not be said that these three women were passed the age of child bearing.

The writer does not dispute this part of the judgement but Upjohn J. also made comments upon the case of Butt v Kelson which may be open to question. He referred to well established

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(1) ibid 207
(2) (1954) 1 W.L.R. 5
(3) (1952) Ch. 197
(4) (1954) 1 W.L.R. 5

authority that where trustees have been given a pure discretion as to the exercise of a power, the courts will not enforce the exercise of the power against the wishes of the trustees although it will prevent them from exercising it improperly.[1] Upjohn J. continued:-

> "I think that the case of Butt v Kelson[2] is difficult to reconcile with those cases and I am not prepared to grant any relief upon an interlocutory motion. Furthermore, in my judgement the right way of looking at the position is that here are trustees ... who are anxious to exercise their discretion."[3]

It is submitted that the cases cited by Upjohn J. are distinguishable. They relate to the exercise of a pure power. The voting rights which attach to shares are trust property. If beneficiaries agree, they are entitled to direct the trustees as to how the voting rights are to be exercised. If a pure power given to the trustees by the testator was involved, then the beneficiaries could not intervene as long as it was not exercised improperly. Similarly, if the trustees are directors the beneficiaries cannot influence the exercise of their powers in that capacity directly. Their only remedy is through the use of their power to direct the voting.

The Supreme Court of Victoria has recently considered the cases already mentioned in Walker v Willis.[4] Here all the shares were held by the trustees who were also the directors. Fifty per cent were held for the plaintiff contingently upon him attaining the age of twenty five. The rest were held partly by the trustees themselves and partly for members of his family.

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(1) See Tempest v Lord Camoys (1882) 21 Ch. D. 571 @ 578 per Jessel M.R.

(2) (1952) Ch. 197

(3) (1954) 1 W.L.R. 5 @ 8

(4) (1969) V.R. 778

The directors decided to call the annual meeting for the 10th October in one year. The articles provided that all the directors should retire at the annual general meeting. The plaintiff sought an interlocutory injunction to prevent the holding of the meeting until he attained the age of twenty five in the following month and became a registered shareholder. The directors admitted that they intended to prevent the plaintiff from voting by holding the annual general meeting in October.

The plaintiff founded his argument upon two bases. The first was the principle that a director could be restrained from the improper exercise of his fiduciary powers. The case of Grant v John Grant & Sons Pty. Ltd. [1] was cited for the proposition that directors could not use their fiduciary powers to perpetuate their control over the affairs of the company. Lush J. held that since the plaintiff was not the actual shareholder and was not yet absolutely entitled to the beneficial interest he could not rely on Grant v John Grant & Sons Pty. Ltd. which provides the basis of a remedy for a shareholder against the directors. [2] The plaintiff did not have the necessary standing. Lush J. further held that the plaintiff had not made out a prima facie case of bad faith.

It was further argued for the plaintiff that the trustees' powers as directors were in effect trust property and that they should regulate the affairs of the company so that when the plaintiff reached twenty five his voting powers would be able to be exercised at the annual general meeting of the year in question. [3] Lush J. followed Butt v Kelson [4] and rejected this argument. The powers of the defendant trustees as directors were not trust property but were rather to be exercised for the benefit of the company. [5] The decision to call the annual general

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(1) (1950) 82 C.L.R. 1
(2) (1969) V.R. 778, 781
(3) ibid 780
(4) (1952) Ch. 197
(5) (1969) V.R. 778, 781

meeting was taken in the exercise of the directors' powers of management. The powers involved were not trustees' powers as such. The plaintiff could not, therefore, direct the trustees to exercise these powers for his benefit.[1]

There remained the question whether the plaintiff could direct the trustees how the voting power of the trust shares was to be exercised at the general meeting. Lush J. held, following In Re George Whichelow Ltd.[2] that as the plaintiff was not absolutely entitled to the beneficial interest in the shares he could not direct the trustees as to how they should vote.[3]

We have now seen some of the limitations that must be put upon the principle enunciated in Kirby v Wilkins[4] that a trustee must exercise the voting power in accordance with the directions of his beneficiaries. The later cases seek to define the extent of the principle especially in relation to the situation where the trustees are also the directors of the company. This does have relevance to corporate raiders who may wish to use the trust as a means of getting around a pre-emptive rights article. Even if the directors of a company are the trustees this does not, of itself, ensure control of the board. Different considerations apply if the beneficiary has a majority shareholding - he could then use his powers to remove the directors.

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(1) ibid 781 - 782

(2) (1954) 1 W.L.R. 5

(3) (1969) V.R. 778, 781

(4) (1929) 2 Ch. 444

PART VI

THE VALUATION OF SHARES OFFERED TO SHAREHOLDERS IN ACCORDANCE WITH PRE-EMPTIVE RIGHTS ARTICLES

Pre-emptive rights articles will almost inevitably provide some method for the determination of the price of shares that are to be sold to the other members of the company. It is usual to provide that failing agreement, the price is to be determined either by arbitration [1] or by the company's auditor or accountant or other named individual. [2] In the second situation, the articles may provide that the auditors are to act as experts and not as arbitrators. [3] Dale & Sclater has [4] a precedent which after providing for the auditor to act as an expert and not as an arbitrator, expressly excludes the provisions of the Arbitration Act 1908. It is intended to concentrate on valuations made by auditors or other nominated officials.

A. THE GROUNDS UPON WHICH VALUATIONS CAN BE SET ASIDE

The basic statement of the law is that of Sir John Romilly M.R. in the early case of Collier v Mason. [5] He said:-

> "This court, upon the principle laid down by Lord Eldon, must act on the valuation, unless there be proof of some mistake, or some improper motive, I do not say a fraudulent one, as if the valuer had valued something not included or had valued it on a wholly erroneous principle ... or even, in the absence of any proof of any one of these

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(1) e.g. Gold v Penny (1960) N.Z.L.R. 1032

(2) e.g. Lyle & Scott v Scott's Trustees; Dale & Sclater, Private Companies in New Zealand (1968) @ 87-88; Arenson v Arenson (1973) 2 W.L.R. 553; Beynon v Acme Engineering Co. Ltd. (1945) N.Z.L.R. 729

(3) See Dean v Prince (1954) 1 Ch. 409; cf. Arenson v Arenson (1973) 2 W.L.R. 553 where there was an agreement to this effect although not embodied in the articles.

(4) Private Companies in New Zealand (1968) 87-88

(5) (1858) 25 Beav. 200

> things, if the price was so excessive or so small as only to be explainable by reference to some such cause ... " [1]

This passage was accepted as correct by the Court of Appeal in Dean v Prince.[2] Evershed M.R. did not attempt to lay down any exhaustive definitions but held that the plaintiff was entitled to succeed if she could show that the auditor had made a mistake of a substantial character or had materially misdirected himself in the course of his valuation.[3] In a later passage he said that the valuation could be set aside if the auditor made a "material mistake or erred in principle".

Denning L.J. considerably expanded upon the passage contained in the judgment of Sir John Romilly M.R. in Collier v Mason.[4] He first pointed out that the auditor was to act as an expert and give his opinion as to the value of the shares. As valuation is largely a matter of opinion, it will be difficult to say that it is wrong but the courts will upset a valuation under certain conditions:-

> "It can be impeached not only for fraud but also for mistake ... For instance, if the expert added up his figures wrongly; or took something into account which he ought not have taken into account, or conversely; or interpreted the agreement wrongly; or proceeded on some erroneous principle ... Even if the court cannot point to the actual error, nevertheless, if the figure itself is so extravagantly large or so inadaquately small that the only conclusion is that he must have gone wrong somewhere, then the court will interfere... On matters of opinion the courts will not interfere; but for mistake

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(1) ibid 204
(2) (1954) 1 Ch. 409
(3) ibid 418
(4) (1858) 25 Beav. 200, 204

of jurisdiction or of principle, and for mistake of law, including interpretation of documents, and for miscarriage of justice, the courts will interfere ... " [1]

Wynn-Parry J. accepted the principle laid down by Sir John Romilly M.R. in Collier v Mason as being applicable to the present case, and took a very similar view to that of Denning L.J.

In Frank H. Wright (Constructions) Ltd v Frodoor Ltd. [2] - also a case where the binding force of a valuation not contained in the articles of association was challenged - Roskill J. said:-

"The circumstances in which the court will interfere with a certificate of this kind are extremely restricted. The court will not and should not be astute to upset the decisions of those whom the parties have freely chosen to decide their problems for them ... Parties ... take their experts (whether accountants or otherwise) for better or worse with the attendant risks of error which are inherent in the ordinary human weaknesses of any tribunal. But there are some occasions which are well defined when the court will and must interfere." [3]

Roskill J. then referred to Collier v Mason and the later case of Weekes v Gallard [4] which was also decided by Sir John Romilly M.R. He referred to the judgments delivered by the Court of Appeal in Dean v Prince and considered them to be applicable to the case before him. The judgment of Harman J. in the court below was cited for the proposition that the courts can interfere if the valuation is a "speaking

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(1) ibid 427

(2) (1967) 1 W.L.R. 506

(3) ibid 524

(4) (1869) 21 L.T. 655

Explain

valuation" but not otherwise. We will return to this part of Harman J's judgment in connection with a later case.

The next case that should be mentioned is the decision of Ungoed-Thomas J. in Jones (M) v Jones (R.R.).[1] The learned judge in the course of his judgment cited both Collier v Mason and Lord Denning's judgment in Dean v Prince with apparent approval. He held that the valuation there was made on a wrong basis and, consequently, was a valuation made on an "erroneous principle".[2]

In none of the cases so far considered has the Court of Appeal decision in Dean v Prince been doubted but it now must be read in the light of certain observations of Lord Denning M.R. in Arenson v Arenson.[3] This case (as reported) is mainly concerned with the liability of auditors for negligence in making a valuation. The agreement under which the valuation was made was not embodied in the articles, but nothing seems to turn on this factor.

The other two members of the Court of Appeal in this case did not discuss the grounds upon which a valuation could be held not to be binding upon the parties. Lord Denning thought fit to examine this area of the law to "shorten the task of others that may have to deal with it. In the course of his judgment he considered the binding force of arbitrations and certificates for building or engineering work. Of particular interest for present purposes are his observations upon agreements to accept a valuation made by an expert. His Lordship started with the position at Common Law where the parties are bound :- Lord Denning dissented

"Even if he makes a mistake in his calculations or makes

(1) (1971) 1 W.L.R. 840

(2) ibid 854

(3) (1973) 2 W.L.R. 553; (1973) 2 All E.R. 234

the valuation on what one or other considers to be a wrong basis, still they are bound by their agreement to accept it. If his valuation is not a speaking valuation - if he gives no reasons or does not explain the basis on which he has proceeded - clearly they are bound."[1]

Lord Denning then considered whether it made any difference if the expert gives reasons, and pointed out that Harman J. at first instance in <u>Dean v Prince</u>[2] had held as a preliminary matter that as the auditors had given reasons for their decision, a court could inquire into their correctness. Harman J. reached his conclusion by analogy with the situation where trustees or directors exercise discretionary powers. A court will not force these to break their silence but if they should do so a plaintiff may challenge their motives in court.

Lord Denning was not prepared to give unqualified approval to Harman J.'s conclusion:-

"This may be right, though I am not quite sure about it. At any event, that exception stated by Harman J. does not apply in this case. Here the auditors did not give any reasons, nor did they state the basis on which they made their valuation. They kept silent. Undoubtedly at Common Law their valuation was final and binding and not open to be questioned by the parties or either of them."[3]

He then turned to the position in equity:-

"In equity, however, it may be different. Sir John Romilly M.R. once said that a court of equity might

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(1) ibid 560
(2) (1953) Ch. 590
(3) (1973) 2 W.L.R. 553, 560-561

refuse specific performance if the valuation was influenced by fraud, mistake or miscarriage ... But some years later he said that 'the only defence to such a suit (for specific performance) would be fraud or collusion' see Weekes v Gallard.[1] Howsoever that may be, I have found no case in which equity has intervened on the ground that the valuer has made a mistake." [2]

His Lordship cited the cases already dealt with in the preceeding pages and found that Jones (M) v Jones (R.R.)[3] was the only case in which a valuation was upset. He then stated that:-

"Even if equity can intervene on the ground of mistake, there may be no room in the present case for the interposition of equity. There is no question of specific performance. The agreement has been fully executed ... There cannot be restitutio in integrum." [4]

From the above it can be seen that Lord Denning takes a much more narrow approach than he took in Dean v Prince. He was not prepared to unreservedly accept that a "speaking valuation" could be challenged at Common Law despite settled authority in the analogous situation of arbitrations. It has been decided by a long series of cases - one of which Lord Denning cited[5] - that an error of law on the face of the award is a ground for setting it aside.

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(1) (1869) 21 L.T. 655

(2) ibid 561

(3) (1971) 1 W.L.R. 840

(4) ibid 561

(5) Hodgkinson v Fernie (1857) 3 C.B.N.S. 189, 202

Lord Denning further cast doubts as to the exact extent to which a court would interfere in equity. In Dean v Prince he had said that courts could intervene if the valuation was made under a mistake.[1] In Arenson v Arenson he is not so categorical. In justification, he mentions that in Weekes v Gallard [2] Sir John Romilly M.R. said that the only defence to the suit would be fraud or collusion. This inconsistency with Collier v Mason is hard to explain. The earlier case was not mentioned in Weekes v Gallard, although the case of Parken v Whitly[3] was cited in arguement in both cases. Another reason given for his new found doubts is that he could not find a case where a party had actually succeeded in equity simply on the ground that the valuer made a mistake. This may well be so, but it is submitted that this cannot alter the validity of a general principle if it is sound.

Lord Denning thus reached his conclusion that the valuation could not be challenged in this case by an examination of the position at Common Law and equity in turn. The valuation could not be set aside in accordance with the Common Law because it was not a speaking order. It could not be set aside in equity because there was no reason for the imposition of equity. Specific performance could not be sought. No account seems to have been taken of the Rule of Law that where there is a conflict between the rules of equity and Common Law, equity should prevail.[4]

In the present situation, there is a conflict in as much as equity would intervene in a wider variety of circumstances. If the auditors valuing company shares did not give any reasons

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(1) see (1954) Ch. 409, 427

(2) (1869) 21 L.T. 655

(3) 1 Turn. & Russ. 366

(4) see section 99 Judicature Act 1908

it would not be possible to challenge their valuation at Common Law in the absence of fraud or collusion. In equity the position was different. Sir John Romilly in a passage already cited said that even if it could not be proved that the valuer had acted upon a mistake or some erroneous principle, nevertheless, the court would set aside the valuation if the price was so excessive or so small as to be explainable only by reference to such cause.[1] This passage, it will be remembered, was approved and expanded upon by Denning L.J. in Dean v Prince.[2]

If the correct approach is that the rules of equity concerning the grounds for setting aside valuations should prevail, then it must follow that Lord Denning erred in Arenson v Arenson when he considered the position at Common Law and equity separately. Assuming the rules of equity to be now applicable to all situations, then the omission to give reasons in the present case should not have been fatal. The alleged mistake was of such substantial proportions that a court would have had little difficulty in inferring that an erroneous principle had been acted upon despite the absence of a 'speaking' valuation.

While the writer favours the view that the principles of equity should determine the availability of a remedy in all cases, it is admittedly difficult to extract positive support for this view from decided cases. Collier v Mason and Weekes v Gallard were both suits for specific performance before the Judicature Acts. Dean v Prince was an action for a declaration. Harman J. at first instance, held that as the valuers had not chosen to keep silent, the court could question their reasons.

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(1) see 25 Beav. 200, 204

(2) (1954) 1 Ch. 409, 427

This is in accordance with the position at Common Law. The Court of Appeal, as previously mentioned held that the applicable principles were contained in *Collier v Mason*. The preliminary point decided by Harman J. was not re-argued in the Court of Appeal. It is submitted that the Court of Appeal's acceptance of *Collier v Mason* is significant as *Dean v Prince* was not a case where an equitable remedy was being sought. Denning L.J. did not allude to any supposed difference between Common Law and equity. He, in fact, expanded considerably on the principles enunciated in *Collier v Mason* and stated that the cases about valuers bear some analogy with cases on domestic tribunals. He referred to the Court of Appeal decision in *Lee v Showmen's Guild of Great Britain* [1] in which he was a member of the court. It is suggested that this is a reasonable approach. In the area of administrative law the courts have become increasingly willing to review the decisions of tribunals. It is suggested that increased judicial activism in the field of valuations is also appropriate.

It is difficult to agree with Lord Denning [2] that because the parties have made their bed they must lie on it. Lord Denning was referring to a valuation of shares but the agreement was not contained in the articles. When the valuation requirement is part of the pre-emptive rights articles of a company the justification for the court's interference is even stronger. A shareholder must accept the terms of the articles without negotiation (unless he has been involved in the actual formation).

Another case that is relevant to the present question

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(1) (1952) 2 Q.B. 329

(2) in *Arenson v Arenson* (1973) 1 W.L.R. 553, 560

is Frank H. Wright (Constructions) Ltd. v Frodoor Ltd.[1] Roskill J. mentioned the line of authority running from Collier v Mason to the Court of Appeal decision in Dean v Prince as well as Harman J's judgment in the same case upon the strength of which he concluded:-

> "In the present case, Cooper Brothers have set out their reasons, and it is open, therefore, to the defendants, if they can, to seek to upset that certificate."[2]

This was a case where specific performance was sought and, consequently, the position in equity was relevant on any interpretation of the law. A speaking order was not necessary and, it is submitted, the the above passage is incorrect. It would have been open to the defendants to upset the certificate regardless of whether reasons were given.

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(1) (1967) 1 W.L.R. 506

(2) ibid 526

B. IMMATERIAL ERRORS IN VALUATIONS

In Frank H. Wright (Constructions) Ltd. v Frodoor Ltd.[1] one of the grounds upon which it was sought to set the valuation aside was the inclusion of the word 'not' in one of the paragraphs of the valuation. This did not affect the arithmetical result but was purely an inadvertent mistake. Roskill J. said:-

> "There can be no doubt on the authorities that if this had been a material error, it would have entitled the defendants to have the certificate set aside without more."[2]

It was argued that even if the error did not affect the final sum certified, the valuation should still be set aside. Roskill J. referred to the judgment of Evershed M.R. in Dean v Prince which he considered authority for the view that before a court will set aside a certificate for error, the error must be 'material'. A material error was one which materially affected the result. He concluded as follows:-

> "If this error had been material, it would have been enough to vitiate the whole of the certificate, small as it might be and regrettable as the consequences might be. But in my judgment ... this error is not material because it does not affect the result."[3]

A converse situation occurred in Jones (M) v Jones (R.R.).[4] Here the defendants argued that an error in principle does not vitiate a valuation unless it can be shown that a valuation

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(1) (1967) 1 W.L.R. 506

(2) ibid 529

(3) ibid 529

(4) (1971) 1 W.L.R. 840

on the correct principle would result in a materially different figure. The defendants apparently relied on a passage in the final paragraph of the judgment of Evershed M.R. in Dean v Prince where he stated that although the valuer had erred in principle, the plaintiff had failed to establish that had the correct principle been considered, a materially different figure would have resulted. Denning L.J. and Wynn-Parry J. did not deal with this point as they decided that the correct principle had been considered.

Ungoed Thomas J. examined the passage mentioned above and divided Evershed M.R.'s observations into three stages:-

> "... in the course of arriving at this conclusion his observations might perhaps be read as showing that he took three stages: (1) that the auditor decided that the break up valuation was alone admissible as alternative to a going concern valuation: (2) that such decision was wrong in principle: and (3) that the objection to the valuation nevertheless failed because it was not proved that a valuation in situ or otherwise would produce a 'materially different' figure of value from the auditor's valuation on a break-up basis." [1]

On the assumption that his interpretation contained in the above passage was correct, Ungoed-Thomas J. was of the opinion that Evershed M.R. had reasoned incorrectly. Where a valuation based on a principle is challenged on the ground that the principle was wrong then the only inquiry was whether it was wrong or not:-

> "It was immaterial ... that it was wrong in principle for the auditor to decide that the break-up value was alone admissible as an alternative to the going

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(1) (1971) 1 W.L.R. 840, 854

> concern. It was not that decision, but the valuation that was being attacked as wrong in principle and the valuation was, in the circumstances of that case, right in principle. However much the auditor stumbled in arriving at the right principle of valuation, he arrived at it."[1]

Ungoed Thomas J. distinguished Frank H. Wright (Constructions) Ltd. v Frodoor Ltd. which was a case where the mistake could not affect the valuation price. The difference in the present case was that the valuation had been made in a manner contrary to the directions given to the valuer. The case was one of "immaterial error". The correct principles had been invoked and the error (the insertion of the word 'not') did not indicate otherwise. Evershed M.R, purported to construct a quite different test. He seems to have held that in order to upset a valuation the valuer must not only have erred in principle but also it must be proved that a "materially different" valuation would have resulted had the correct principle been used. The twofold test was rejected by Ungoed-Thomas J.:-

> "... I do not conclude that there is any requirement of general application that where a valuation is made on an erroneous principle, yet the valuation nevertheless stands unless it is shown that a valuation on the right principle would produce a materially different figure from the figure of the valuation that he made ... The authorities ... to my mind establish that if a valuation is erroneous in principle, it is vitiated and cannot be relied on even though it is not established that the valuation figure is wrong."[1]

The writer respectfully agrees with Ungoed Thomas J.'s conclusions. As he pointed out,[2] if the position was

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(1) (1971) 1 W.L.R. 840, 856

(2) ibid 856

otherwise, the plaintiff could be faced with a very heavy burden of proof which might be almost impossible to satisfy. On the facts of the present case, however, Ungoed-Thomas J. held that the plaintiffs had established that had the valuation been made upon the correct principles, a substantially higher figure would have been obtained.

C. CONCLUSIONS

The law relating to the valuation of shares has now been considered in some length. The appointment of an expert whether he be the auditor or an outside party is a favoured method of valuing the shares of a company. Such a method recognises that there is a large 'opinion' element in such valuations. Despite this, the courts must intervene to prevent obvious injustices between the parties in much the same way as they do in the case of tribunals and inferior courts. In the case of pre-emptive rights articles, it is impossible to set the price at which shares are to be sold at some future date. Parties to a normal contract can always negotiate a price before they enter into the contract. A shareholder is bound by the articles and the courts supervisory jurisdiction is thus expecially important to prevent abuse.

APPENDIX I

A. Dale & Sclater. p. 87-88

(a) No shares shall be transferred to a person who is not a member so long as any member is willing to purchase the same at a fair price, provided that this restriction shall not apply to a transfer by a member to the wife, husband, parent, brother, sister, or child of such member.

(b) In order to ascertain whether any member is willing to purchase a share or shares the proposing transferor shall give notice in writing (hereinafter called the Transfer Notice) to the directors of the company of his desire to transfer such share or shares. The Transfer Notice may include several shares and in that case shall operate as if it were a separate notice in respect of each. Such Transfer Notice shall state the sum which the proposing transferor estimates as the fair price for such share or shares, and shall constitute the company the agent of the proposing transferor for the sale of such share or shares or any of them to any member of the company at the price stated in such transfer notice. The Transfer Notice shall not be revocable except with the consent in writing of the directors.

(c) If the company shall within one month of receipt of such Transfer Notice find a member (herinafter called the purchasing member) willing to purchase the share or shares and shall give notice thereof to the proposing transferor such proposing transferor shall upon payment of the stated price be bound to transfer the share or shares agreed to be purchased to the purchasing member.

(d) In the event of any difference arsing between the proposing transferor and the purchasing member as to the fair price of the share or shares to be sold such difference shall be referred to the auditor of the company for his decision and such auditor shall on the appointment of either party certify in writing the sum which in his opinion is the fair price for such share or shares and in so certifying the auditor shall be considered to be acting as an expert and not as an arbitrator and accordingly the Arbitration Act 1908 or any Act amending the same or in substitution therefor shall not apply.

(e) If in any case the proposing transferor after having become bound as aforesaid makes default in transferring the share or shares the company may receive the purchase money and shall thereupon cause the name of the purchasing member to be entered in the register of members as the holder of the share or shares purchased by him and shall hold the purchase money in trust for the retiring transferor. The receipt of the company for such purchase money shall be a good discharge to the purchasing member and after his name has been entered in the register of members in purported exercise of the aforesaid power, the validity of the proceedings shall not be questioned by any person.

(f) If the company shall not within the one month after being served with the Transfer Notice find a member ready and willing to purchase the share or shares and give notice as hereinbefore provided the proposing transferor shall at any time within three calendar months after the expiration of such period of one month be at liberty subject to the provisions contained in the following clause to sell and transfer the share or shares (or such of them as have not been disposed of in the meantime) to any person at not less than the fair price stated in the Transfer Notice or estimated as hereinbefore provided, provided that satisfactory proof of the bona fide payment of such price is given to the directors.

(g) Notwithstanding the provisions of paragraph (f) hereof the directors may refuse to register any transfer of a share or shares (a) where the company has a lien on such share or shares (b) where it is not proved to their satisfaction that the proposed transferee is a responsible person or (c) where the directors are of opinion that the proposed transferee is [illegible] membership of the company.

(h) The company in General Meeting may [illegible] time may vary rules as to the [illegible] in any notice served on the company [illegible] hereof shall be offered to members [illegible] to the purchase thereof and in particular may give any member a preferential right to purchase the same.

B. Lyle and Scott article.

"Subject to the provisions of cl. 7, cl. 8 and cl. 12 no registered holder of more than one per centum of the issued ordinary share capital of the company shall, without consent of the directors, be entitled to transfer any ordinary share for a nominal consideration or by way of security, and no transfer of ordinary shares by such a shareholder shall take place for an onerous consideration so long as any other ordinary shareholder is willing to purchase the same at a price, which shall be ascertained by agreement between the intending transferor and the directors and, failing agreement, at a price to be fixed by the auditor of the company for the time being. Any such ordinary shareholder who is desirous of transferring his ordinary shares shall inform the secretary in writing of the number of ordinary shares which he desires to transfer, and the price shall immediately be fixed as aforesaid. Thereafter the secretary shall intimate the same to all the other holders of ordinary shares simultaneously by written notice containing particulars of the intending transfer. Thereafter each ordinary shareholder receiving such notice shall be entitled, within fourteen days from the date of the notice, to intimate in writing to the secretary that he offers to purchase some or all of the shares mentioned in the intimation made to him; otherwise he shall not be a party to the offer. On the expiry of the foresaid fourteen days' notice, the secretary shall report the result to the directors who shall divide and appropriate the shares specified in the notice among the offerers in proportion to the number of ordinary shares held by them respectively or as near thereto as possible, provided that no offerer shall have apportioned to him a greater number of shares than he has offered to purchase. If any difficulty shall arise in apportioning the said shares or any of them, the directors may appropriate the shares in respect of which such difficulty arises among the offerers in such manner as they think fit or otherwise in their sole discretion. If after intimation by the secretary to the ordinary shareholders in manner aforesaid the number of shares offered to be purchased by them shall be less than the number of shares which the intending transferor gave notice of his desire to transfer, or if the offering ordinary shareholders shall fail to complete their purchase of such shares as shall be appropriated to them within one month after the date of such appropriation, the intending transferor may transfer the shares undisposed of to any person, whether a member of the company or not, as he thinks proper, provided that he shall not take for them less than the price to be ascertained as aforesaid, without first offering them in manner foresaid to the other ordinary shareholders at such lower price."

APPENDIX II

8. Article 24 of Table A is hereby deleted and in lieu thereof the following Clause is substituted :

The Directors shall refuse to register any transfer of a share or shares on or in respect of which any call or instalment is due and unpaid and the directors may in their absolute discretion refuse to register any transfer or transmission of a share or shares to any person to whom they do not approve without assigning any reason for such refusal.

9. The directors may decline to register any transfer or to permit the transmission of any share upon which the Company has a lien.

10. (a) Subject to the provisions of subclause (f) of this clause no share shall be sold or transferred by any member or by the personal representative of any deceased member unless and until the rights of pre-emption hereinafter conferred shall have been exhausted but every sale or transfer of shares shall be subject to the provisions of Clause 8 hereof.

(b) Every member or assignee as aforesaid who may desire to sell or to transfer any shares and every personal representative of a deceased member who may desire to sell or transfer any shares of such deceased member shall give notice in writing (hereinafter called "the transfer notice") to the Directors that he desires to make such sale or transfer. The transfer notice may include several shares and shall operate as a separate notice in respect of each. The transfer notice shall not be revocable except with the sanction of the Directors.

(c) The transfer notice shall constitute the Directors the agents of the person giving such notice for the sale of such shares either in one lot or in separate lots to any member or members of the Company or any other person or persons approved by the Directors in their absolute discretion at a price to be agreed upon between the person giving the transfer notice and the Directors or in the case of difference or failing any agreement then at a price to be determined by two independent valuers one to be appointed by the member desiring to sell and the other by the Directors and in the event of their disagreement by an umpire previously appointed by such valuers as being a fair market value of such shares.

(d) If the Directors as such agents shall within 28 days after such price has been agreed on or determined as aforesaid (as the case may be) find a member or members or other approved person or persons as aforesaid willing to purchase the shares at such price and shall give notice thereof to the member assignee or personal representative (as the case may be) he shall be bound upon payment of such price (subject to any lien which the Company may have under the Company's Articles of Association and to a deduction in respect thereof) to transfer the shares to such purchaser.

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be deemed at the expiration of that period to have actually given such notice in respect of such shares specifying as the value thereof the fair

APPENDIX III

TRANSFER OF SHARES

7. (a) (i) CLAUSES 24 and 25 of Table A shall not apply to the company.

(ii) NO person or member shall be entitled to sell, transfer or otherwise dispose of the beneficial interest in any shares if any member or other person whom the directors are prepared to register as a shareholder is willing to acquire the same pursuant to the provisions set out below.

(b) (i) EXCEPT where the transfer is made pursuant to Article 8 hereof every member or trustee in bankruptcy who may desire to sell transfer or otherwise dispose of the beneficial interest in any shares and every personal representative of a deceased member who may desire to sell or transfer any shares of the deceased member (such persons being included in the expression "the proposing transferor") shall give notice in writing (hereinafter called "a transfer notice") to the company that he desires to transfer the same. Such a transfer notice shall specify the sum the proposing transferor considers to be the value thereof and shall (subject as is hereinafter in this Article provided) constitute the company his agent for the sale of the shares to any member or members of the company or other person or persons nominated by the directors at the sum so fixed or at the option of the purchasing member or members or person or persons nominated by the directors of the company at the fair value to be fixed in accordance with paragraph (iv) of this Article. If a transfer notice shall include several shares it shall not operate as if it was a separate transfer notice in respect of each such share and the proposing transferor shall be under no obligation to sell or transfer part only of the shares specified in the transfer notice. Except as provided in paragraph (v) of this Article, the transfer notice shall not be revocable without the sanction of the directors in writing.

(ii) IN the event of a member, trustee in bankruptcy or personal representative as aforesaid selling transferring or otherwise disposing of the beneficial interest in any shares or giving any mortgage charge or proxy or making any declaration of trust or being party to any transaction intended to result in or which could result in the beneficial ownership of such shares being disposed of or transferred otherwise than in accordance with these Articles and failing to give a transfer notice as provided in paragraph (i) above the directors may give to the holder of such shares notice in writing calling upon the holder to give a transfer notice as provided in paragraph (i) above and unless within fourteen days of such notice the holder shall so give a transfer notice he shall

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be deemed at the expiration of that period to have actually given such notice in respect of such shares specifying as the value thereof the fair value as fixed in accordance with paragraph (iv) of this Article and thereupon the directors may proceed in all respects as if such member had so given such a transfer notice and all references to transfer notice in this Article shall be read so as to include such a notional transfer notice.

(iii) EXCEPT as provided in paragraph (v) of this Article if the company shall within the space of two calendar months after being served with such transfer notice find a member or members or any other person or persons whom the directors, in their discretion are prepared to register as a shareholder or shareholders, willing to purchase the shares (herein called "the transferee" or "the transferees") and shall give notice thereof to the proposing transferor he shall be bound upon payment of the price or fair value as herein provided (subject to any lien which the company may have under these Articles and by a deduction thereof) to transfer the shares to the transferee or transferees.

(iv) IN case any difference arises between the proposing transferor and a transferee as to the fair value of the shares such fair value shall be fixed on the application of either party by a person to be nominated by the President for the time being of the New Zealand Society of Accountants or if for any reason he refuses or is unable to make a nomination, then to be nominated by the President of the New Zealand Law Society Such person when nominated and in certifying the sum which in his opinion is the fair value of the shares shall be considered to be acting as an expert and not as an arbitrator, and accordingly the Arbitration Act, 1908, shall not apply.

(v) IF the fair value fixed as aforesaid is less than the sum specified by the proposing transferor in his transfer notice as the sum he considers to be the value of the shares the proposing transferor shall be entitled, at any time before the expiration of fourteen days after the date of his receiving notice of the fixing of the fair value as aforesaid, to revoke the transfer notice given by him. If the proposing transferor fails to revoke the trasnfer notice within the specified time then the same shall remain in full force and effect and he shall be bound thereby.

(vi) IF in any case the proposing transferor, after becoming bound as aforesaid, makes default in transferring the shares the company may execute a transfer or transfers of the shares on behalf of the proposing transferor and the company may receive the purchase money and shall thereupon cause the name or names of the transferee or transferees to be entered in the register as the holder and shall hold the purchase money (subject to any lien in favour of the company as aforesaid) in trust for the proposing transferor. The directors' receipt shall be a good discharge to the transferees for the purchase price and no question shall be raised as to the title of the transferees to the shares after they are registered as the holders thereof.

(vii) SUBJECT to the provisions of these Articles and until otherwise determined by the company by special resolution, the shares specified in any transfer notice given to the company as aforesaid shall be dealt with as follows:

(a) The said shares shall be offered in the first instance to the holders of the class of shares contained in the transfer notice as nearly as may be in proportion to the number of existing shares in that class held by them respectively, and the offer shall, in each case, limit the time within which the same, if not accepted, will be deemed to be declined, and may at the same time contain a notification that any such shareholder who desires an allotment of shares in excess of his proportion should, in his reply to the company, state how many excess shares he desires to have.

(b) If all such shareholders do not claim their proportions the unclaimed shares shall be used for satisfying the claims in excess.

(c) If thereafter any shares specified in a transfer notice and offered as aforesaid shall not have been accepted, the directors may offer such shares to any person or persons whom they are prepared to register as a sharehotder or shareholders.

(viii) IF the company shall not within the space of two calendar months after being served with a transfer notice find a member or members or other person or persons whom the directors are prepared to register as a shareholder or shareholders willing to purchase the shares and give notice in manner aforesaid, the proposing transferor shall at any time within three calendar months afterwards be at liberty to sell and transfer the shares to any person at a price not lower than the value specified in the transfer notice or the fair value fixed as aforesaid and the prior paragraphs of this Article shall not apply to such transfer.