(d) has conspired with others to effect the contravention

ASIC v Somerville (2009) NSWSC – Solicitors who assisted directors to set up "phoenix" companies – were involved in the breach of s 181(1) by the directors

TO WHOM DIRECTORS AND OFFICERS' DUTIES OWED?

- To "the company as a whole"

- Not to individual shareholders: **Percival v Wright [1902] 2 Ch 421; Coleman v Myers [1977] 2 NZLR 225; Brunninghausen v Glavanics [1999] NSWCA 199**
- Not to potential investors: **ASIC v Maxwell [2006] NSWCA 1052** **(no s181 duties owed to directors; though in breach of s180)**
- Not to employees: **Parke v Daily News [1962] Ch 927**
- But – as company approaches insolvency - duty to consider creditor interests: **Kinsela v Russell Kinsela Pty Ltd (in liq) (1986) 4 NSWLR 722**

GOOD FAITH

Bell Group Ltd (in liq) v Westpac Banking Corp (No 9) (2008) [2008] WASC 239	
RATIO	• The test whether directors acted bona fide in the interests of the company as a whole is largely (though by no means entirely) **subjective.** • It is a factual question that focuses on the state of mind of the directors. • The question is whether the directors (not the court) consider that the exercise of power is in the best interests of the company

I.e. It is highly unlikely that Charles believed this was in the best interests of Windsor, as he was actively working to divert assets and money away from Windsor to Chedwanne.

PROPER PURPOSE – BUT FOR TEST

Mills v Mills [1938] HCA 4	
FACTS	• Board approved bonus shares to ordinary shareholders – increasing voting power of the MD (providing the dividend distribution to be by way of bonus shares –in lieu of $$) • Minority director – argued the majority directors did not act bona fide in the best interests of company
RATIO	• HCA held: Conduct will not be invalidated merely because directors obtain a benefit - (recognised it is natural for directors to have an interest in the success of company) - **Provided – directors act fairly between the different classes of shareholders** • Court must consider: If there are several purposes behind an impugned act - Would the directors have still acted in the way they did "but for" the improper purpose (ie if it didn't exist) - **Was there a legitimate commercial purpose for the action?**

Harlowe's Nominees Pty Ltd v Woodside (Lake Entrance) Oil Co NL [1968] HCA 37	
RATIO	• Woodside's directors acted for proper purpose in issuing shares to a JV partner – Decision challenged by a substantial shareholder • ".. Although primarily the power is given to enable capital to be raised when required for the purposes of the company, there may be occasions when the directors may fairly and properly issue shares for other reasons - so long as those reasons relate to a purpose of benefiting the company as a whole, as distinguished from a purpose, for example, of maintaining control of the company in the hands of the directors themselves or their friends": at 493

Teck Corporation Ltd v Millar (1972) 33 DLR (3d) 288	

FACTS	• Afton: Competing offers from (1) Teck Corp (had acquired a major shareholding in Afton on-market; wanted board seat) and (2) Canex (Afton's directors – decided this to be of better value for Afton)
	• After Teck's share purchase – Afton agreed that Canex would
	  ○ Take over the operation of Afton's mining operations; and
	  ○ Receive 30% of Afton's shares at a lower price than shares to Teck Corp
	• This agreement – Had effect of frustrating Teck Corp's takeover

RATIO	• Afton's directors had not breached their duties - they were entitled to take account of a variety of factors in determining what was in the **best interests of the company** • **Conduct which frustrates a takeover will not of itself be improper - need to show some evidence of bad faith / improper purpose**

Australian Securities & Investments Commission v Adler (2002) 168 FLR 253	
RATIO	Allowing the company to purchase high-risk assets at a time when the company wanted to reduce its risk exposure would breach the duties owed under s 181

Ngurli Ltd v McCann [1953] HCA 39 (company took action against Clifford's executor McCann after his passing)	
FACTS	• Governing dir's share held by Clifford's brother Horace – and 60 ordinary shares held by Southcott's sister and her daughter • Under Clifford's will - Horace took governing shares with "super voting" (4x) powers, and power to manage company - But only for the administration of Clifford's estate – his sister and other relatives would control the Ngurli companies • **Horace – Used his governing shares to issue further shares to executor as payment for the Ngurli companies' debts** – based on the understanding that he would then purchase back the shares - and have control of Ngurli et al • Clifford's sister – Challenged Horace's actions – improper, ulterior purpose
RATIO	• **HELD:** She had the right to rectify the share registers of the Ngurli companies to remove shares invalidly issued by Horace **(power to remove shares was exercised for an improper purpose)**

Howard Smith Ltd v Ampol Petroleum [1974] AC 821- KEY CASE; Issuing shares to assist with a takeover – was an improper purpose	
FACTS	• Howard Smith Ltd and Ampol Ltd – both competing for Miller Ltd • Ampol Ltd (and associates) owned 55% of shares in Miller • Directors of Miller – wanted to attract a higher bidder - So issued shares to HS on the proviso that HS would offer more $$ for Miller than Ampol - This share issue diluted Miller's share capital – so • Ampol's 55% shareholding would have less voting power)
RATIO	• **Ampol – Challenged Miller's share issue - made for an improper purpose** • **UKPC – Held Miller's directors were acting for an improper purpose in issuing the shares to HS – seeking to frustrate Ampol's hostile takeover** **Enunciated a 2-step test:** • **What was the nature of the power? (power to issue shares to raise $$)** • **Consider the substantial purpose for which the power was exercised - reach a conclusion whether that purpose was (a) proper or (b) improper**

Whitehouse v Carlton Hotel Pty Ltd (1987) 162 CLR 285	
FACTS	• Mr Whitehouse – "Governing" director of family company • Three classes of shares – Class A (held by Mr W. – unrestricted voting powers); Class B (held by Mrs W. – only permitted voting after Mr W. died); and Class C (held by the children – provided only profit sharing, no voting rights) • After divorce – Mr W. issued Class B shares to his two sons (who sided with him, while daughters sided with Mrs W.), to ensure his sons maintained control over company once he died • Mr W. – then fell out with both sons – passed board resolution to amend the share register to remove the Class B shares • Sons – Successfully sought rectification of the share register
RATIO	HELD: Mr W. had acted for an improper purpose in issuing the shares - manipulating voting power of company **RATIO: Directors and other officers must use their powers for their intended purpose, not a collateral purpose**

S187- DIRECTORS OF WHOLLY-OWNED SUBSIDIARIES

S187: A director of a corporation that is a wholly-owned subsidiary of a body corporate is taken to act in good faith in the best interests of the subsidiary if: (a) the constitution of the subsidiary expressly authorises the director to act in the best interests of the holding company; and (b) the director acts in good faith in the best interests of the holding company; and (c) the subsidiary is not insolvent at the time the director acts and does not become insolvent because of the director's act

Directors of a subsidiary within a corporate group are obliged to consider the interests of their particular company – rather than sacrificing these interests in favour of the broader corporate group: **Walker v Wimborne [1976] HCA 7**

INTERESTS OF COMPANY'S CREDITORS

Kinsela v Russell Kinsela Pty Ltd (in liq) (1986) 4 NSWLR 722

- As a company enters insolvency – the primary focus of directors' and officers' duties transforms from shareholders to creditors
- The directors of a family funeral business breached their duties to the company by entering into an uncommercial transaction when the company was approaching insolvency - **signing a lease with a closely related company on terms much lower than the prevailing market rate**

REMEDIES FOR BREACHES

By ASIC – regulatory considerations:

- **Criminal prosecutions –s184**

S184(1) A director or other officer of a corporation commits an offence if they:

(a) are reckless; or
(b) are dishonest;

and fail to exercise their powers and discharge their duties:

(c) in good faith in the best interests of the corporation; or
(d) for a proper purpose.

- **Civil penalties**
- **Civil litigation**

Members – private considerations; common law and equitable remedies:

- Damages
- Account of profits
- Constructive trusts
- Injunctions (see **s1324**)

See also **s 185: ss 180 to 184** have effect in addition to, and not in derogation of, any rule of law in relation to the duty or liability of a person because of their office or employment in relation to corporation

MODULE 11: MANAGING CONFLICTS OF INTEREST

1. **S182-** MISUSE OF **<u>POSITION</u>** (**civil penalty provision**)
2. **S183-** MISUSE OF **<u>INFORMATION</u>**
3. **S184-** GOOD FAITH, USE OF POSITION AND USE OF INFORMATION- **CRIMINAL OFFENCES**

- **MANAGING CONFLICTS OF INTEREST- S191, 193, 195, 194**

  - **ASIC;** Likely to go for civil; or civil penalties or criminal
  - **MEMBERS;** May want accounts of profits; constructive trusts; injunctions etc. (conflicts of interest / fiduciary duties in the context of members)