[HIGH COURT OF AUSTRALIA.]

ROFE . . . . APPELLANT;
RESPONDENT,

AND

CAMPBELL . . . . RESPONDENT.
APPLICANT,

ON APPEAL FROM THE SUPREME COURT OF NEW SOUTH WALES.

H. C. OF A. 1931.

SYDNEY, *April* 14; *May* 1.

Gavan Duffy C.J., Rich, Starke, Dixon and McTiernan JJ.

Company—Capital—Memorandum of association—Ordinary and preference shares—Power of directors to issue preference shares—No positive provision in articles.

Although the memorandum of association of a company empowers the division of its original capital into preference as well as into ordinary shares, such power cannot be exercised by the directors unless authorized so to do by positive provision in the articles of association; such provision being either in express terms or by necessary intendment.

The articles of association of a company by art. 10 provided that "The shares shall be under the control of the directors who may allot or otherwise dispose of the same to such persons on such terms and conditions and at such times as the directors think fit and with full power to give to any person the call of any shares either at par or at a premium and for such time and for such consideration as the directors think fit. The directors may reserve any of the shares in the original or increased capital of the company upon such terms as to payment for same and otherwise as they may deem expedient."

Held, that this article did not deal with the classification of shares but only with the terms and conditions of their allotment and disposal.

Decision of the Supreme Court of New South Wales (*Harvey* C.J. in Eq.) reversed on this point.

Art. 117 provided that "The management of the business of the company shall be vested in the directors who in addition to the powers and authorities by these presents or otherwise expressly conferred upon them may exercise all such powers and do all such acts and things as may be exercised or done by the company and are not hereby or by statute expressly directed or required to be exercised or done by the company in general meeting but subject nevertheless to the provisions of the statutes and of these presents and regulations from time to time made by the company in general meeting. Provided that no regulations so made shall invalidate any prior act of the directors which would have been valid if such regulations had not been made."

Held, that this article was concerned with the management of the business of the company and not with the relations of the members *inter se*. It did not operate to authorize the directors to issue original capital as preference shares.

Decision of the Supreme Court of New South Wales (*Harvey* C.J. in Eq.) affirmed on this point.

APPEAL from the Supreme Court of New South Wales.

In a list of contributories compiled by William Harrington Palmer, as official liquidator of Marlow Rolls Theatres Ltd., the name of Thomas Ernest Rofe appeared as being the owner in his own right of 8,000 £1 preference shares. An application to settle such list, by the official liquidator to the Supreme Court in its equitable jurisdiction, was heard before the Master in Equity when Rofe claimed that no preference shares were ever validly created by the Company in accordance with its memorandum or articles of association or otherwise, and that no preference shares in the Company had ever been validly allotted to him, and, therefore, he ought not to be placed on the list of contributories of the Company in respect of the said preference shares or any of them. He further claimed that he had never received any share certificates from the Company in respect of the shares nor had he received any dividends in respect thereof. The prospectus of the Company showed that both 10 per cent cumulative participating preference shares and ordinary shares of £1 each were offered for public subscription. Rofe's application for shares, made on 7th March 1929, was, so far as material, as follows: "Referring to the prospectus of your Company, I hereby apply for 8,000 10 per cent cumulative participating preference shares in your Company"; the application being made subject to certain terms and conditions as to payment, calls, and appointment as a director at a remuneration of not less than £500 per annum. The letter from Rofe was dealt with at a meeting of the directors

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held on 12th March, when it was resolved that "the letter and shares be treated and allotted in accordance with the articles of association"; and two days later Rofe was informed in writing by the secretary of the Company that "in accordance with your application the directors of the above Company have allotted to you 8,000 preference shares." The only reference in the memorandum of association to the shares of the Company was clause 5, which stated that "the capital of the Company is £250,000 divided into 250,000 shares of one pound each, with power to divide the shares in the capital for the time being into several classes, and to attach thereto respectively and preferential deferred, qualified, or special rights, privileges, or conditions." The articles of association included (*inter alia*) the following articles:—"7. The capital is £250,000 and comprises 250,000 shares of £1 each." "10. The shares shall be under the control of the directors who may allot or otherwise dispose of the same to such persons on such terms and conditions and at such times as the directors think fit and with full power to give to any person the call of any shares either at par or at a premium and for such time and for such consideration as the directors think fit. The directors may reserve any of the shares in the original or increased capital of the Company upon such terms as to payment for same and otherwise as they may deem expedient." "46. The Company in general meeting may from time to time increase the capital by the creation of new shares of such amount as may be deemed expedient." "48. The new shares shall be issued to such persons and upon such terms and conditions and with such rights and privileges annexed thereto as the general meeting resolving upon the creation thereof shall direct and if no direction be given as the directors shall determine and in particular such shares may be issued with a preferential or qualified right to dividends and in the distribution of the assets of the Company and with a special or without any right of voting." "117. The management of the business of the Company shall be vested in the directors who in addition to the powers and authorities by these presents or otherwise expressly conferred upon them may exercise all such powers and do all such acts and things as may be exercised or done by the Company and are not hereby or by statute expressly directed or required to be exercised or done by the Company in general meeting but subject nevertheless to the provisions of the statutes and of these presents and regulations from time to time made by the Company in general meeting. Provided that no regulations so made shall invalidate any prior act of the directors which would have been valid if such regulations had not been made." "127. Subject to the rights attached to shares issued on special conditions and subject as aforesaid the profits of the Company shall be divisible among the members in proportion to the capital paid up or deemed to be paid up on the shares held by them respectively :— " The Master excluded Rofe's name from the list of preferent shareholders, but expressed no opinion as to whether such name should appear on the list of ordinary shareholders, the question whether it should be so included not having been raised on the application.

On a summons to vary the Master's certificate and order taken out by Alexander Ewen Campbell, who had been appointed the official liquidator of the Company on the death of William Harrington Palmer, *Harvey* C.J. in Eq. held that under the articles the directors were authorized to issue shares with special preferential rights in dividends or a preferential right to shares in the capital in the event of liquidation if they thought fit, and that therefore the directors had power to issue the shares in question to Rofe, and that his name should Not be removed from the list of contributories on that ground.

From that decision Rofe now appealed to the High Court.

It was announced by the parties that the appeal would be limited to the question as to whether upon a proper construction of the articles the directors were authorized to issue shares in the original capital of the Company with preferential rights attached thereto.

Browne K.C. (with him *Dudley Williams*), for the appellant. The articles of association must be looked at in order to determine whether the directors had power to issue preference shares. The subject articles are based upon Form 251, *Palmer's Company Precedents*, 13th ed., Part I., pp. 622 *et seqq.* It cannot be said that art. 10 empowers the directors to issue preference shares ; the

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phrase "terms and conditions" in that article is not wide enough to confer such a power, it refers only to the sale of shares. As to whether future capital shall be ordinary or preference capital can only be determined by a resolution of the Company. The directors have no power to annex preferential rights to any shares, and such a power cannot be taken under the articles because the memorandum of association is silent on the matter (*Hutton* v. *Scarborough Cliff Hotel Co.* (*A*) (1)). Whether such words, purporting to grant the power, are there or not is immaterial (*Andrews* v. *Gas Meter Co.* (2), which overruled *Hutton* v. *Scarborough Cliff Hotel Co.* (*B*) (3)). The usual method of creating preference shares is by fixing in the articles of association what the shares are. Art. 10 does not confer rights and privileges. Under that article the directors may offer shares to shareholders and others, and decide as to the terms of allotment, and the limitation and times of calls. The power of issuing preference shares is retained in the hands of the Company. As to what is meant by "issue" see *Buckley* on the *Companies Acts*, 10th ed., p. 214.

[RICH J. referred to *Ramsbottom* v. *Scottish American Investment Co.* (4).]

Such a power in the hands of directors would be open to grave abuse, and therefore it is most unlikely that it was intended to give them such power. There is nothing in art. 127 which makes it necessary to give such a wide meaning to the words "conditions." An article similar to art. 117 was dealt with in *Hutton* v. *Scarborough Cliff Hotel Co.* (*A*) (1), and in *Andrews* v. *Gas Meter Co.* (5) the decision in that case was held to be correct.

[DIXON J. But in *Hutton's Case* (1) the material clause did not appear in the memorandum of association.]

The decision of *Harvey* C.J. in Eq. that art. 117 is simply an article which deals with the powers of management of the business of the Company is correct. It does not follow that because the Company has the power to do certain things the directors necessarily have the same power. Art. 117 only confers a power to exercise

(1) (1865) 2 Dr. & Sm. 514 ; 62 E.R. 715.
(2) (1897) 1 Ch. 361.
(3) (1865) 2 Dr. & Sm. 521 ; 62 E.R. 717.
(4) (1891) 28 Sc. L.R. 419.
(5) (1897) 1 Ch., at p. 368.

the objects of the Company for the purpose of carrying on the Company's business (*Foster* v. *Foster* (1)).

Weston, for the respondent. The implication can be read into art. 7 or derived from it. It is competent to the Company or the directors to say that shares of a certain classification shall be issued. The memorandum of association and art. 7 do nothing more than limit the aliquot portion of each share. The memorandum of association, and not the articles, is the place to find the necessary power. Clause 5 of the memorandum of association creates a presently exercisable power to create preferences in regard to existing capital, and art. 117 transfers that power to the directors. It is not unusual for such power to be vested in directors. In order to give a power to issue preference shares it is sufficient that the provision should be made either in the memorandum of association or in the articles (*Andrews* v. *Gas Meter Co.* (2)). If the Court is of opinion that on a proper construction of art. 117 the power in the memorandum of association is transferred to the directors, a consideration of art. 10 is unnecessary. A right to impose conditions in connection with the issue of shares includes a power to attach a preference as to dividends (*Harrison* v. *Mexican Railway Co.* (3)). The power given by clause 5 of the memorandum of association is a self-executing power to divide the shares in existence into different classes. Art. 117 indicates that the Company proposed to exercise the power through the directors when the business of the Company required it. Every power which the Company possesses vests in the directors. In construing the articles regard should be given to the history of company law and the need of such articles when they were originally drawn. It may be that certain articles were inserted for more abundant caution and at worst are unnecessary. The word "conditions" in art. 10 is quite adequate for the purpose of authorizing the directors to attach a preference to shares. What is encompassed by the word "conditions" is indicated by the sense in which it is used in art. 127. The articles referred to in *Palmer's Company Precedents*, 13th ed., Part I., pp.

(1) (1916) 1 Ch. 532, at p. 546.
(2) (1897) 1 Ch., at pp. 368 *et seqq.*
(3) (1875) L.R. 19 Eq. 358, at p. 366.

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622 *et seqq.*, are quite different from the articles here under review, and reference to them does not serve any useful purpose. The decision in *Foster* v. *Foster* (1) is not applicable: it applies only to the memorandum and articles there in question, which are different from the articles in this case.

Browne K.C., in reply. The statement by *Rigby* L.J. in *Andrews* v. *Gas Meter Co.* (2) is *obiter dictum* only. The words under review in *Harrison* v. *Mexican Railway Co.* (3) were "privileges and conditions," and the decision does not go so far as to say that in the absence of the word "privilege" the word "condition" would be sufficient. The construction sought to be put upon art. 117 by the respondent would make many other articles unnecessary.

Cur. adv. vult.

May 1. The following written judgments were delivered:—

GAVAN DUFFY C.J., RICH, DIXON AND MCTIERNAN JJ. This is an appeal from an order of *Harvey* C.J. in Eq. by which he allowed an appeal by the official liquidator to the Court under sec. 85 of the *Companies Act* 1899 (N.S.W.) from the Master who, in settling the list of contributories, excluded the name of the appellant from the list of preferent shareholders, where the official liquidator had placed it. His Honor reversed the decision of the Master and restored the name of the appellant to its place among the preferent shareholders on the list of contributories. The appellant applied for 8,000 preference shares of the original capital of the Company which were offered by the directors for subscription, and his application was accepted and the shares allotted to him by the directors. The appellant's contention was that he did not become a member of the Company, because the articles of association did not authorize the issue of any of the original capital of the Company as preference shares and he had agreed only to take preference shares. His Honor, after examining the relevant articles of association, reached the conclusion that the directors were authorized by the constitution

(1) (1916) 1 Ch. 532.
(2) (1897) 1 Ch., at p. 372.
(3) (1875) L.R. 19 Eq. 358.

of the Company to issue part of its original capital as preference shares and make the allotment in question. Upon the appeal from this decision the parties agreed that our decision must be confined to the question whether the directors were authorized by the articles to issue part of the original capital as preference shares because, if we were of opinion that the articles did not confer such an authority, questions remained for consideration in the Court below whether, notwithstanding that the contract of membership in all its terms was made by the directors without authority in the first instance, the appellant might be retained upon the list of contributories either as a preferent or as an ordinary shareholder. (Cf. *Waverley Hydropathic Co.* v. *Barrowman* (1); and, if there be a question of ratification, reference may be made to *Marshall's Valve Gear Co.* v. *Manning, Wardle & Co.* (2) and to *Attorney-General for the Dominion of Canada* v. *Standard Trust Co. of New York* (3).) It was not and could not be contended that the issue of part of the original capital in the form of preference shares was beyond the corporate powers of the Company. Not only is there nothing in the memorandum of association inconsistent with the issue of preference capital, but clause 5, which states the amount and division of the Company's capital, adds the words: "with power to divide the shares in the capital for the time being into several classes, and to attach thereto respectively and" (*sic*) "preferential deferred, qualified, or special rights, privileges, or conditions."

The question is not one of the existence of a corporate power of the Company to issue preference shares, but of the title of the directors to exercise that power. Moreover, we do not think the question depends upon restrictions, express or implied, contained in the articles preventing inequality or differentiation between shares forming part of the original capital. It is true that art. 7 provides that the capital is £250,000 and comprises 250,000 shares of £1 each, but it can no longer be maintained that this amounts to or imports a contract *inter socios* that the shares shall be uniform and rank equally (*Andrews* v. *Gas Meter Co.* (4)). The true

(1) (1895) 33 Sc.L.R. 131.

(2) (1909) 1 Ch. 267, at p. 272, per *Neville* J.

(3) (1911) A.C. 498, at p. 504, per Viscount *Haldane*.

(4) (1897) 1 Ch. 361.

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question is whether the articles contain a positive provision empowering the directors to attach to part of the original capital preferential rights. An express power contained in the articles is enough to enable the directors to issue capital as preference shares (*Palmer's Company Precedents*, Part I., 12th ed., pp. 465-466; *Turnbull & Jones* v. *Turnbull* (1)), but the power must be given to them by the articles expressly or by necessary intendment. The learned Judge was of opinion that in fact the power was so conferred upon the directors by art. 10 of the articles of association. This article is as follows:—"The shares shall be under the control of the directors who may allot or otherwise dispose of the same to such persons on such terms and conditions and at such times as the directors think fit and with full power to give to any person the call of any shares either at par or at a premium and for such time and for such consideration as the directors think fit. The directors may reserve any of the shares in the original or increased capital of the Company upon such terms as to payment for same and otherwise as they may deem expedient." We find ourselves unable to agree with this interpretation of the article. We think this article does not deal with the classification of shares but only with the terms and conditions of their allotment and disposal. It places the shares such as they are under the control of the directors. Those shares, with whatever rights, privileges, or priorities belong to them, may be allotted or otherwise disposed of by the directors. The terms and conditions upon which they may be disposed of or allotted are the terms of the contract with the applicant and not part of the rights attached to or inherent in the share as property. We do not think that the words "terms and conditions" can bear so wide a meaning as would be required to authorize the addition to shares of rights and privileges affecting not merely the relation of the applicant to the Company but the relative rights and priorities of existing and future members of the Company. The learned Judge appears to have relied on *Harrison* v. *Mexican Railway Co.* (2). But the language of the article in that case can only bear the meaning that the privileges with which it was sold were to belong to the

(1) (1913) 32 N.Z.L.R. 670.

(2) (1875) L.R. 19 Eq. 358.

share. We think our conclusion upon the meaning of art. 10 is supported by the provisions made in arts. 46-52 in relation to new capital which specifically authorize the classification of that capital and its issue with preferential and qualified rights. The respondent, however, contended that art. 117 operated to authorize the directors to issue original capital as preference shares. Art. 117 provides as follows :—" The management of the business of the Company shall be vested in the directors who in addition to the powers and authorities by these presents or otherwise expressly conferred upon them may exercise all such powers and do all such acts and things as may be exercised or done by the Company and are not hereby or by statute expressly directed or required to be exercised or done by the Company in general meeting but subject nevertheless to the provisions of the statutes and of these presents and regulations from time to time made by the Company in general meeting. Provided that no regulations so made shall invalidate any prior act of the directors which would have been valid if such regulations had not been made." We agree with the learned Judge in thinking that this article has no such operation. Our reason for this view lies in the terms of the article itself. It is concerned with the management of the business of the Company and not with the relations of the members of the Company *inter se.* This distinction is well expressed in a passage from the judgment of *Bradley* J. in *Railway Co.* v. *Allerton* (1), quoted in *Brice* on *Ultra Vires*, 3rd ed., pp. 579, 580.

For these reasons we are of opinion that the appeal should be allowed and the order of *Harvey* C.J. in Eq. discharged.

The matter should be remitted to the Supreme Court to be dealt with as may be just.

The appellant must have his costs here and in the Court below out of the assets of the Company.

STARKE J. The capital of the Marlow-Rolls Theatre Limited is, as specified in the memorandum of association, £250,000, divided into 250,000 shares of £1 each, with power to divide the shares in the capital for the time being into several classes, and to attach thereto respectively any preferential deferred, qualified or special

(1) (1873) 18 Wall. 233, at pp. 235-236.

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rights, privileges or conditions. This capital clause is an old form, and the power taken by it was inserted to meet the decision in *Hutton* v. *Scarborough Cliff Hotel Co.* (*B*) (1), now overruled (*Andrews* v. *Gas Meter Co.* (2); *Palmer's Company Precedents*, 6th ed., vol. I., p. 221; 12th ed., vol. I., p. 552). The memorandum must specify the amount of capital with which the company proposes to be registered, divided into shares of a certain fixed amount (*Companies Act* 1899 (N.S.W.), sec. 7), but in other respects "the rights of the shareholders in respect of their shares and the terms on which additional capital may be raised are matters to be regulated by the articles of association rather than by the memorandum." The inclusion, however, of the power above mentioned in the memorandum of association is not forbidden by law (*Andrews* v. *Gas Meter Co.*; *In re Welsbach Incandescent Gas Light Co.* (3)). It might, I apprehend, be exercised by the shareholders of the company in a meeting duly convened, or without a formal meeting if all the shareholders in fact assented to the issue of shares with preferential rights attached thereto (see *Parker & Cooper Ltd.* v. *Reading* (4)), and without any alteration or addition to the articles of association. But the question in this case is whether the directors of the Company have, without any assent of the shareholders, authority to issue to the appellant Rofe 8,000 shares in the original capital of the Company with a cumulative participating preference of ten per cent per annum attached thereto. If the capital of the Company had been increased by the creation of new shares, art. 48 would govern the matter. It provides: "The new shares shall be issued to such persons and upon such terms and conditions and with such rights and privileges annexed thereto as the general meeting resolving upon the creation thereof shall direct and if no direction be given as the directors shall determine and in particular such shares may be issued with a preferential or qualified right to dividends and in the distribution of the assets of the Company and with a special or without any right of voting." But, as to the original capital, the authority of the directors depends upon

(1) (1865) 2 Dr. & Sm. 521; 62 E.R. 717.
(2) (1897) 1 Ch. 361.
(3) (1904) 1 Ch. 87.
(4) (1926) Ch. 975.

the construction of other articles of association. Art. 117 provides: "The management of the business of the Company shall be vested in the directors who in addition to the powers and authorities by these presents or otherwise expressly conferred upon them may exercise all such powers and do all such acts and things as may be exercised or done by the Company and are not hereby or by statute expressly directed or required to be exercised or done by the Company in general meeting. . . ." In the construction of this article, it is not unimportant to observe that the directors may delegate their powers to committees of their own number, or to the managing director (see arts. 106, 111). Articles in the form of clause 117 authorize the directors doing anything the Company can do (*In re Anglo-Danubian Steam Navigation and Colliery Co.* (1); *In re Patent File Co.*; *Ex parte Birmingham Banking Co.* (2); *In re Pyle Works* [*No.* 2] (3)). But the opening words of the present article suggest this limitation—that what they do must be done in the course of the management of the business of the Company, for the purpose of its business operations; and that, in my opinion, is its true scope. Express authority must be found for directors to vary the capital of a company or to attach privileges and conditions to shares in the capital, and no such authority can be found in the general words of art. 117. (See *Brice* on *Ultra Vires*, 3rd ed., p. 579.) Next, art. 10 provides: "The shares shall be under the control of the directors who may allot or otherwise dispose of the same . . . on such terms and conditions and at such times as the directors think fit and with full power to give any person the call of any shares either at par or at a premium and for such time and for such consideration as the directors think fit. . . ." But that clause, in my opinion, only gives the directors control over the shares of the Company as they exist or are specified in the memorandum of association, with such rights and privileges attached thereto as may be found in it or in the articles of association. It contains no authority to divide the capital into classes or to attach preferential rights or privileges thereto.

(1) (1875) L.R. 20 Eq. 339. (2) (1870) 6 Ch. App. 83.
(3) (1891) 1 Ch. 173.

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Starke J.

The appeal should be allowed and the matter remitted to the Supreme Court.

It may be that the appellant can be retained upon the list of contributories of the Company upon some other basis, but this Court, as I understand the matter, confines itself, at the request of the parties, to the determination of a pure question of law, namely, whether the articles of association of the Company upon their proper construction authorize the directors to issue shares in the original capital of the Company with preferential rights attached thereto.

Appeal allowed. Order of Harvey C.J. in Eq. discharged. Matter remitted to the Supreme Court to be dealt with as may be just. Costs of the appellant here and in the Court below out of the assets of the Company.

Solicitors for the appellant, *Lane, Rex & Co.*
Solicitors for the respondent, *Sly & Russell.*

J. B