[HIGH COURT OF AUSTRALIA.]

RICHARD BRADY FRANKS LIMITED . . APPELLANT;
PLAINTIFF,

AND

PRICE AND OTHERS . . . . . RESPONDENTS.
DEFENDANTS,

ON APPEAL FROM THE SUPREME COURT OF NEW SOUTH WALES.

H. C. OF A. 1937.

SYDNEY, *July* 30; *Aug.* 3, 4, 17.

Latham C.J., Rich and Dixon JJ.

Company—Debentures—Issue—Resolutions on two different dates—Competent quorum of directors present on second date only—Validity of debentures—Bona fides of directors.

Appeal—Questions of fact—Functions of court of appeal.

At a meeting of a board of directors of a company on 3rd November 1931 a resolution was passed for the issue of a series of debentures to certain named persons. At a further board meeting on 17th November 1931 a resolution was passed that "the series of debentures . . . prepared in pursuance of resolution of 3rd November, 1931, be sealed and issued to the respective persons named therein." At the meeting on 17th November a quorum of directors competent to vote was present and voted, but at the earlier meeting there was no such quorum present.

Held that the resolution of 17th November was a substantive and independent exercise of the directors' power to bind the company and not a mere formal carrying out of a decision finally resolved upon at the earlier meeting, and that it contained clear authority for the issue of the debentures; therefore the validity of the debentures could not be attacked on the ground that they purported to be issued pursuant to a resolution passed at a meeting when the requisite quorum of directors was not present.

Cox v. *Dublin City Distillery* [*No.* 2], (1915) 1 I.R. 345, distinguished.

The company had for some time been in financial difficulties and the prospect of an improvement was not good. From time to time certain of the directors

and other persons had lent money to the company on "short call" and had guaranteed the company's overdraft. The debentures were issued to these directors and persons. The plaintiff claimed that the debentures were not issued bona fide and, therefore, were invalid. The trial judge found on the evidence that in issuing the debentures the directors acted in the interests of the company and of the general body of shareholders and not in the interests of the proposed debenture holders.

Held that the plaintiff had not discharged the onus of establishing want of bona fides on the part of the directors, and, upon the evidence, the finding of the trial judge should not be disturbed.

Upon questions of fact an appeal court will not interfere with the decision of the trial judge unless there is some good and special reason to throw doubt upon the soundness of his conclusions.

Decision of the Supreme Court of New South Wales (*Long Innes* C.J. in Eq.): *Richard Brady Franks Ltd.* v. *Price*, (1936) 37 S.R. (N.S.W.) 37; 53 W.N. (N.S.W.) 238, affirmed.

APPEAL from the Supreme Court of New South Wales.

In a suit brought in the Supreme Court of New South Wales in its equitable jurisdiction by Richard Brady Franks Ltd. against Herbert Price, Rose Eaton Thwaites, Annie Adeline Price, Otto Christian Dorhauer, Herbert Robert Holt, Richard Brady & Sons Ltd., Alfred Joseph Morgan and Otto Christian Dorhauer (as executors of the will of Frederick William Dorhauer, deceased) and the Permanent Trustee Co. of New South Wales Ltd. (as executor of the will of John Brady, deceased), the plaintiff sought a declaration that certain debentures were inoperative and void, and an inquiry as to the dealings with the debentures and an account of all moneys in connection therewith. No appearance was entered by or on behalf of the defendant Richard Brady & Sons Ltd. The defendants Herbert Robert Holt and the Permanent Trustee Co. of New South Wales Ltd. entered a submitting appearance, and the remainder of the defendants entered a disputing appearance.

The facts sufficiently appear in the judgment of *Long Innes* C.J. in Eq., in which his Honour said :—

"In this case the plaintiff company (hereinafter called the company) whose principal object was to carry on the business of manufacturers, importers and sellers of all kinds of steel and metal work for doors, windows, stairs, lifts and other appliances used in any building or

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

industry, and which was incorporated on 26th March 1926 with a capital of £25,000 divided into 25,000 shares of one pound each, the whole of which have been issued and are fully paid, claims a declaration that certain debentures and sub-divided debentures aggregating £10,150 are wholly invalid and inoperative as against the plaintiff on the ground that the issue of the same was *ultra vires* of the company and on certain other grounds which have been raised by various amendments of the statement of claim.

"The issue of debentures was clearly within the powers of the company, but the allegation that the issue of the debentures in question was *ultra vires* of the company has by the particulars supplied been modified to the charge that their issue was *ultra vires* of the directors under the circumstances alleged.

"The present case differs from most cases in which relief of this nature is sought in that it has been instituted, not for the purpose of avoiding the debentures in the interests of the general body of creditors, for it is not suggested that the assets when realized will not be amply sufficient to satisfy the claims of all creditors, including those of the present debenture holders, who if the debentures are set aside will be entitled to rank as unsecured creditors of the company, but at the instance, and risk, of a number of shareholders who are desirous of obtaining a declaration that the debentures are invalid as a preliminary step to the institution of other proceedings for damages for trespass and conversion against the receivers for the debenture holders, who, on 24th June 1932, entered into possession under one of the debentures in question, and carried on the business of the company from that date until it went into liquidation on 21st November 1933.

"In view of the fact that the receivers for the debenture holders were two of the directors of the company, including the chairman of the board, that they carried on the business of the company in the same manner as it had theretofore been carried on by the board, and that, I understand, no assets were converted by them, it is difficult to see what damages, other than nominal, could be recovered in that respect in such subsequent proceedings; and as the case made by the company in this suit and by those shareholders at whose instance it was instituted is that the financial condition and

prospects of the company at the date of the issue of the debentures were such that liquidation was inevitable, it is equally difficult to see what damages could be recovered for loss of reputation consequent upon such entry into possession by the receivers for the debenture holders; but, notwithstanding, this case has been prosecuted with great zeal and the hearing has engaged the attention of the court for thirteen days, seven of which were taken up by the argument.

"The first two grounds upon which the validity of the debentures was impeached may be briefly stated as follows: (*a*) that the issue of the debentures was not a proper exercise by the directors of their powers; (*b*) that such issue was not in fact authorized by a quorum of directors competent to transact and vote upon the business in question.

"The question whether the company is entitled to succeed on either of those first two grounds depends upon the determination of disputed questions of fact, and before stating or discussing the further grounds upon which it rests its claim, it is necessary to determine those questions of fact. It will be convenient to deal first with the question whether the issue of the debentures was in fact authorized by a quorum of directors competent to transact and vote upon that business.

"On 17th November 1931, on which date the original series of debentures was issued, the board of directors of the company consisted of six persons; the defendant Herbert Price, who was chairman of the board; Frederick William Dorhauer, who died on 10th April 1934, and whose legal personal representatives are the defendants Alfred Joseph Morgan and Otto Christian Dorhauer; the defendant Herbert Robert Holt; John Brady, who died on 21st August 1933, whose legal personal representative is the defendant, the Permanent Trustee Co. of New South Wales Ltd., and who was, I understand, at the material date a shareholder in and a director of Richard Brady & Sons Ltd.; William Salisbury Baker and Frank Reginald Alldritt.

"The debentures issued on 17th November 1931 were nine in number, short particulars of which are: (i) £1,000 to the defendant Rose Eaton Thwaites; (ii) £1,000 to the defendant Annie Adeline

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

Price, wife of the defendant Herbert Price ; (iii) £1,000 to the defendant Otto Christian Dorhauer ; (iv) £1,000 to Frederick William Dorhauer ; (v) £250 to the defendant Herbert Robert Holt ; (vi) £400 to the defendant Richard Brady & Sons Ltd. ; (vii) £5,000 to the defendant Herbert Price and Frederick William Dorhauer ; (viii) £250 to Frederick William Dorhauer ; and (ix) £250 to the defendant Otto Christian Dorhauer. Of these all except that numbered (vii) were issued as securities for loans previously made to the company at short call ; and that numbered (vii) was to secure Herbert Price and Frederick William Dorhauer in respect of a guarantee given by them to the Bank of New South Wales in respect of the company's overdraft with a limit of that amount. The joint debenture of £5,000 was accompanied by a collateral agreement of even date between the company of the one part and Herbert Price and Frederick William Dorhauer (therein called the guarantors) of the other, one clause of which provided that should the guarantors desire to sell the whole or any part or parts of the said debenture the solicitors of the company should prepare the transfer and any subdivided debentures rendered necessary, and that the company should execute any such subdivided debentures and issue them " to the purchasers from the guarantors." Other clauses of that agreement provided that the purchase money of any such sale or sales should be paid into an account in the name of the company with the bank, to be known as the debenture account, and that such moneys should be used for the payment off of the overdraft by the company, and that until the guarantors were called upon to pay the overdraft to the bank the interest payable under the debenture should be paid into the same account to be used for paying the interest payable to the bank on the overdraft.

" Pursuant to such collateral agreement a transfer of £250, portion of the joint debenture, was executed in favour of the defendant Herbert Robert Holt on or before 16th February 1932, although it does not appear whether the relative debenture was issued by the company, and on 13th May 1932 a further subdivided debenture for £150 was issued by the company to John Brady, who on 24th June 1932, purporting to exercise the powers thereby conferred upon him, appointed the defendant Herbert Price and Frederick

William Dorhauer as joint receivers of the whole of the company's property, who on the same date entered into possession of the same as such receivers.

"Art. 119 provides that unless otherwise determined by a general meeting two shall form a quorum at meetings of the board of directors; it is not suggested that the number was altered by any determination of a general meeting of the company.

"It is admitted that directors stand in a fiduciary relation towards the company, and that a director cannot, unless the articles otherwise provide, contract with the company. The rule is based upon the principle that a person who occupies a fiduciary position is not allowed to enter into engagements which conflict, or which may possibly conflict, with the interests of those whom he is bound to protect; and it is well settled that the fact that the contract is with another company in which the director in question is merely interested as a shareholder is sufficient to bring the case within the rule. The rule, however, may be relaxed by the articles, and art. 112 of the company is as follows: 'No director will be disqualified by his office from contracting with the company either as vendor purchaser or otherwise nor shall any such contract or arrangement or any contract or arrangement entered into by or on behalf of the company with any company or partnership of or in which any director shall be a member or otherwise interested be avoided nor shall any director so contracting or being such member or so interested be liable to account to the company for any profits realized by any such contract or arrangement by reason only of such director holding that office or of the fiduciary relation thereby established but no such director shall vote in respect of any such contract or arrangement and the fact of his possessing an interest (whether as director or member as the case may be) where it does not appear on the face of the contract must be disclosed by him at the meeting of directors after the acquisition of his interest.'

"This article still leaves untouched the incompetence of any interested director to vote as such in respect of any contract or arrangement in regard to which he had an interest which was in conflict with that of the company. In the present case, of the six members of the board as constituted in November 1931, three,

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

Herbert Price, Frederick William Dorhauer, and Herbert Robert Holt, were incompetent to vote in support of the relative resolution by reason of the fact that debentures were to be issued direct to them respectively. John Brady was also incompetent by reason of the fact that he was a shareholder in Richard Brady & Sons Ltd., another intended debenture holder. This left only two, W. S. Baker and F. R. Alldritt, who were competent to vote in regard to the matter in question.

"The minute book of the company records a board meeting held on Tuesday, 3rd November 1931, at 9.40 a.m., at which H. Price (chairman), F. W. Dorhauer, W. S. Baker, H. R. Holt and Joseph Brady (the last-mentioned as alternate director for John Brady) are recorded as being present, and the secretary, Albert George Fisher, as in attendance.

"The minutes of that meeting (to which further reference will be made subsequently) record that, after hearing an explanation by the chairman as to the reason for calling the meeting, and after discussion: 'Mr. Holt moved and Mr. Baker seconded that the company issue forthwith a series of debentures to secure repayment of moneys owing to each of Messrs. Price, Dorhauer, Holt and Richard Brady & Sons Ltd., and to Messrs. Price and Dorhauer, as guarantors for the overdraft at the Bank of New South Wales, Pitt St., Sydney, jointly, redeemable in twelve months from the date of issue subject to such conditions as the debenture-holders approve and in such denominations as may be expedient with interest at 7% per annum or as allowed by Government.—Carried unanimously.'

"The explanation made by Herbert Price, prior to this resolution being moved, referred to the fact that the burden of financing the company had fallen on 'Messrs. Price, Dorhauer, Holt and Richard Brady & Sons Ltd. who had through themselves or their nominees advanced £10,150 to the company.' It is not disputed that the reference to 'their nominees' was understood as referring to the defendants Rose Eaton Thwaites, Annie Adeline Price and Otto Christian Dorhauer, and that it was intended that the proposed series of debentures should include appropriate debentures to them respectively.

"The minutes further record a board meeting held on 17th November 1931, at which Messieurs H. Price (chairman), John Brady, F. R. Alldritt, W. S. Baker, F. W. Dorhauer and H. R. Holt are recorded as present, and the secretary as in attendance.

"The minutes of that meeting record (*inter alia*) as follows:— 'Issue of Debentures. Letter from the company's solicitor, dated 16th inst, re issue of debentures was read. Moved by Mr. Holt, seconded by Mr. Alldritt that the series of debentures totalling £10,150 prepared in pursuance of resolution of 3rd November '31 be sealed and issued to the respective persons named therein. Carried unanimously. Agreement re Joint Debenture. Moved by Mr. Alldritt seconded by Mr. Holt that the agreement between the company and Messrs. Price and Dorhauer as to the joint debenture for £5,000 be signed by the chairman of directors on behalf of the company. Carried unanimously."

"It is not suggested that the presence at these meetings of interested directors, and their participation in the discussions, would invalidate the proceedings, provided that the two disinterested directors, W. S. Baker and F. R. Alldritt, recorded as being present, voted in favour of the material resolution on 17th November 1931. It is not suggested that F. R. Alldritt was not present on that occasion, nor that, if Baker was present, either he or F. R. Alldritt did not vote in support of that resolution.

"The first question for determination is whether Baker was present on those occasions.

"He says he was not present at the meeting of 3rd November. The 3rd November 1931 was Melbourne Cup Day. Baker was by occupation a builder, temporarily thrown out of business by the prevailing depression, which considerably affected the building trade. He says that by reason of the day being Cup Day and of his being engaged in some occupation other than that of builder at that time, he is sure that he did not attend the board meeting on that day, which was held apparently at 9.40 a.m. He declined to state his then occupation, claiming privilege from answering questions in that connection on the ground that his evidence might incriminate himself; for that reason counsel for the defendants did not cross-examine him as to his whereabouts at the time in question, even in respect to details which would not involve self-incrimination.

H. C. OF A. 1937. RICHARD BRADY FRANKS LTD. v. PRICE.

"Even assuming that Baker was on that day pursuing the occupation of a starting-price bookmaker, I am not satisfied that the pursuit of that vocation was incompatible with his attendance at the board meeting held on that day at 9.40 a.m. ; but, even if he was present, that meeting would still lack the necessary quorum of disinterested directors competent to vote on the material resolution, and whether he was or was not present on that occasion is immaterial, except so far as the determination of that fact would bear upon the correctness of the minutes and the degree of credence to be attached to the evidence of Herbert Price and A. G. Fisher.

"As regards the board meeting of 17th November 1931, Baker does not profess to remember where he was on that date and at the material time, but says he was not present at any board meeting when either of the two resolutions already stated were moved and carried.

"In passing I may mention that at a board meeting held on 19th May 1931 he had himself moved, and F. R. Alldritt had seconded, a resolution " that in view of the financial assistance given to the company by Messrs. Price and Dorhauer, any steps considered necessary by them to protect their interests in the matter of preference or otherwise be undertaken forthwith '—which resolution was carried, from which I may infer that he would not have been opposed to the relevant resolutions and would have voted in favour of them if he was present at the board meetings of 3rd and 17th November in the same year.

"I read Baker's evidence as a statement that he was not present on 17th November. A. G. Fisher, the then secretary of the company, the defendant Herbert Price, and F. R. Alldritt say he was. Of the other persons who, according to the minutes, were present, F. W. Dorhauer is dead, and H. R. Holt and Joseph Brady, whose evidence might have been of value, were not called by either side.

"Mr. *Teece* contended that Baker was a liar who had committed perjury. I saw nothing in his demeanour to lead me to that view, and I am not disposed to think that, because he may have been carrying on business as a starting-price bookmaker, he is for that reason a person whose evidence is necessarily untrustworthy ; but even honest witnesses may be mistaken in their recollection.

"It appears that at board meetings rough minutes were taken by both the chairman, Price, and the secretary, Fisher, and that the actual minutes were compiled by Fisher from both sets of rough minutes, either alone or in collaboration with Price, which were at any rate either settled or approved by the latter before entry into the minute book. The minutes record Baker as present on both occasions. To hold that the minutes were incorrect on this point would involve a conclusion that Fisher and Price conspired to manufacture and record false evidence, and that they have supported such false evidence by perjury.

"Price is no doubt an interested party, and it is not beyond the bounds of possibility that such a conspiracy might have taken place, for although Fisher is not now in the employ of the company, he was in its employ at the material date, and at a time when other positions were difficult to obtain, and had he been a party to the falsification of the minutes, he would be interested to deny that fact and avoid the consequences which might otherwise ensue. On the other hand there was nothing in the demeanour of either Price or Fisher to lead me to believe that they were dishonest or attempting to mislead the court. Alldritt is a disinterested witness, and I see no reason to doubt that he honestly believes that Baker was present on 17th November ; it is, however, at least possible that his recollection may be at fault, particularly if it has been vitiated by being 'refreshed.'

"Baker himself, however, admitted that he believed that he was present at a board meeting when the question of the transfer of certain shares to one Clarke was the subject of discussion. This matter was, according to the minutes, under discussion at the two board meetings held on 3rd and 17th November. Baker says he was not present at either meeting ; the minutes record him as present at both ; if his recollection has failed him as to one, it may equally have failed him as to the other. Under these circumstances I think that the minutes of the meeting of 17th November, supported by the oral evidence of Fisher, Price and Alldritt, are of greater evidentiary value than the recollection of Baker, and I hold not only that the company has failed to discharge the onus which lies on it of

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

establishing the absence of a competent quorum, but go further and find that Baker was present at the meeting of 17th November 1931.

"I hold, therefore, that the attack on the validity of the debentures based on the absence of a quorum competent to vote on the resolution in question fails.

"I pass now to consider the second question of fact, which is whether the directors of the company in regard to the issue of the debentures acted solely in the interests of the proposed debenture holders and for the personal gain and advantage of the said persons and for the purpose of procuring a preference to the said persons and not in any way in the interests of the company or for the benefit or in any way for the purposes of the company.

"It is obvious that the company was at the material date in financial difficulties, after having enjoyed some years of real or fictitious prosperity. Incorporated on 23rd June 1926, it had for the year ended 30th June 1927 declared and paid a dividend at the rate of 10 per cent; for the year ended 30th June 1928, a like dividend of 10 per cent and a bonus of 2s. 6d. per share; and for the year ended 30th June 1929, on an assumed net profit of £3,081 3s. 5d., a further dividend at the rate of 12½ per cent.

"Unfortunately it appears that that profit for that year was not in fact earned. The directors' report for the next year, which ended 30th June 1930, reports that there was a loss for that year's trading operations of £8,735 6s. 6d. due to the then general depression in the building trade and other causes mentioned.

"The depression continued, and the directors' report for the year ended 30th June 1931 presented at the fifth annual general meeting on 24th November 1931, contained these statements:—'Your directors have to report that owing to the continual decline in business offering in the building trade, your works, as far as the manufacture of steel windows for which the company was primarily started, was for the greater part of the year practically at a standstill. . . . The total loss as disclosed in the balance sheet as submitted to you, carried to profit and loss account is £5,143 14s. 9d., and as the year started with a debit of £9,167 13s. 2d., the amount to the debit of P. and L. account to the 30th June 1931 is £14,311 7s. 11d. The loss on trading for the year was due solely to the

keen market and the small amount of sales, and your directors were seriously concerned as to the advisability of attempting to carry on. . . . Your directors have financed the company to enable it to carry on for the year, and now ask you to take your share in this regard for the future, recommending that you endeavour to carry on, notwithstanding the difficulties, in the hope of eventual success.'

"The position at the material date may, therefore, be summarized by stating that the depression affecting the building trade still continued; that of the original capital of the company, £25,000, no less than £14,311 7s. 11d. had been lost, leaving remaining approximately £10,688; and that the company had borrowed on short call £5,000 as follows: from the defendant Rose Eaton Thwaites, who had acted on the advice of the defendant Herbert Price, £1,000; from the defendant Annie Adeline Price £1,000; from Frederick William Dorhauer, on the joint account of himself and his brother the defendant Otto Christian Dorhauer, £2,500; from the defendant H. R. Holt £250; and from W. S. Baker £250.

"At a board meeting held on 30th September 1931, the chairman, H. Price, reported that the Bank of New South Wales had written under date 17th September asking that the bank account should be in good order at 30th instant, as that date was the end of the bank's half-year, and stated that finance for the next fortnight would be extremely hard, but that the position was expected to ease somewhat towards the end of October.

"At a previous board meeting held on 28th July 1931 the chairman, H. Price, had reported that the auditor, Mr. E. S. Wolfenden, had refrained from continuing his audit of the company's books until his account for services for the half-year ended 31st December 1930 was paid; that the account had now been paid, and that the audit was now in progress.

"On 30th September 1931 the account of the company with the bank was overdrawn £4,922; on 31st October 1931, £3,607 9s. 7d.; on 3rd November 1931, £4,053 4s. 4d. and on 17th November 1931, £4,378 5s. 9d.; the overdraft being secured by the guarantee of the defendant Herbert Price and F. W. Dorhauer.

"The loan of £250 from W. S. Baker had been made on 30th June 1931, at the suggestion or request of Herbert Price, who informed

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

him that the company was short of ready cash and would find it difficult to pay the next week's wages.

"On 24th October 1931 W. S. Baker requested repayment of his advance of £250; and the request not having been complied with, his solicitors, by letter dated 28th October 1931, demanded repayment not later than Monday, 2nd November, threatening immediate legal proceedings to recover same without further notice in the event of non-compliance with the demand. This demand brought matters to a crisis.

"On 30th October 1931 a board meeting was held, which was attended by Herbert Price, F. W. Dorhauer, H. R. Holt, Joseph Brady as alternate director for John Brady and, apparently by invitation, by James Brady, as representing Richard Brady & Sons Ltd.

"The record of the business transacted at this meeting, as appearing in the minute book, is as follows: 'Chairman explained that the meeting had been called in connection with a matter of urgent importance. A letter was read from Mr. Baker demanding the return of £250 loaned to the company. A letter was also read from Barnes, Hughesdon and Davis, Mr. Baker's solicitors, demanding on his behalf repayment of the aforesaid £250 by 2nd November '31. Chairman explained that Mr. Baker had loaned the company an amount of £250, Mr. Holt had also loaned a similar amount, and these, with the amounts previously loaned by Mr. Dorhauer and himself, made the total loan to the company £5,000. Mr. Baker had now asked for the return of his £250. The company was still having a difficult proposition in meeting the demands of its creditors, and in view of its financial position, the chairman declined to make any preferential payment. Mr. Dorhauer his co-director and himself are joint and several guarantors to the bank, and are the largest creditors of the company, and if Mr. Baker, a co-director, enforced his claim on the company, it would have no other option but to go into liquidation, as it had no means of meeting its overdraft at the bank or its other creditors. The position of the company now and for the past three months, owing to the volume of work in hand, was better than it had been for the past eighteen months, and it would be a pity to liquidate a company, which would

mean shareholders would not get one penny, if it could be avoided. After a general discussion in which Mr. Dorhauer supported the attitude of the chairman, Messrs. James and Joseph Brady agreed on behalf of Richard Brady & Sons Ltd. that if this company paid their account, they would at the same time return the amount, to be held as deposit at call on similar terms to the existing deposits. Moved by Mr. Dorhauer, seconded by Mr. Holt, that the action of Messrs. James and Joseph Brady on behalf of Richard Brady & Sons Ltd. in advancing the sum of £400 on deposit at call is appreciated, and that the thanks of the company be forwarded in writing to Richard Brady & Sons Ltd. Carried. . . . Moved by Mr. Dorhauer, seconded by Mr. Joseph Brady, that Mr. W. S. Baker's claim of £250 be paid on Monday next, together with interest to date. Carried. Moved by Mr. Holt, seconded by Mr. Joseph Brady, that the chairman's actions be endorsed. Carried.'

" Consequent upon that meeting W. S. Baker's loan was repaid by the company's cheque on 2nd November ; the board meeting was held on 3rd November to which reference has already been made ; on 9th November the company paid the trade debt of Richard Brady & Sons Ltd. of £395 8s. 6d. ; on 17th November Richard Brady & Sons Ltd. advanced to the company £400 at call ; and on the same 17th November the board meeting was held at which the issue of the debentures was resolved, and the same were issued on the same day.

" On 24th November 1931, the fifth annual general meeting of the company was held, at which no mention was made of the issue of the debentures in question.

" On 13th May 1932, the company issued to John Brady a subdivided debenture for £150, which represented portion of the original joint debenture for £5,000 ; the £150 provided by John Brady being paid into the company's No. 2 bank account in reduction of its overdraft with the Bank of New South Wales. On 24th June 1932, John Brady, in purported exercise of the powers contained in such subdivided debenture, appointed Herbert Price and F. W. Dorhauer as joint receivers of the whole of the company's property with the approbation and concurrence of all the other debenture holders, and on the same day Herbert Price and F. W. Dorhauer, as such

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

receivers, entered into possession of the company's undertaking and assets.

"It was contended by counsel for the plaintiff that the evidence establishes that at the material date liquidation was inevitable; that the issue of the debentures was solely due to the desire of the directors to do a kindly action, or the fair thing, in regard to protecting the proposed debenture holders who had assisted the company; that the key to the whole transaction was afforded by the resolution of the board of 19th May 1931 'that, in view of the financial assistance given to the company by Messrs. Price and Dorhauer, any steps considered necessary by them to protect their interests in the matter of preference or otherwise be undertaken forthwith'; and that it was the intention of the directors to carry on the company only for the six months necessary to protect the debentures from being set aside as either a fraudulent or at least a *de facto* preference.

"On the other hand the resolution of 19th May was not acted upon forthwith, and I see no reason to infer that the giving of the debentures was purposely postponed until the company was insolvent; and am inclined to think that, without any intention to obtain credit by the postponement of the issue of a debenture to secure the guarantors of the bank overdraft, the issue of such debenture would in all probability have been postponed indefinitely but for the crisis brought about by the insistence by W. S. Baker upon repayment of his short call loan of £250.

"Herbert Price stated that it was this demand which created the necessity for the issue of debentures. He says that it had throughout been understood that all short call creditors were to be regarded as on an equal footing, and that when one was paid all must be paid; that F. W. Dorhauer, who on behalf of himself and his brother had advanced £2,500 on short call, insisted that if Baker's loan was repaid his loan of £2,500 must also be repaid; that he himself, on behalf of his wife and Miss Thwaites, each of whom had advanced £1,000 on his advice and on the same footing, would also have insisted on those loans being repaid if Baker and Dorhauer were repaid, and that, as the company could not find cash to repay the £5,000 on short call, liquidation would be inevitable if this were insisted upon,

with the result that the shareholders would lose practically the balance of their capital. He says that the plan eventually adopted was a means of, first, satisfying Baker's demand by repayment of his loan of £250; secondly, placating the other short call creditors; and, thirdly, giving the company twelve months' breathing space in which it might win through to success; and that these results were achieved by the arrangement whereby Richard Brady & Sons Ltd. in effect agreed to take Baker's place by lending to the company £400, which was practically the amount of their trade debt; which placated the other short call creditors, who, in addition to receiving security in the shape of debentures, regarded Richard Brady & Sons Ltd. as taking the place of Baker and returning to the company rather more than the amount taken therefrom by Baker; while the acceptance by them of debentures redeemable at the expiration of twelve months relieved the company of the risk of being called upon before then to repay any short call creditors and gave it an opportunity of weathering the depression.

"If this view is accepted it would be impossible to find that the action of the directors was 'not in any way in the interests, or for the benefit, or in any way for the purposes of the company.'"

Long Innes C.J. in Eq. held that the debentures were valid and dismissed the suit but allowed one set of costs only between the two sets of defendants appearing and disputing: *Richard Brady Franks Ltd.* v. *Price* (1).

From that decision the plaintiff appealed to the High Court.

Spender K.C. and *Hutton*, for the appellant.

Spender K.C. The judge of first instance should have found that Baker was not present at the meeting of directors held on 17th November 1931. Upon such a finding it necessarily would have followed that the debentures were invalid. Even assuming the presence of Baker at that meeting, what took place on that occasion was not a substantive resolution determining whether the debentures should be issued or not, but was merely a ministerial confirmation of the debentures themselves. In other words, it was not substantively decided at that meeting that the debentures should be issued.

(1) (1936) 37 S.R. (N.S.W.) 37; 53 W.N. (N.S.W.) 238.

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

In any event the facts disclose, and the true inference from the undisputed facts is, that the directors used the occasion to advance their own interests in preference to the interests of the shareholders. The evidence shows that Baker was not present at the meeting held on 3rd November 1931, nor at the meeting held on 17th November. The witnesses who gave evidence to the contrary were either interested or faulty in their recollection. The minutes of those meetings are inaccurate. Baker was regarded by the judge of first instance as an honest witness. This court is in as good a position as the trial judge to determine this aspect of the matter. There was no competent quorum at either of the meetings. In the circumstances, the resolution passed at the meeting held on 17th November was not by way of ratification and had no validity as supporting what was resolved upon at the prior meeting. The resolution was passed not for the purpose of ratifying an invalid act, but merely as machinery to carry out what was assumed to be valid in the previous resolution. That was not a deliberative resolution and had no effect (*Cox* v. *Dublin City Distillery* [*No.* 2] (1); *Colonial Bank of Australasia* v. *Loch Fyne Gold Mining Co.* (2)).

[RICH J. referred to *A. M. Spicer & Son Pty. Ltd.* v. *Spicer* (3).]

Hutton. The relevant article of association in this case, namely art. 138, differs from the article of association considered in that case. The resolution of 17th November cannot stand by itself. It must be considered in conjunction with the prior resolution, having regard to its validity in the absence of a competent quorum, the instructions from the solicitor, and the fact that effect was given to those instructions without any consideration by the directors as to the advisability of issuing the debentures. The resolution was regarded as a mere formality, and was dealt with in a perfunctory manner. Thus the invalidity of the prior resolution, upon which, in the circumstances, the issue of the debentures depended, was not cured (*Colonial Bank of Australasia* v. *Loch Fyne Gold Mining Co.* (4)). The directors at each of the two meetings were, by reason of art. 112, incompetent

(1) (1915) 1 I.R. 345, at pp. 364, 366, 370, 376.
(2) (1866) 3 W.W. & a'B. (L.) 168.
(3) (1931) 47 C.L.R. 151.
(4) (1866) 3 W.W. & a'B. (L.), at p. 173.

to deal with the matter of the issue of the debentures. The debentures were not issued bona fide and are therefore void. They were not issued for the purpose of protecting the interests of the shareholders at large, but were issued solely for the protection of the interests of the directors and their friends.

[LATHAM C.J. referred to *Palmer's Company Precedents*, 12th ed. (1922), vol. 1, p. 722.]

Teece K.C. (with him *Seaton*) for the respondents Herbert Price, Rose Eaton Thwaites and Annie Adeline Price. The judge of first instance correctly found that Baker was present at the meeting held on 17th November 1931. [He was stopped on this point.] The distinction between an act which is *ultra vires* and a breach of trust is shown in *Attorney-General for Canada* v. *Standard Trust Co. of New York* (1). The evidence establishes that in issuing the debentures the directors were not actuated by improper motives, but, on the contrary, did so in the best interests of the company as a whole. At most the debentures created a preference in favour of some creditors over other creditors; this preference did not result in any prejudice to shareholders. Directors are not trustees for creditors, but only for shareholders; therefore directors who prefer one creditor to another do not thereby commit a breach of trust against the shareholders (*In re Wincham Shipbuilding, Boiler and Salt Co.*; *Poole, Jackson and Whyte's Case* (2); *Re A. M. Wood's Ships' Woodite Protection Co. Ltd.* (3)).

[DIXON J. referred to *In re Washington Diamond Mining Co.* (4).]

Directors are entitled equally with other persons, to prefer one creditor to another creditor unless such preference would constitute an infringement of the bankruptcy law (*Glegg* v. *Bromley* (5)). The evidence does not disclose that subsequent to the issue of the debentures there was any change of policy on the part of the directors. The court will not reverse a finding of fact unless it be proved that that finding is erroneous (*Dearman* v. *Dearman* (6)). Here the evidence abundantly justifies the finding of fact made by

(1) (1911) A.C. 498.
(2) (1878) 9 Ch. D. 322, at pp. 328, 329.
(3) (1890) 62 L.T. 760, at p. 762.
(4) (1893) 3 Ch. 95.
(5) (1912) 3 K.B. 474.
(6) (1908) 7 C.L.R. 549.

H. C. OF A. 1937. RICHARD BRADY FRANKS LTD. v. PRICE.

the judge of first instance. The appellant has not discharged the onus on it of showing that the members of the competent board of directors acted in breach of their duty to the company. Even if the debentures were invalidly issued to Brady the remainder of the transaction would not be affected thereby and would remain valid. The issue of the debenture in favour of Price and Dorhauer, they being guarantors, is, in the circumstances, authorized by the articles of association. There is no evidence whatever on which the court could find that the directors in authorizing the issue of the debentures were not acting bona fide in the interests of the company. The passing of the resolution of 17th November was a deliberative act and not merely a ministerial act on the part of the directors. There is a very great difference between the material facts in *Cox* v. *Dublin City Distillery* [*No.* 2] (1) and the facts in this case. The law does not recognize a contract to enter into a contract, as here. If parties enter into an alleged contract in law, all the terms and conditions of which have not been settled, there is no contract in law, it is still only a negotiation, and there can be no specific performance of it and no damage (*Coope* v. *Ridout* (2); *Von Hatzfeldt-Wildenburg* v. *Alexander* (3)).

[DIXON J. referred to *Sinclair, Scott & Co. Ltd.* v. *Naughton* (4).]

The evidence shows that at the meeting of 17th November the directors applied their minds to the resolution. Even if that resolution only purported to carry out a contract previously made it amounted to a ratification (*In re Portuguese Consolidated Copper Mines Ltd.*; *Ex parte Badman*; *Ex parte Bosanquet* (5), which was not brought under the notice of the court in *Cox's Case* (1)). If an unauthorized act is acted upon by a principal or his authorized agent it is thereby ratified. Assuming, therefore, that the resolution of 3rd November was unauthorized, it was ratified by the resolution of 17th November. The law as to ratification is stated in *Halsbury's Laws of England*, 2nd ed., vol. 1, p. 235.

[DIXON J. referred to *Davison* v. *Vickery's Motors Ltd.* (6).]

By appearing on the occasion of the settlement of the petition to wind up the company the appellant impliedly adopted the terms

(1) (1915) 1 I.R. 345.
(2) (1921) 1 Ch. 291.
(3) (1912) 1 Ch. 284.
(4) (1929) 43 C.L.R. 310.
(5) (1890) 45 Ch. D. 16.
(6) (1925) 37 C.L.R. 1, at pp. 15, 22, 24, 25.

of settlement and thereby recognized the existence of the debentures as good and valid debentures. The invalidity of a debenture operates only from the time when it is set aside.

In this suit the appellant, after claiming invalidity of the debentures, could have asked for an account against the receivers or an action for damages. It could have obtained all the results obtainable at common law.

[DIXON J. referred to *David Jones Ltd.* v. *Leventhal* (1).]

The giving by ostensible agents of security for past debts was the subject of a decision in *In re Fireproof Doors Ltd.*; *Umney* v. *The Company* (2). Costs should be allowed to each set of respondents represented before the court, or, in the alternative, if one set of costs only is allowed, those costs should be awarded to the respondents for whom we appear.

Shortland, for the respondents Otto Christian Dorhauer, and Alfred Joseph Morgan and Otto Christian Dorhauer (as executors of the will of Frederick William Dorhauer, deceased). These respondents have a greater financial interest involved than have the respondents on whose behalf the court has just been addressed; therefore they are entitled to costs. The respondent Otto Christian Dorhauer, who, although present at some meetings, was never a director, had no notice of any irregularity in the issue of the debentures; so far as he is concerned it is merely a case in which it was *ultra vires* of all the directors and not merely *ultra vires* of the company. There does not appear to be any decision of the court where the issue of debentures for antecedent loans has been set aside on the ground that the directors were not acting solely in the interests of the company. It is for the company to decide what is in its own best interests (*Shuttleworth* v. *Cox Brothers & Co. (Maidenhead)* (3)), and the evidence establishes that the issue of the debentures was for the company's benefit. Directors are entitled to prefer one creditor to another and even to prefer themselves (*In re Lloyd's Furniture Palace Ltd.*; *Evans* v. *The Company* (4)). The resolution of 17th November is quite sufficient to justify the issue of the debentures.

There was not any appearance for the other respondents.

(1) (1927) 40 C.L.R. 357.
(2) (1916) 114 L.T. 994; (1916) 2 Ch. 142.
(3) (1927) 2 K.B. 9, at p. 19.
(4) (1925) Ch. 853.

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

Hutton, in reply. The interests of the various respondents are not in conflict, therefore, in the event of the appellant not succeeding, there should be only one set of costs awarded to the respondents. The two resolutions are part of one transaction and should be read together.

Cur. adv. vult.

Aug. 17.

The following written judgments were delivered :—

LATHAM C.J. This is an appeal from a judgment of *Long Innes* C.J. in Eq, dismissing a suit to set aside certain debentures issued by the plaintiff company in favour of a number of directors and other persons who were relatives or friends of such directors. The company, which was incorporated in 1926, carried on the business of manufacturing and selling steel and metal doors and sashes. From 1929 the company was in difficulties and discussions took place from time to time among the directors as to providing the necessary finance to enable the company to carry on. Two of the directors, Herbert Price and F. W. Dorhauer, guaranteed the liability of the company on its bank overdraft up to £5,000. Other directors or their friends made advances to the company and W. S. Baker, who was also a director, lent the company £250 for a temporary purpose. In October 1931 the position was that directors and other persons had advanced about £5,000 to the company, that Price and Dorhauer were liable under their guarantee up to an amount of £5,000 for the bank overdraft, the overdraft at that time standing at about £4,000. The company also owed trade debts of about £5,000, but it had moneys owing to it which enabled it to meet its trade debts as required from time to time.

In October, however, Baker required payment of his money. The other directors who had made advances took the view that if Baker was paid they and their friends ought also to be paid. It would not have been possible to pay them without running a real risk of putting the company into liquidation, and the evidence of the directors was that they desired to avoid this being done. Richard Brady & Sons Ltd. was a trade creditor of the company for about £395. John Brady was a director of that company and also of the

plaintiff company. An arrangement was made at a meeting on 30th October 1931 that the debt of Richard Brady & Sons Ltd. should be paid and that Richard Brady & Sons Ltd. should then pay £400 to the company to be regarded as a loan " on short call," that is, on the same terms as advances made by other directors. On 3rd November another meeting of the board was held, and it was decided that the company should issue forthwith a series of debentures in order to give security for moneys owing to three of the directors, H. Price, F. W. Dorhauer and H. R. Holt, and to Richard Brady & Sons Ltd., and also to give security to Messrs. Price and F. W. Dorhauer as guarantors to the bank. The directors who were recorded as being present on that occasion were Messrs. Price, F. W. Dorhauer, Baker, Holt and Joseph Brady representing John Brady. Messrs. Price, Dorhauer, Holt and Brady were all interested in the issue of the debentures. Baker was the only person recorded as present who was not so interested. The articles of association provided that two directors should form a quorum and also provided that no director should be disqualified by his office from contracting with the company but that no director who was interested in any contract or arrangement with the company " shall vote in respect of any such contract or arrangement."

It is settled that, under such articles, in order to entitle a board of directors to act on behalf of a company, there must be present a quorum of directors who are competent to vote in relation to the business which they purport to transact (*In re Greymouth Point Elizabeth Railway and Coal Co. Ltd.*; *Yuill* v. *Greymouth Point Elizabeth Railway and Coal Co. Ltd.* (1); *A. M. Spicer & Son Pty. Ltd.* v. *Spicer* (2)). There were not two persons present at the meeting on 3rd November who were not interested in the issue of the debentures and therefore the resolution passed cannot be relied upon for the purpose of establishing the validity of the debentures.

On 17th November a further meeting of the board of directors was held and the minutes contained the following record of business done: " Letter from the company's solicitor dated 16th inst. re issue of debentures was read. Moved by Mr. Holt seconded by Mr. Alldritt that the series of debentures totalling £10,151 prepared

(1) (1904) 1 Ch. 32.

(2) (1931) 47 C.L.R. 151.

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

Latham C.J.

in pursuance of resolution of 3rd November 1931 be sealed and issued to the respective persons named therein. Carried unanimously." The letter from the company's solicitor set out the full names of the proposed debenture holders and the amounts to be allotted to each of them, and advised the directors as to the precise form of the resolution to be adopted.

On this occasion the directors recorded as being present included Baker and one Alldritt. Neither of these directors was interested in the issue of the debentures, and accordingly, if they were both present, there was a competent quorum. Admittedly Alldritt was present, but it was contended for the plaintiff that Baker was not present at either meeting (3rd or 17th November) though he was recorded in the minutes as being present and taking an active part. The learned trial judge heard a great deal of evidence upon this question and he came to the conclusion that Baker (despite his denial on oath) was present on both occasions.

In my opinion this court should not upset this finding of the learned judge who saw and heard the witnesses. If Baker were not present at the meetings, then certainly the chairman of the directors and the secretary, and probably other directors, must have been engaged in a conspiracy to concoct minutes with the object of showing with verisimilitude that he was present, and this must have been done for the purpose of supporting the validity of the debentures. Whether such a conspiracy was likely was essentially a matter for the learned judge to determine. A conclusion upon such a matter would be influenced very largely by the opinion formed of both the character and the capacity of the persons concerned. In my opinion, the finding that Baker was present on 17th November, which is the crucial matter, should not be disturbed.

The next question which arises is whether the resolution of 17th November was effective for the purpose of authorizing the issue of the debentures. The point which is taken is that the resolution in terms refers to a " series of debentures totalling £10,150 prepared in pursuance of resolution of 3rd November 1931." The resolution of 3rd November 1931 was passed at a meeting at which a competent quorum was not present and was therefore in itself ineffective to

authorize the issue of debentures on behalf of the company. It is urged that the terms of the resolution of 17th November show that the directors present were merely purporting to act in pursuance of the earlier resolution and that they did not deliberately and independently determine on that day that the debentures should be issued. Reference is made to *Cox* v. *Dublin City Distillery* [*No.* 2] (1). In that case the resolution which authorized the making of the contracts contained in a series of debentures was passed at a meeting at which a competent quorum was not present. The facts are different in the present case.

In my opinion the resolution of 17th November does not in any way depend upon the resolution of 3rd November. The earlier resolution was not effective to authorize the issue of any debentures because the conditions of the debentures had not then been determined. The later resolution refers to the earlier resolution only for the purpose of describing the debentures as being " debentures prepared in pursuance " of the earlier resolution. The later resolution, which was passed by a competent meeting, contains clear authority for the issue of each of the debentures which were in fact issued. In my opinion, therefore, this objection fails.

The next objection to the judgment under appeal is that the learned judge ought to have found that the directors did not act bona fide for the benefit of the company when they decided to issue the debentures and that the debentures are accordingly invalid, at least in the case of debentures issued to directors who were fully acquainted with all the facts, whatever may be the position with respect to some debenture holders who were not themselves directors. The powers of directors must be exercised not only in the manner required by law but also bona fide for the benefit of the company as a whole (*Allen* v. *Gold Reefs of West Africa Ltd.* (2)). A court, however, does not presume impropriety. In this case there is no doubt that the issue of the debentures was within the powers of the directors. The onus is on the plaintiff who challenges the action of the directors to establish that they did not act bona fide for the benefit of the company. In a case where this question arose

(1) (1915) 1 I.R. 345.

(2) (1900) 1 Ch. 656, at p. 671.

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

Latham C.J.

(*Shuttleworth* v. *Cox Brothers & Co. (Maidenhead) Ltd.* (1) *Bankes* L.J., after referring to *Allen* v. *Gold Reefs of West Africa Ltd.* (2), said: "In the present case it seems to me impossible to say that the action of these defendants was either incapable of being for the benefit of the company or such that no reasonable men could consider it for the benefit of the company" (3). The learned judge in the case under appeal has found that it is affirmatively proved that the directors intended to exercise their powers for the benefit of the company. There was clearly evidence which, if believed, justified this finding. The company was in a difficult position. It was necessary to take some action to prevent creditors descending upon it with the not improbable result that the company would have been forced into liquidation. It is not for a court to determine whether or not the action of the directors was wise. The question is whether it is shown that they did not honestly act for what they regarded as the benefit of the company. In my opinion the finding of the learned judge upon this question is supported by evidence and should be upheld. Thus I am of opinion that the appeal should be dismissed.

In the proceedings before *Long Innes* C.J. in Eq., the defendants were not all represented by the same solicitors and counsel and only one set of costs was allowed between them. It is contended by the appellant that in this court only one set of costs should be allowed as between the respondents, although two of the respondents were represented separately from such other respondents as have appeared and taken part in the proceedings. I am of opinion that there was no need for separate representation of any of the respondents. The fact that one of the respondents who is separately represented was not a director does not distinguish his case from that of the other debenture holders. The company had enough assets to pay all its creditors, including the debenture holders. I am unable to see that there was any actual or possible conflict of interest between the respondents, and I am therefore of opinion that the appeal should be dismissed with costs, but that only one set of costs should be allowed to the respondents. In my opinion, to avoid difficulties in taxation, two-thirds of such costs should be paid to the solicitors

(1) (1927) 2 K.B. 9. (2) (1900) 1 Ch., at p. 671.
(3) (1927) 2 K.B., at p. 19.

for Herbert Price, Rose Eaton Thwaites and Annie Adeline Price, and one-third of such costs should be paid to the solicitors for Otto Christian Dorhauer, and Alfred Joseph Morgan and Otto Christian Dorhauer (as executors of the will of Frederick William Dorhauer, deceased).

RICH J. In this appeal three questions were argued with regard to the issue of the debentures the subject of this suit. The first question was whether there was a disinterested quorum of directors at either of the meetings of 3rd and 17th November. Art. 119 provides that two shall form a quorum at meetings of the board of directors and art. 112 in effect says that no director shall vote upon any matter in which he shall be interested. Its object was to ensure to the company that its directors should not be placed in a position in which their personal interests might be in conflict with the duty they owed to the company, and that in all transactions entered into by them on behalf of the company, the company should be able to rely upon their unbiassed and independent judgment (*Victors Ltd.* v. *Lingard* (1)). A disinterested quorum was not present at the meeting of 3rd November. But at the meeting of 17th November the minutes recorded that the quorum included Baker and Alldritt, both of whom had no personal interest in the issue of the debentures. Baker denied that he had been present but a mass of evidence was presented to the learned judge who found on this issue that Baker was present. " Upon questions of fact an appeal court will not interfere with the decision of the judge who has seen the witnesses and has been able, with the impression thus formed fresh in his mind, to decide between their contending evidence, unless there is some good and special reason to throw doubt upon the soundness of his conclusions " (*Ruddy* v. *Toronto Eastern Railway Co.* (2), and other cases cited in *Federal Commissioner of Taxation* v. *Clarke* (3)). After a careful consideration of the relevant evidence I have not found reasons adverse to the conclusion come to by the learned judge who has seen and heard the witnesses and determined the case upon comparison of their evidence. It was next contended

(1) (1927) 1 Ch. 323, at pp. 329, 330.
(2) (1917) 33 D.L.R. 193.
(3) (1927) 40 C.L.R. 246, at pp. 263-266, 292, 293.

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

Rich J.

on behalf of the appellant that no effective resolution had been passed to authorize the issue of the debentures, firstly, because no competent quorum was present at the meeting of 3rd November, and secondly, because the resolution passed at the meeting of 17th November was merely ancillary and incidental to that of the previous meeting. The first resolution can only be considered for the purpose of interpreting the second resolution. The second resolution so construed represents that the series of debentures has been prepared and is in order awaiting authority to issue the series and then proceeds to determine upon and authorize its issue. The last objection to the judgment under appeal was that the power had not been exercised by the directors " bona fide for the benefit of the company as a whole." At the hearing before the learned judge the plaintiff accepted the onus of proving this proposition. The phrase " bona fide for the benefit of the company as a whole " no doubt tends to become a cant expression in these matters but is not yet a shibboleth. Many of the cases which illustrate this " phrase " relate to the alteration of articles of association by shareholders in general meeting. No court " should consider itself fettered by the form of words, as if it were a phrase in an Act of Parliament which must be accepted and construed as it stands " (*Shuttleworth* v. *Cox Brothers & Co. (Maidenhead)* (1)). But the learned judge found that " the evidence as a whole preponderates in favour of the view that in regard to the issue of debentures the directors acted in the interests of the company and of the general body of shareholders and not in the interests of the proposed debenture holders " and found this issue of fact against the plaintiff. In order to succeed in a case like the present the plaintiff must prove the equivalent of fraud or bad faith. In *Hirsche* v. *Sims* (2) the Earl of *Selborne* formulated a test which seems applicable to the present case as follows : " If the true effect of the whole evidence is, that the defendants truly and reasonably believed at the time that what they did was for the interest of the company, they are not chargeable with *dolus malus* or breach of trust merely because in promoting the interest of the company they were also promoting their own." Upon such a question an opportunity of seeing the parties concerned is a matter

(1) (1927) 2 K.B., at p. 26.

(2) (1894) A.C. 654, at pp. 660, 661.

of special importance in arriving at a conclusion. In the present case it is enough to say that the evidence does not establish any reason for disturbing the finding of the learned judge to which I have referred.

The appeal should be dismissed.

DIXON J. On 17th November 1931 instruments were executed on behalf of the plaintiff company purporting to secure by way of floating charge sums amounting to £10,150. Of these sums, £5,150 consisted of money deposited with the company at call and £5,000 formed a contingent liability of the company, a liability to the guarantors of its overdraft. The security or debenture thus covering the guarantors was issued upon terms which empowered them to subdivide the amount and sell parts of the security as separate debentures, subject, however, to the condition that the proceeds should be paid into the bank in reduction of the overdraft. The power was exercised and, on 13th May 1932, a debenture of £150, parcel of the amount of £5,000 specified in the guarantors' debenture, was issued to a transferee from the guarantors.

On 24th June 1932, the holder of the new debenture appointed receivers and managers who took possession of the company's undertaking and carried it on under the provisions of the debentures.

On 21st November 1933, the shareholders resolved that the company should be voluntarily wound up.

On 1st September 1935, the liquidator, in the name of the company, filed a statement of claim instituting the suit out of which this appeal arises. The prayer sought a declaration that the debentures were inoperative and void, and an inquiry as to the dealings with the debentures and an account of all moneys in connection therewith.

Long Innes, C.J. in Eq., decided that the debentures were valid and dismissed the suit.

Under the company's articles of association, at meetings of the board of directors two formed a quorum and the powers of the directors remained exercisable so long as a sufficient number to form a quorum was present. The usual provision was made that no director should be disqualified by his office from contracting with the company and no contract should be avoided by reason of

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

Dixon J.

a director's interest therein. But a proviso forbade every director to vote upon any matter in which he had an interest. Articles of such a kind are interpreted to mean that there must be present at the meeting a quorum consisting of directors none of whom is disqualified from voting upon the business transacted (See *A. M. Spicer & Son Pty. Ltd.* v. *Spicer* (1), where the authorities are cited).

The first ground on which the validity of the debentures is impeached is that no competent quorum existed at the meeting of 17th November 1931 when the resolution was passed authorizing the issue of the debentures. The minutes of the meeting in question show that two directors were present who admittedly had no interest in the issue of the debentures. The accuracy of the minute as to the presence of one of them is attacked, but the weight of evidence supports its correctness and *Long Innes* C.J. in Eq. found that the director in question was in fact present. In my opinion the attack on that finding is hopeless.

The second ground of attack is that in assenting to the resolution upon which reliance is placed the two directors forming the competent quorum did not give or purport to give their approval to the transaction or to authorize it. In terms the resolution adopted at the meeting of directors held on 17th November 1931 did authorize the actual issue of the debentures. But it had been preceded by two important meetings of the board. At the first of these, held on 30th October 1931, the directors considered a demand made on behalf of a member of the board for repayment to him of a sum of £250 which he had lent to the company. This formed part of the money deposited at call which was owing to members of the board or their relatives. As the company was in financial difficulties, the other directors not unnaturally were unwilling to make an immediate payment in cash to one such creditor and not to others. But it happened that a member of the board was in a position to convert a trade debt for £400 owing by the company into a deposit like that called up, and this he agreed to do. In adopting that course he was regarded by his fellow directors as affording a means of allowing the payment of the £250 demanded. It is not altogether easy to see the reason of this, but apparently a deposit at call was treated

(1) (1931) 47 C.L.R., at p. 187.

as in effect a fixed deposit, because it was understood that the course taken by the director seeking immediate payment of his £250 would not be imitated. Thus the director who converted the trade debt into a deposit, in effect, recouped the fund depleted by the withdrawal of the £250. Acting upon the same view, the board at the next meeting, which was held on 3rd November 1931, considered the question of issuing in respect of the deposits debentures with a currency of twelve months certain. Two of the directors had guaranteed the company's overdraft up to £5,000, and the board dealt also with securing the company's contingent liability to them by means of a debenture or debentures. At this meeting there was only one director present who had no interest in the transactions. There was, therefore, no competent quorum. But, nevertheless, a resolution was in fact passed that the company should issue forthwith a series of debentures to secure repayment of moneys owing to depositors and to secure the guarantors of the overdraft. The resolution provided that the debentures should be redeemable in twelve months from the date of issue, subject to such conditions as the debenture holders might approve.

On these facts it is said that there was no independent decision of the two directors forming the competent quorum present at the subsequent meeting of 17th November 1931, but only a resolution approving of the means adopted for carrying out a determination already arrived at, by which they conceived the matter to be settled. Reliance was placed on the decision of the Irish Court of Appeal in *Cox* v. *Dublin City Distillery* [*No.* 2] (1). The contention is answered by the terms of the resolution of 17th November and the inchoate nature of the resolution of 3rd November 1931. In *Cox* v. *Dublin City Distillery* [*No.* 2] (1), at the earlier of the two meetings, that at which there was no competent quorum, the directors made a contract which, it was held, apart from the defect would have bound the company. At the second of the meetings, that at which there was a competent quorum, no more was done than to record the fact of the sealing and issuing of the instruments fulfilling the supposed contract. This was an insufficient exercise of the authority confided to a competent quorum to contract on the company's behalf with

(1) (1915) 1 I.R. 345.

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

Dixon J.

their co-directors or make a contract in which some of the latter were interested.

In the present case the earlier meeting resolved on nothing which would amount to a contract. In the interval the terms of the debentures were arranged, the persons to whom they were to be issued were nominated and the instruments were drawn up by the company's solicitors. By the resolution at the later meeting an express authorization was given to seal and issue the debentures in pursuance of the previous resolution. This was the contractual act and to it the two competent directors gave their assent by voting for the resolution. No contention has been advanced that the presence of the other directors at the meeting and their voting for the resolution, notwithstanding their incompetence to do so, vitiated the resolution. In my opinion the objection fails that the requirements of the articles of association were not observed.

Of the grounds upon which the validity of the debenture was impugned before *Long Innes* C.J. in Eq., there remains only one more upon which reliance was placed in support of the appeal. That ground is that in issuing the debentures to secure the money deposited at call and the contingent liability of the guarantors to the bank, the directors acted entirely in the interests of the depositors or lenders and of the guarantors and not at all in the interests of the company. Directors are fiduciary agents and their powers must be exercised honestly in furtherance of the purposes for which they are given. Under the general law of agency it is a breach of duty for an agent to exercise his authority for the purpose of conferring a benefit on himself or upon some other person to the detriment of his principal. But, at the same time, if his act is otherwise within the scope of his authority it binds the principal in favour of third parties who deal with him bona fide and without notice of his fraud (*Hambro* v. *Burnand* (1); *Lloyds Bank* v. *Chartered Bank of India, Australia and China* (2), per *Scrutton* L.J.). The rule, no doubt, is the same with respect to the acts of directors. It follows that a transaction carried out by directors for their own or some other persons' benefit and not to further any purpose of the company is voidable but not void.

(1) (1904) 2 K.B. 10.

(2) (1929) 1 K.B., at p. 56.

The object of this proceeding is said to be to obtain a declaration that the debentures under which the receivers took possession of the company's undertaking on 24th June 1933 were invalid and void, so that an action at law may be brought against them for trespass and conversion. It may, therefore, be important to distinguish between invalidity or voidness and voidability. It might not be enough for the plaintiff's purpose to show that the debentures were issued in such circumstances that in equity they would be set aside. It appears that the ordinary creditors and secured creditors will alike be paid in full and, apart from the question whether, under the debentures, a justification exists for the acts of the receivers in assuming control of the undertaking, it is difficult to see that anything now turns upon the validity of the securities. But no doubt if it were established that the debentures were issued in fraud of the company, then, except where it appeared that the debenture holder took bona fide, the debenture would be set aside and accounts and appropriate inquiries would be decreed unless it was affirmatively shown that in the events that had happened no useful result could possibly ensue. Those impeaching the transaction must sustain the burden of proving that the directors acted in their own interests and were not in fact exercising their powers in supposed furtherance of any purpose or advantage of the company. In considering such a question, it is important to ascertain what are the purposes for which powers are given and to remember that the fiduciary duty of the directors is to the company and the shareholders. It is not enough that they preferred their own interests or those of some other persons to the interests of strangers to the company, as, for instance, to those of the creditors of the company.

In the present case one of the powers expressly conferred by the articles upon the directors is as follows : " To execute in the name and on behalf of the company in favour of any director or other person who may incur or be about to incur any personal liability whether as principal or surety for the benefit of the company such mortgages of the company's property (present and future) as they may think fit and any such mortgage may contain a power of sale and such other powers covenants and provisions as shall be agreed upon." This power extends to giving security to directors in

H. C. OF A. 1937.

RICHARD BRADY FRANKS LTD. v. PRICE.

Dixon J.

respect of liabilities already incurred for the benefit of the company and it is evident that the circumstance that such a director is thereby placed in a better position and given priority to other creditors is not in itself necessarily an objection to the exercise of the power. The allegation is that, when the debentures were issued in respect of the deposits at call amounting to £5,150 and the guaranty for £5,000, the purpose of the transaction was nothing but conferring upon lenders and guarantors who themselves were directors, or were represented by directors, all the advantages given by such a security. The company was in difficulties. A liquidation might be found unavoidable and, it is said, they simply wished to secure the debts in question. There are many circumstances supporting this view of the transaction. But, on the other side, there is a body of evidence explaining the issue of the debentures on the ground, stated briefly, that it was part of an arrangement by which none of the depositors or guarantors was to call in his debts or liability for twelve months, in order to give the company an opportunity of improving its position without any one of them following the example of the director who had called in his £250 and so, perhaps, precipitating a collapse. On the whole evidence, *Long Innes* C.J. in Eq. was not satisfied that the sole purpose of issuing the debentures was to benefit the depositors and guarantors. He said: "I have come to the conclusion that the plaintiff has failed to discharge the onus which rests upon it in regard to this issue of fact; and I think, on the contrary, that the evidence as a whole preponderates in favour of the view that in regard to the issue of debentures the directors acted in the interests of the company and of the general body of shareholders and not in the interests of the proposed debenture holders. I find this issue of fact against the plaintiff."

It is, in my opinion, impossible to reverse this finding. It is founded upon the learned judge's interpretation of oral evidence, much of which consisted of confused explanations, and upon his estimate of the characteristics and honesty of the witnesses who gave the evidence and attempted the explanations. Moreover the question is not whether the operation of the transaction was or might give a preference over ordinary creditors or benefit those receiving debentures at their expense, but whether the object was

wholly the advantage of the directors or their associates so that the interests of the company were sacrificed or disregarded. The burden of establishing bad faith in this sense has not been sustained.

In my opinion the appeal should be dismissed with costs.

Appeal dismissed with costs. One set of costs only to be allowed to respondents, two-thirds of such costs to be paid by the appellant to the solicitors for Herbert Price, Rose Eaton Thwaites and Annie Adeline Price, and one-third of such costs to be paid to the solicitors for Otto Christian Dorhauer, and Alfred Joseph Morgan and Otto Christian Dorhauer (executors of the will of Frederick William Dorhauer, deceased).

Solicitors for the appellant, *William Patterson & Co.*

Solicitors for the respondents Herbert Price, Rose Eaton Thwaites and Annie Adeline Price, *J. J. Jagelman & Son.*

Solicitors for the respondents Otto Christian Dorhauer, and Alfred Joseph Morgan, *A. J. Morgan & Co.*

J. B.