NSW YOUNG LAWYERS
A Fresh Perspective

8 April 2005

The Secretary
Parliamentary Joint Committee on Corporations and Financial Services
Department of the Senate
Parliament House
Canberra ACT 2600

Dear Sir/Madam,

Re: Exposure Draft Bill for Consultation - Corporations Amendment Bill (No. 2) 2005

The Business Law Committee of New South Wales Young Lawyers would like to thank the Parliamentary Joint Committee on Corporations and Financial Services ("the PJC") for the opportunity to make submissions in relation to the exposure draft of the Corporations Amendment Bill (No. 2) 2005 ("the Exposure Draft Bill").

By means of introductory comments, we support the intentions of the Exposure Draft Bill to facilitate increased shareholder participation in corporate governance, while reducing the associated costs of such participation. We acknowledge and support the importance of retaining effective mechanisms so that shareholders, particularly minority shareholders, are able to examine the affairs of the company and voice concerns to the company and its members.

Shareholder participation is vital in ensuring accountability of the company's board and management and it is important that the need to manage the associated costs to the company does not become the sole aim of this initiative. The driving focus must remain on producing legislative initiatives that encourage companies to better value increased shareholder participation, without watering down the rights of shareholders.

The Business Law Committee of NSW Young Lawyers thanks the PJC for considering this submission, which was compiled with the assistance of Committee members Duncan Brakell and Jeremy Green. Duncan, Jeremy or I would be very willing to discuss this submission should the PJC see fit.

Yours truly,

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The Business Law Committee of NSW Young Lawyers makes the following submission in relation to the Exposure Draft Bill:

1 Calling of a general meeting by directors when requested by members - section 249D.

Item 1: For the reasons expressed below, we do not support the proposed amendment to s 249D.

Before the Government repeals s 249D(1) of the *Corporations Act 2001* (Cth) ("the Act") and thereby abolishes the obligation on directors to call a general meeting upon the request of 100 members who are entitled to vote at the meeting ('the 100-member rule'), it must provide a reasonable and quantifiable justification for doing so.

The Explanatory Memorandum to the Exposure Draft Bill cites the following reasons for repealing the 100-member rule:

> 'increasing public concern about the impact of the [100-member] rule on the conduct of company business': [1.4]
>
> 'further examples of vexatious use of the 100 member rule': [1.7]
>
> 'the rule allows for special interest groups to threaten the imposition of large and unnecessary costs on companies, for publicity purposes or to influence negotiations with the company, to the detriment of the vast majority of members': [2.3]
>
> 'disproportionate influence to minority shareholders': [2.3]

Putting to one side the lack of evidence provided by the Government to support any of the above apparently anecdotal claims, of particular concern is the Government's willingness to *repeal* the 100-member rule, without first considering options for *reform*. It appears the Government, while correctly identifying weaknesses and potential for misuse of the 100-member rule, has not considered whether its legislative objectives could be achieved without the repeal of the 100-member rule. Further, it is submitted, by proposing to maintain in isolation the five per cent threshold currently found in s 249D(1)(a) of the Act, the Government's legislative objectives may not be achieved notwithstanding the abolition of the 100-member rule.

As outlined above, in repealing the 100-member rule, the Government claims to be addressing concerns about misuse of the provision by 'special interest groups' (whatever these may be), such as by threatening to requisition a general meeting 'for publicity purposes or to influence negotiations with the company'. The Government clearly shares the concerns of Rob Carter, Chief Executive Officer of NRMA, who made the following observations in a speech to the Australian Institute of Company Directors:

> What we are now seeing is a proliferation of broad community interest activities being canvassed at company meetings. Meetings that have often been called for the purpose of dealing with these matters alone or the addition of agenda items which the relevant shareholder/members know will have little chance of general support but which they require to be discussed.[1]

To the extent that the proposed amendments seek to eliminate or discourage misuse of the law, it has our unqualified support. However, the Act already provides a number of protections from misuse of company meetings. One of which is s 249N(1)(b); yet, incongruously, the Government seeks to water down this protection through amendments proposed in the Exposure Draft Bill.[2] We also remind the Government of s 249Q, which requires a meeting of a company's members to be held for a proper purpose and further submit that s 249Q provides the protection the Government is seeking to achieve by repealing the 100-member rule. If a special interest group comprising 100 members was to requisition a meeting purely for 'publicity purposes' (arguably, an improper purpose), by virtue of s 249Q, the directors can refuse to comply.[3]

We acknowledge the purposes for which a meeting of a company may be properly called are many. We also acknowledge the Courts' willingness to construe widely the phrase 'proper purpose'. Indeed, provided that the resolution sought to be passed is within the power of the members to consider and pass, and provided the meeting is called for that purpose and not for some extraneous purpose so as to constitute it an abuse, there is no restriction on the power to requisition.[4]

It would appear the mischief that the Government is seeking to address is where a relatively small number of members, presumably with knowledge of the breadth of the 'proper purpose rule', attempt to dress their wolfish purpose in a sheep's requisition to call a meeting of members. Although, given the Government does not seek to limit or enumerate the purposes for which members may request a meeting to be called, it must be that the Government is solely concerned with the number of members who may call the meeting, rather than the purpose for which the meeting is called. Indeed, were the Government truly concerned about meetings being used for improper purposes, it would not propose the amendments to s 249N that it has.[5]

If this is true, in simply abolishing the 100-member rule, the Government has used the most blunt instrument possible for dealing with a complex problem.

It cannot be denied, as noted by Windeyer J in *NRMA Ltd v Snodgrass*,[6] that it is 'extraordinary that in a company limited by guarantee with about 2 million

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[1] Rob Carter, 'Challenges in Corporate Governance: Loyalty to Whom?' (2002) in Simon Milne and Nicola Wakefield Evans, 'Shareholder Requisitions - the 5%/100 Member Provision' (2003) 31 *Australian Business Law Review* 285, 286.

[2] We make comment on the proposed amendment to s249N below and do not repeat those comments here.

[3] See, eg, *NRMA Ltd v Parker* (1986) 6 NSWLR 517, where the purpose of the meeting was to instruct the board of directors to conduct the election of directors in a particular way. However, where a meeting is requisitioned to consider some valid and some invalid resolutions, the meeting should be convened to consider the valid resolutions: *Totally and Permanently Incapacitated Veterans of NSW Limited v Gadd* (1998) 28 ACSR 549, 551

[4] *NRMA Ltd v Snodgrass* [2001] NSWSC 76, [10] (Windeyer J).

[5] We make comment on the proposed amendment to s249N below and do not repeat those comments here.

[6] [2002] NSWSC 590, [13].

members a general meeting can be summoned by requisition of 100 members, namely one in every 20,000 or 0.005 percent'. The Government must act, and the law must be changed, to ensure such a disproportionate balance of power ceases to exist. However, the Government must be concerned about any group of a company's members having a disproportionate level of influence, not only very small minorities.

Thus, rather than simply repeal a provision that has been a part of Australian corporate law since, at least, the Companies Acts of 1961, we urge the PJC to recommend the Government consider amendments and alternatives and give this complex problem the consideration and analysis it deserves. Undoubtedly, in many instances, particularly involving today's larger public companies, the 100-member rule is too low a bar. Conversely, for smaller public (and all proprietary) companies, the 100-member rule is too high a bar to reach.

We submit that a viable option for the Government is to develop a continuum, based, perhaps, on market capitalisation or numbers of members, which would provide the flexibility to balance the interests of the company and those of its members. The continuum would, essentially, provide for the right to requisition a meeting of members to be exercisable only by a greater number (or percentage) of members as the size of the entity or entity's membership increases. It is open to the Government to implement such an option by making regulations, rather than by amending the Act, by using its express regulation-making power under s 249D(1A).

Finally, it is submitted that some form of quantitative analysis is required in relation to the continuing relevance of the five per cent of votes threshold ("the five per cent threshold"). One can only assume there was considered to be, at the time of their introduction, a degree of parity between five per cent of votes and 100 members. If the Government considers one of these measures now to be inadequate, then, arguably, so must be the other. For example, it may be that a more adequate threshold should be one per cent of members or 10 per cent of all votes that may be cast at the meeting.

The perceived risk in our view is that, on the limited anecdotal evidence provided, the five per cent threshold may be misused by those members with a greater allocation of voting rights. We note that the Government originally rejected an earlier proposal to repeal the 100-member rule because the five per cent threshold in isolation set a threshold that was too high in a market containing a large proportion of retail investors.[7] Surprisingly, it appears the Government has now retreated from this stance, notwithstanding the increased and increasing level of retail participation in the market. Further, the gap between 100 members with minimal shareholdings and five per cent of the available votes is disproportionately high in the larger public companies, which means the proposed amendment potentially tips the balance in favour of

[7] 'Government Response to the Report of the Parliamentary Joint Standing Committee on Corporations and Securities: Matters Arising from the Company Law Review Act 1998' (Government Response), 16 in Milne and Wakefield Evans, above n 1, 288.

institutional investors.[8] In larger public companies, 10,000 individual members could combine their shareholdings and still not represent five per cent of the available votes. Yet, arguably, 10,000 members represent more than what the Government would call a 'special interest group'. An institutional investor, by comparison, would have little difficulty in reaching the five per cent threshold and has the added advantage of informal opportunities to raise issues with the company outside of general meetings. This kind of disproportionate influence must be equally as unpalatable as that currently wielded by small minorities of members of Australia's largest companies.

We therefore urge the PJC to recommend the Government consider alternatives to repealing the 100-member rule and take the time to engage in quantitative analysis in order to arrive at an appropriate threshold for the requisition of general meetings. Until these steps are taken, we cannot support the proposed amendment.

Item 2: Subject to our comments in relation to *Item 1*, above, and to the extent that these comments affect the operation of the amendments proposed in *Item 2*, we do not object to the proposed amendment.

2 Members resolutions for annual general meetings ("AGM") - section 249N.

Item 3: Subject to our comments in relation to *Item 1*, above, and to the extent that these comments affect the operation of the amendments proposed in *Item 3*, we support the proposed amendment, only to the extent that it seeks to improve shareholder participation in the greater interests of the company and members.

However, the proposed amendments to ss 249D and 249N appear to be inconsistent with one another from a policy perspective. The policy incongruence comes about on the one hand by the Government's proposal to abolish the 100-member rule in attempt to contain the influence of so-called special interest groups, yet on the other, the proposed amendment arguably provides an easier avenue for such groups to ensure that their resolutions are listed on the AGM agenda.

We agree with the underlying governance principles of the proposed amendment to enhance shareholders' ability to participate in AGMs, but simply permitting 20 members of a company to force the company (through resolution) to spend time at the general meeting discussing items that may have little or no relevance to the vast majority of the company's members is not, in our view, the retention of an effective mechanism for minority shareholders to examine the affairs of the company. Rather, the current requirement that an issue be of interest to at least 100 members of a company before it can be discussed at the company's general meeting provides a greater level of certainty of relevance of the issue and should be retained. That said, we do not discount the emerging importance of providing minority shareholders with a voice at general meetings and the right to be given a fair and reasonable opportunity to question the actions of their company.

[8] Editorial, 'Meeting the Need for EGMs', *The Australian Financial Review* (Sydney), 15 November 2000, 50 in Simon Milne and Nicola Wakefield Evans, above n 1, 288.

In support of our comments made under *Item* 1, we again submit that some form of quantitative analysis must be provided to justify the reduction of the minimum number of members that may give a company notice of a resolution from 100 to 20. Legislative amendments must be based on considered, reasonable and qualified policy.

3 Distribution of members' statements – section 249P.

Item 5: One of the many critical facets of corporate governance reform is the importance of increasing shareholder participation in general meetings, and, independent of our comments made in relation to *Item 1*, we agree that the proposed amendment is a valuable mechanism for bringing about greater member communication.

4 Electronic circulation of members' resolutions and members' statements - sections 249O and 249P.

Item 4: The recommendations are consistent with the amendments made under Schedule 8 of the *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act 2004* (Cth). We agree that the proposed amendments act to encourage effective and efficient distribution of notices to members.

Item 6: Subject to our comments in *Item 4*, we support the proposed amendment.

5 'Cherry-picking' of proxy votes – subsections 250A(4) and 250A(5).

Item 7: Subject to our comments below, we support the proposed amendment.

The proposed amendment to s 250A(4) is, undoubtedly, an improvement on the current situation; however, the current situation, at best, is illogical and, at worst, defies the common law of agency. The Act currently obliges only the chair of the meeting to vote on a poll and to vote each and every directed proxy given by a shareholder. Any other proxy is under no obligation to vote on a poll at all.

In *Cousins v International Brick Co Ltd*,[9] Lord Hanworth MR defined a proxy as '[a] person representative of the shareholder who may be described as his agent to carry out a course which the shareholder himself has decided upon'. Similarly, in the same case, Lawrence LJ (at 102) stated '[t]he proxy is merely the agent of the shareholder, and as between himself and his principal is not entitled to act contrary to the instructions of the latter'.

The decision of the United Kingdom Court of Appeal in *Cousins* has never received curial disagreement in Australia and, indeed, has received positive treatment as recently as 2002 by the NSW Court of Appeal in *Cadwallader v Bajco Pty Ltd*.[10] In support, we note also the unanimous decision of the NSW

[9] [1931] 2 Ch 90, 100.
[10] [2002] NSWCA 328, 152 (Dyson J), with whom Santow JA and Gzell J agreed.

Court of Appeal in *Whitlam v Australian Securities and Investments Commission*,[11] where the Court commented (at 160) that a proxy 'certainly had a duty as a fiduciary to the proxy givers to act in accordance with their directions'. We acknowledge that the proxy in question was the chair of the annual general meeting; however, in our view the Court's comments, as extracted, appear to be wider in effect and extend, at least, to all directors acting as proxy.

Thus, the common law position has always been that a proxy is the agent of the shareholder making the appointment and, as a result, is obliged to follow the direction of the shareholder as principal. That is, the common law recognises that when a shareholder appoints a person as their proxy, the shareholder is, in essence, directing the proxy to vote on the shareholder's behalf; in the case of a directed proxy, the shareholder is saying 'if I were able to attend the meeting, I would vote and would vote in the following way; I expect you to perform this precise function for me.' Yet, the existing statutory position, under s 250A(4)(d), permits a proxy to decide both whether or not to vote the proxies and which of those proxies to vote.

To the extent that the proposed amendment to s 250A(4) removes the ability of a proxy, having decided to vote on a poll, to 'cherry-pick' the proxies that will be voted, the amendment has our support. We hope that this amendment will go at least part of the way to ensuring that we do not see a recurrence of the behaviour surrounding the 2002 Coles-Myer annual general meeting.

However, in our view, the proposed amendment to s 250A(4) does not go far enough. We would encourage the PJC to recommend the Government take the opportunity in this raft of legislative amendments to require all proxies to vote on a poll. The current proposed amendments do not address the situation where a proxy is capable of voting on a poll and deliberately decides not to vote any of the proxies.

The Government acknowledges that it 'is good corporate governance to seek to ensure that persons appointed to vote as proxies vote those proxies according to the proxy terms', but considers the imposition of an obligation on all proxies to vote as being 'too onerous on shareholders'.[12] The Government provides two examples of the onerousness of such an obligation: first, that persons may be unknowingly appointed as proxies and, second, that there may be legitimate circumstances where a person other than the chair is unable to vote on a poll at all.[13] Neither of these situations are sufficient justification for not imposing an obligation on all proxies to vote. Moreover, both of these situations can be catered for within a general obligation to vote. Indeed, in proposing a new s 250A(5)(d) (see Item 8 of the Exposure Draft Bill), the Government has itself removed the concern about people unknowingly being appointed a proxy. A general obligation on proxies to vote at meetings could be made subject to a condition precedent that it be reasonable for the proxy to attend the meeting.

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[11] [2003] NSWCA 183.
[12] Explanatory Memorandum to the Exposure Draft of the Corporations Amendment Bill (No. 2) 2005 at [2.30].
[13] Id.