HIGH COURT OF AUSTRALIA

Harlowe's Nominees Pty. Ltd.

Vs.

Woodside (Lakes Entrance) Oil Co. N.L.

(Barwick C.J.(1), McTiernan(1) and Kitto(1) JJ.)

21 June 1968

BARVICK C.J.

1. This appeal is from a judgment of the Supreme Court of Victoria (Gillard J.) and the respondents, herein called respectively Woodside and Burmah, were the defendants. Harlowe, a holder of shares in the capital of Woodside, sought a declaration that a certain allotment of shares by Woodside to Burmah was invalid, and an order rectifying the register of members of Woodside by removing the name of Burmah as the holder of the shares which were the subject of that allotment. The ground upon which Harlowe claimed this relief was that the allotment was wrongful in that the directors of Woodside in making it exercised fiduciary powers otherwise than bona fide in the interests of that company as a whole, and that Burmah was at all material times aware of the facts which made it wrongful. (at p490)

2. Woodside is a no-liability mining company engaged in exploring areas on-shore in Gippsland and off several parts of the coast of Australia, with a view to discovering oil and natural gas. In its explorations it was working in collaboration with other companies including Burmah. The allotment in question was made by a resolution of the board of directors of Woodside on 31st August, 1966. It was an allotment of 9,000,000 shares of 50c each, paid up to 10c per share, and was made at a premium of 20c per share pursuant to an agreement under seal dated 17th August 1966, between Woodside and Burmah. The agreement provided for the payment by Burmah, upon application, of $900,000 to be applied in paying up the shares to 10c each, and this payment was duly made. The agreement also provided that the share certificate should be marked "Not negotiable until fully paid as to calls and premiums" and that immediately upon the allotment Burmah should have full voting rights. Other provisions were that the first call on the 9,000,000 shares and on the existing contributing shares in Woodside's capital should not be made before 1st December 1966 and should not be for more than 5c per share, and that thereafter calls should not be made on the 9,000,000 shares unless made at the same time and for the same amount as on any other then-existing contributing shares, provided that Burmah might at any time request Woodside to call up the amount remaining uncalled on the 9,000,000 shares only and that Woodside should forthwith make such call. The premium of 20c per share was deferred so as to be payable as to 10c per share within six months after payment of the final call on the 9,000,000 shares, and as to the remaining 10c per share within twelve months after such payment ; but the full premium was to become immediately due and payable if the 9,000,000 shares should be forfeited for non-payment of a call and not be redeemed. The agreement entitled Burmah to have a nominee appointed to the board of Woodside, and it gave Burmah certain rights with respect to future issues and certain protection against dealings by Woodside with petroleum rights. (at p491)

3. It will be seen that the allotment substantially improved the position of Woodside in relation to the planning and execution of explorations and the development of any areas which might be found to be oil-bearing or gas-producing on a commercial scale. Its cash position was improved by $900,000, and an additional $3,600,000 became immediately obtainable by the making of calls. True, calls would not be enforceable by action, the remedy for non-payment being forfeiture of the shares; but there was every reason for confidence that the money would be forthcoming from Burmah as soon as the need for it should arise. Burmah had ample resources to draw upon ; it would be naturally anxious to participate in the exploitation of any find that might be made ; and not only would it have invested $900,000 in Woodside but under the agreement it would be liable for the premium of $1,800,000 even if it should forfeit its shares. The ready availability of the increased capital which the agreement and the allotment thus achieved was important as giving Woodside greater freedom for the planning of explorations with its collaborators and as putting it in a position to proceed at once with the large expenditure on development which would be immediately desirable if oil or gas on a commercial scale should be found. (at p491)

4. Of course Harlowe, as a substantial shareholder in Woodside, suffered a disadvantage from the allotment, in that the 9,000,000 shares carried immediate voting rights so that existing shareholdings became fractions of 29,000,000 instead of fractions of 20,000,000. Harlowe had been buying Woodside shares heavily on the exchange, and if its object was to effect changes in the control of Woodside its hopes were seriously prejudiced, if not destroyed, by the allotment to Burmah. Its anxiety to impeach the allotment in the courts is readily understandable. The case that it set out to establish in the action was, in substance, that at the time of the agreement Woodside had no immediate need of the additional share capital, and that its directors, to the knowledge of Burmah, committed it to the issue of the 9,000,000 shares for the irrelevant and inadmissible purpose of preventing Harlowe from obtaining the voting power it had expected to obtain or, at least, without duly considering whether or not the making of the issue was truly in the interests of their company as a whole. (at p492)

5. It was contended for Harlowe that if this case in either of its alternatives were made out by the evidence in respect of each of the directors, or each of a majority of the directors, the allotment would prima facie be liable to be set aside. Questions would still arise as to the effect (if any) of certain facts upon any right which Harlowe might have to seek relief (even if it had sued in the action expressly as representing all shareholders in Woodside other than Burmah). These facts are that proceedings to impeach the allotment were not begun until 6th October 1966, and that in the meantime there were extensive dealings in Woodside's shares on the stock exchange, including substantial purchases by Harlowe itself. But the primary question was whether the directors of Woodside were in fact guilty of a misuse of power in allotting the shares to Burmah. At the trial of the action, Harlowe, having the onus of proof upon it, failed to satisfy the judge on this question, and for that reason the action was dismissed. (at p492)

6. At the threshold of the argument for Harlowe on the appeal was a submission of law which was put in the form of a corollary upon the undoubted general proposition that a power vested in directors to issue new shares is a fiduciary power which the directors are not entitled to exercise otherwise than bona fide for the benefit of the company as a whole. The suggested corollary is that an exercise of the power cannot be maintained as having been bona fide in the interests of the company unless the company had at the time of the exercise an immediate need of the capital to be paid up on the new shares. In many a case this may be true as a proposition of fact ; but in our opinion it is not true as a general proposition of law. To lay down narrow lines within which the concept of a company's interests must necessarily fall would be a serious mistake. We were invited

to do so by reference to a sentence in the judgment of Williams J. in Grant v. John Grant & Sons Pty. Ltd. [1950] HCA 54; (1950) 82 CLR 1, at p 32 , which was said to mean that an exercise of a power to issue shares must be invalid if the company "is not in need of further capital". This expression seems to have been taken by his Honour from the headnote to Piercy v. S. Mills & Co. Ltd. (1920) 1 Ch 77 . If the judgment of Peterson J. in that case, including his quotations from the judgment of Byrne J. in Punt v. Symons & Co. Ltd. (1903) 2 Ch 506 , be read in full it becomes apparent that Williams J. could not have meant to cast any doubt upon the correctness of the principle which is explained in the last cited case at pp. 515, 516. The principle is that although primarily the power is given to enable capital to be raised when required for the purposes of the company, there may be occasions when the directors may fairly and properly issue shares for other reasons, so long as those reasons relate to a purpose of benefiting the company as a whole, as distinguished from a purpose, for example, of maintaining control of the company in the hands of the directors themselves or their friends. An inquiry as to whether additional capital was presently required is often most relevant to the ultimate question upon which the validity or invalidity of the issue depends ; but that ultimate question must always be whether in truth the issue was made honestly in the interests of the company : Richard Brady Franks Ltd. v. Price [1937] HCA 42; (1937) 58 CLR 112, at p 142 ; Mills v. Mills [1938] HCA 4; (1938) 60 CLR 150, at pp 163, 169 ; Ngurli Ltd. v. McCann [1953] HCA 39; (1953) 90 CLR 425, at pp 438-441 . Directors in whom are vested the right and the duty of deciding where the company's interests lie and how they are to be served may be concerned with a wide range of practical considerations, and their judgment, if exercised in good faith and not for irrelevant purposes, is not open to review in the courts. Thus in the present case it is not a matter for judicial concern, if it be the fact, that the allotment to Burmah would frustrate the ambitions of someone who was buying up shares as opportunity offered with a view to obtaining increased influence in the control of the company, or even that the directors realized that the allotment would have that result and found it agreeable to their personal wishes : Mills v. Mills [1938] HCA 4; (1938) 60 CLR 150 . But if, in making the allotment, the directors had an actual purpose of thereby creating an advantage for themselves otherwise than as members of the general body of shareholders, as for instance by buttressing their directorships against an apprehended attack from such as Harlowe, the allotment would plainly be voidable as an abuse of the fiduciary power, unless Burmah had no notice of the facts. (at p494)

7. The first task of the trial judge, then, was to decide whether it was established to his satisfaction, even if only on a balance of probabilities, that the directors were actuated by an impermissible purpose. There were five of them : Withers the managing director, Donaldson the chairman of directors, Hughes-Jones, Humphris and Tarrant. The board meetings were informal affairs, and the minutes were not kept in any such detail as to assist materially in the inquiry. The judge's findings were based to a large extent upon his opinion of the witnesses, but it is strongly urged that they were vitiated by errors in appreciation of the proved circumstances and in assessment of the inherent probabilities of the case. (at p494)

8. It is right to keep in mind, as counsel for Harlowe has urged us to do, that at the time of the agreement with Burmah there was an active market for Woodside shares, and that the ruling prices were well above par - indeed the margin above par was greater than the premium Burmah agreed to pay. Additional capital might thus have been obtained by offering the new shares either proportionately to existing shareholders or to the public. Either way Harlowe would have had at least an opportunity of participating in the new issue. The placement with Burmah therefore represented a deliberate choice by the directors, and the suggestion is that the choice must have been made for the sake of denying to Harlowe (at that time an unidentified "mystery buyer") the chance of acquiring any of the 9,000,000 new shares and so for the sake of enhancing the likelihood of the

directors retaining their positions on the board. All this leaves out of account, however, that even though an issue of shares might have been successfully offered to existing members or to the public, and even though a higher premium might have been obtained, it was by no means certain that so large a number as 9,000,000 shares would have been taken up on terms forbidding alienation while the shares were not fully paid, and it was still less certain that an issue of that magnitude would have commanded so large a premium. One point which is emphasized on behalf of Harlowe is that even if Woodside had a need of additional share capital the peculiar number of 9,000,000 shares was not shown to have been reached by any process of precise estimate of the actual needs of Woodside ; and a note which Burmah's chairman of directors made on 23rd May 1966 is pointed to as tending to support the view that the number was selected specifically by reference to the effect the new issue would have upon the position of the "mystery buyer". This note, Ex. V, refers to the "Woodside counter proposal", and shows that the result of issuing 9,000,000 shares with full voting rights would be to range interests holding 37.92 per cent of an issued capital of 29,000,000 shares against "opposing interests" which might have 10.3 to 17.2 per cent of that capital but were "still buying". On the other hand, according to Donaldson the directors had agreed, even before Withers first went to London to negotiate with Burmah, that the placement should be of "substantially a third" of the pre-existing capital, and 9,000,000 was not far from that mark. This was supported by the evidence of Hughes-Jones and Humphris. (at p495)

9. The crucial question of the purpose with which the Burmah placement was made depended fundamentally upon the judge's assessment of the evidence of the four directors who went into the witness-box. The fifth director was Tarrant ; he was abroad at the time of the trial and no evidence had been obtained from him. In fact there was no evidence at all, apart from general evidence of the surrounding circumstances, to give any clue to his purposes or mental processes concerning the Burmah allotment. (at p495)

10. The man who took the most active part in the whole affair was the managing director, Withers, whom the judge regarded as an unsatisfactory witness and a "single-minded opportunist who was not handicapped by any scruples or feelings of loyalty". It was he who had interested Burmah in the idea of taking a large parcel of Woodside shares and had conducted in Australia and in England the negotiations which led to the agreement. In written and oral communications with Burmah's representatives he had pointed to the apparent danger of an imminent take-over of Woodside by the "mystery buyer" ; but his evidence was that in doing this he was merely exciting Burmah's fears in order to serve Woodside's interests by bringing about some such agreement as in fact eventuated, and that the fear of a take-over did not influence his own thinking at all. What he said and wrote in the course of the negotiations contains much to suggest that his real object was to protect his own position in relation to the control of Woodside ; but in the end, the judge, though regarding his evidence with suspicion and distrust, was satisfied that his purpose was not to defeat the "mystery buyer", but was to ensure the financial stability of Woodside. (at p495)

11. His Honour's finding on this matter is strongly attacked. It is pointed out that at the time of the Burmah placement Woodside had available funds in the vicinity of $1,000,000 and had $4,000,000 of uncalled share capital which, in view of the active interest in Woodside shares on the stock exchanges, might be called up with confidence. Moreover, no proved estimate of immediately foreseeable expenditure suggested a need for so large a placement of shares as was made to Burmah - though indeed Withers made an estimate (Ex. 12W) (in May 1966, he said) and produced it, according to Donaldson, to all directors in that month, which showed expected expenditure at $5,440,000 and funds available from cash and calls on uncalled capital at $5,024,000. It must be conceded that there is force in the comment that Withers, in his own interests, would have been far

less likely to deceive Burmah as to the reality of a danger of an imminent take-over - a matter as to which he would almost certainly be found out sooner or later if it were false - than he would have been to lie to the court as to what his purpose was in inducing Burmah to accept the allotment. And it must be added that there is strong evidence that Withers was in fact apprehensive of an impending take-over by some outside interests, that he had a strong personal preference for Burmah, and that the only alternative potential allottee whom he ever considered was another "partner" of Woodside, namely Shell. These considerations are undoubtedly weighty, but they are not irreconcilable with a conclusion that the purpose, even of Withers, in the making of the placement was the purpose of putting Woodside in a position of vastly greater freedom to plan for increasing participation with its "partner", Burmah, in the activities for which hopes in many quarters were running high. Withers was crossexamined at great length, and the judge, fully alive though he was to the general unreliability of the man as a witness, accepted his sworn testimony on the vital point. A court of appeal is simply not in a position to say that in doing so his Honour was wrong. (at p496)

12. Much was said in argument to the effect that the judge erred in supposing that there was reality in the notion, to which Withers and his colleagues repeatedly referred, of ensuring Woodside's financial stability. The submission was that stability has no real meaning in the case of a no-liability company until it has found oil and set up an established production operation, and that in the meantime such a company needs only sufficient funds for operations that either are current or are planned for the near future. This does not seem to us to be a sound criticism of the finding. For reasons which we have already indicated we think that in a very relevant sense even a no-liability company in the position of Woodside, while still at the stage of searching for deposits to be exploited, may well be considered by its directors to need such an assurance of future substantial financial backing by an existing collaborator as the agreement with Burmah provided. (at p497)

13. A fact which counsel for Harlowe has emphasized was that some of the reasons Withers gave in his evidence as having led him to believe that the agreement with Burmah would provide stability for Woodside were never stated in any of the reports that were made to the shareholders of Woodside. There was, for example, no mention of a probability of benefits from a closer association with Burmah in disposing of crude oil if and when produced, or of benefits from an association that existed between Burmah and British Petroleum which possessed established refining and marketing facilities. There was not, of course, a complete absence of reference in the reports to the advantages of the availability of call money and premiums. As the judge pointed out in his reasons, the annual report of Woodside's board dated 28th September 1966, before the litigation began, made specific mention of Woodside's close association with Burmah in off-shore investigations on the north-west coast of Australia and the Gippsland coast, and said that "moneys now available to Woodside, by way of calls and the premium which the Burmah placement has made, total ten and a half million dollars. This is sufficient to meet our budget requirements over the next few years." Still, it is true that other advantages which Withers swore that he had regarded as important were not mentioned in the reports at all. With this and other considerations in mind, one cannot but concede that Harlowe's case at the trial was not unsubstantial. So much depended, however, upon a discriminating assessment of the evidence of all the witnesses as it was given in the witness-box that in a court of appeal considerations such as those above mentioned have nothing like the force that they might possess in the court of first instance, and are not sufficient to displace the trial judge's findings of fact. (at p497)

14. If, as we think, the finding as to Wither's purpose must be accepted, the case for Harlowe becomes very difficult ; for there was not nearly as much reason for regarding with scepticism the evidence of the other three directors who went into the box as there was for so regarding the

evidence of Withers, and the judge, having seen and heard them, was satisfied that at the material time they believed the agreement with Burmah ensured Woodside's future. One criticism of their evidence was that they were unable satisfactorily to amplify the statement in the report of 28th September 1966 as to Woodside's "budget requirements over the next few years" or to explain why they did not spell out to the shareholders all the reasons to which they deposed in the witness-box for thinking that the Burmah agreement was in Woodside's interest. But the judge, having this criticism pressed strongly upon his attention, accepted the evidence of the directors as to the purpose they had in approving the agreement and making the allotment. His view clearly was that though their thinking was greatly influenced by Withers, it was honest thinking, and was directed to the interests of their company and not to the prevention of a take-over. (at p498)

15. It is perhaps desirable to say a word about each of them. Donaldson, the chairman of the board, had more difficulty than Hughes-Jones or Humphris in satisfying the judge of the genuineness of his belief that the agreement served the best interests of the company, partly because he seemed at times not to be perfectly frank in his evidence, and partly because it seemed prima facie likely that he would have been aware of the representations which Withers had made to Burmah as to the signs of an endeavour by the "mystery buyer" to bring about a take-over. But in the end the judge was satisfied of the genuineness of Donaldson's belief, first that Woodside required large sums of money for exploration and development work, secondly that accordingly any capital then raised would be beneficial to the company by giving it financial stability in the sense of enabling it to "programme" (sic) without fear that money would not be forthcoming when called up, and thirdly that Burmah was not being favoured at the expense of the existing shareholders, because an offer to the shareholders or to the public at a premium, subject to the condition against disposing of the shares until fully paid, would not have been successful. (at p498)

16. Hughes-Jones was believed when he said that he considered Woodside was in need of substantial sums of money, that the Burmah agreement would give Woodside "financial stability for the foreseeable future", and that therefore it was for the benefit of the company ; and he was believed when he said that the threat of a take-over did not affect his thinking at all in making the placement. (at p498)

17. Humphris, the remaining director, is in like case. The judge, who regarded him as a careful and highly intelligent person, believed him when he denied that he had had any impression that the "mystery buyer" was seeking to achieve a degree of control of Woodside and when he deposed that he had become enthusiastic for the Burmah agreement as providing Woodside with funds to carry out its future planning and giving it a financial stability such as he believed it should have. (at p498)

18. The attack that has been made on behalf of Harlowe upon the conclusion that (leaving Tarrant aside) the directors other than Withers agreed to the Burmah allotment because they thought it was in the best interests of Woodside, took in the main the shape of a submission that these directors were merely compliant with any recommendation made by Withers, and failed in their duty by not applying their minds to the needs of Woodside sufficiently to form any positive opinion that the allotment on the terms of the agreement was in the interests of that company. It would indeed be enough for Harlowe's purposes in the case to show that the evidence established the negative proposition that whatever induced the board's decision in favour of the agreement it was not a purpose of thereby serving the interests of the company as a whole, and accordingly during the argument on behalf of Harlowe a good deal of time was taken up with submissions based upon an assertion that the evidence showed an absence of attention on the part of the directors other than Withers to any question about the allotment except the question of the premium. It will suffice to

say by way of answer that numerous passages in the evidence would have to be ignored before that view could be adopted. And a point worth remarking upon is that although the Burmah agreement was made pursuant to a "letter of intent" and the full terms of that document were presented to the board at a meeting on 20th June 1966 (Ex. AC) at which Hughes-Jones and Humphris were present, and was then and there unanimously approved, neither Hughes-Jones nor Humphris was asked in the course of lengthy cross-examinations any question at all about the consideration they gave or failed to give to the proposal at that crucial meeting. The decisive fact now, however, is that the judge's findings were against the negative proposition which Harlowe set itself to establish, and it seems to us impossible in all the circumstances of the case for a court of appeal to hold that the proposition was made out. The findings to which we refer are reflected in several passages in his Honour's reasons, but one quotation will suffice. Speaking of Donaldson, Hughes-Jones and Humphris, his Honour said:

> "I am sufficiently convinced of their credibility to hold that they at least did not make a placement with Burmah to thwart or prevent any possible influence or control of any shareholder of the Woodside Co. I also hold that although I believe the directors' opinion of the needs of the company was imprecise, probably intuitive and maybe erroneous, yet each one of them addressed his mind to the relevant problem and exercised the power to issue shares, bona fide, in order to raise money for the company's future requirements which they believed would exist. I am of the view that this was generally (? genuinely) held by each of them and their desire was to give financial stability to the company in its future programme." (at p500)

19. What has been said is enough to dispose of the appeal. If we had been of the contrary opinion a serious question would have remained, namely whether proof of the Woodside directors' breach of duty would have entitled Harlowe to have the allotment set aside as against Burmah. We need not discuss this question; but we must make it clear that we are not to be taken as denying that Burmah's legal title to the shares would have provided an effective answer to a claim for the relief that Harlowe seeks, in the absence of a finding that at the time of the allotment Burmah had notice of the breach of duty. There is no need to consider the further defence of laches and acquiescence. (at p500)

20. The appeal fails and should be dismissed. (at p500)

ORDER

Appeal dismissed with costs.

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