International Survey of Corporate Law in Asia, Europe, North America and the Commonwealth

By Cally Jordan

Centre for Corporate Law and Securities Regulation
INTERNATIONAL SURVEY OF CORPORATE LAW IN ASIA, EUROPE, NORTH AMERICA AND THE COMMONWEALTH

Cally Jordan
Centre for Corporate Law and Securities Regulation

CENTRE FOR CORPORATE LAW AND SECURITIES REGULATION
FACULTY OF LAW
THE UNIVERSITY OF MELBOURNE
1997
Hong Kong Companies Ordinance Review

The Review of the Hong Kong Companies Ordinance was announced by the Financial Secretary in his budget speech of March 2, 1994. "We have tried in the past to respond to developments in the corporate world through piecemeal amendment of the Ordinance. I believe we have reached a stage when a thorough review has become essential. We now need an Ordinance for the 21st century". On November 23, 1994, the Hong Kong Government appointed Mr Ermanno Pascutto, the former Deputy Chairman of the Securities and Futures Commission in Hong Kong, to lead the review of the Hong Kong Companies Ordinance.

Cally Jordan, then an Associate Professor at the Faculty of Law, McGill University in Montreal, Canada was engaged on a full-time basis to research and prepare the reports associated with the Review. She relocated to Hong Kong in order to do so.

The International Survey of Corporate Law in Asia, Europe, North America and the Commonwealth was the first major report produced. It appeared in 1996 and is also available in Chinese. Over a dozen reports, background memoranda and briefing books were prepared in the course of the Review. The final report for the Review of the Hong Kong Companies Ordinance was submitted to the Hong Kong Government on March 31, 1997.

For further information, please contact Cally Jordan directly at telephone (852) 2537 8211; facsimile (852) 2845 9076; and by e:mail 101610.2263@compuserve.com or c/- Stikeman, Elliott, 29 Queen’s Road Central, 11/F, Hong Kong.
Centre For Corporate Law And Securities Regulation

The Centre for Corporate Law and Securities Regulation was established in January 1996. Its objectives are to:

- undertake and promote research and teaching on corporate law and securities regulation
- host conferences to disseminate results of research undertaken under the auspices of the Centre or in other programs associated with the Centre
- develop and promote links with academics in other Australian universities and in other countries who specialise in corporate law and securities regulation
- establish and promote links with similar bodies, internationally and nationally, and provide a focal point in Australia for scholars in corporate law and securities regulation
- promote close links with peak organisations involved in corporate law and securities regulation
- promote close links with those members of the legal profession who work in corporate law and securities regulation.

The Director of the Centre is Professor Ian Ramsay who is also the general editor of the monograph series published by the Centre of which this monograph is a part.

The Centre has an Advisory Board chaired by The Hon Mr Justice Ken Hayne of the Victorian Court of Appeal and comprising senior legal practitioners, company directors and directors of the Australian Securities Commission and the Australian Stock Exchange.

Previous publications of the Centre include:

- Phillip Lipton, The Authority of Agents and Officers to act for a Company: Legal Principles
- Ian Ramsay (ed), Gambotto v WCP Ltd: Its Implications for Corporate Regulation
- Geof Stapledon and Jeffrey Lawrence, Corporate Governance in the Top 100: An Empirical Study of the Top 100 Companies’ Boards of Directors
- Megan Richardson (ed), Deregulation of Public Utilities: Current Issues and Perspectives.

Further information about the Centre is available on the Centre’s Website, the address of which is: “http://www.law.unimelb.edu.au/cclsr.html”. The Administrator of the Centre may be contacted on tel 61 3 9344 5281; fax 61 3 9344 5285; e-mail: “cclsr@law.unimelb.edu.au”.

v
# Table of Contents

**PART 1 — INTRODUCTION**

**Purpose of the Survey**  
Background to the Review  
International Trends  

**Scope of Survey**  
United Kingdom  
Commonwealth  
  *Australia*  
  *Canada*  
  *New Zealand*  
  *South Africa*  
United States  
Continental Europe  
Asia  
  *Singapore*  
  *People's Republic of China*  
Bermuda  

**Jurisdictions Not Considered**  

**Aspects Examined**  

**PART 2 — THE UNITED KINGDOM**

**Introduction**  
A Period of Transition and Instability  
  *The Views of the Commentators*  
  *The Views of the Law Society*  

**Recent Legislative History**  
The Period 1948 to 1983  
  *The Companies Act 1948*  
  *The Companies Act 1967*  
  *European Communities Act 1972, section 9*  
  *The Companies Act 1976*  
  *The Companies Act 1980*  
  *The Companies Act 1981*  
The Period 1985 to the Present  
  *The Companies Act 1985*  
  *The Recharacterisation of Company Law*  

<table>
<thead>
<tr>
<th>PART</th>
<th>Section</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Purpose of the Survey</td>
<td>2</td>
</tr>
<tr>
<td>1</td>
<td>Background to the Review</td>
<td>2</td>
</tr>
<tr>
<td>1</td>
<td>International Trends</td>
<td>2</td>
</tr>
<tr>
<td>1</td>
<td>Scope of Survey</td>
<td>3</td>
</tr>
<tr>
<td>1</td>
<td>United Kingdom</td>
<td>3</td>
</tr>
<tr>
<td>1</td>
<td>Commonwealth</td>
<td>3</td>
</tr>
<tr>
<td>1</td>
<td>Australia</td>
<td>3</td>
</tr>
<tr>
<td>1</td>
<td>Canada</td>
<td>4</td>
</tr>
<tr>
<td>1</td>
<td>New Zealand</td>
<td>4</td>
</tr>
<tr>
<td>1</td>
<td>South Africa</td>
<td>4</td>
</tr>
<tr>
<td>1</td>
<td>United States</td>
<td>4</td>
</tr>
<tr>
<td>1</td>
<td>Continental Europe</td>
<td>5</td>
</tr>
<tr>
<td>1</td>
<td>Asia</td>
<td>5</td>
</tr>
<tr>
<td>1</td>
<td>Singapore</td>
<td>5</td>
</tr>
<tr>
<td>1</td>
<td>People's Republic of China</td>
<td>5</td>
</tr>
<tr>
<td>1</td>
<td>Jurisdictions Not Considered</td>
<td>6</td>
</tr>
<tr>
<td>1</td>
<td>Aspects Examined</td>
<td>6</td>
</tr>
<tr>
<td>2</td>
<td>Introduction</td>
<td>8</td>
</tr>
<tr>
<td>2</td>
<td>A Period of Transition and Instability</td>
<td>8</td>
</tr>
<tr>
<td>2</td>
<td>The Views of the Commentators</td>
<td>8</td>
</tr>
<tr>
<td>2</td>
<td>The Views of the Law Society</td>
<td>9</td>
</tr>
<tr>
<td>2</td>
<td>Recent Legislative History</td>
<td>11</td>
</tr>
<tr>
<td>2</td>
<td>The Period 1948 to 1983</td>
<td>11</td>
</tr>
<tr>
<td>2</td>
<td>The Companies Act 1948</td>
<td>11</td>
</tr>
<tr>
<td>2</td>
<td>The Companies Act 1967</td>
<td>12</td>
</tr>
<tr>
<td>2</td>
<td>European Communities Act 1972, section 9</td>
<td>12</td>
</tr>
<tr>
<td>2</td>
<td>The Companies Act 1976</td>
<td>13</td>
</tr>
<tr>
<td>2</td>
<td>The Companies Act 1980</td>
<td>13</td>
</tr>
<tr>
<td>2</td>
<td>The Companies Act 1981</td>
<td>14</td>
</tr>
<tr>
<td>2</td>
<td>The Period 1985 to the Present</td>
<td>15</td>
</tr>
<tr>
<td>2</td>
<td>The Companies Act 1985</td>
<td>15</td>
</tr>
<tr>
<td>2</td>
<td>The Recharacterisation of Company Law</td>
<td>15</td>
</tr>
</tbody>
</table>
1. Financial Services Act 1986 15
2. The Insolvency Act 1986 16
3. The Company Directors Disqualification Act 1986 17
    The Companies Act 1989 17

Recent Trends in UK Companies Law 18

PART 3 — THE COMMONWEALTH

Australia 22
Introduction 22
Legislative History 24
    Period prior to the draft Companies Bill 1961 24
    Period Following the Draft Companies Bill 1961 25
    The First Cooperative Scheme 26
    The National Scheme 27
General Trends and Developments 28

Canada 31
Introduction 31
Historical Background 33
General Observations and Trends 36

New Zealand 37
Introduction 37
Historical Background 37
General Observations 42

South Africa 43
Introduction 43
Historical Background 44
South African Close Corporations Act 69 of 1984 45
General Observations 47

PART 4 — THE UNITED STATES

Introduction 50
Historical Development 51
General Characteristics of US Corporate Law 52
General Observations 54
# PART 5 — CONTINENTAL EUROPE AND THE EUROPEAN UNION

**Introduction** 58

**France** 60
- Société Anonyme 61
- Société à Responsabilité Limitée 62
- Other Corporate Forms 62

**Germany** 63
- Aktiengesellschaft or AG 63
- Gesellschaft Mit Beschrankter Haftung or GMBH 63

**European Union** 64

# PART 6 — ASIA

**Hong Kong** 66
- Legislative History of the Companies Ordinance 66
  - *Phase One: The UK Model: 1865–1932* 66
    - 1. The Companies Act 1862/Companies Ordinance 1865 67
    - 2. The Consolidations of 1908 and 1929 in the UK and 1911 and 1932 in Hong Kong 67
    - 3. The Opening of the Gap: The Companies Act 1948 (UK) 69
  - *Phase 2: A Period of Legislative Stasis 1932–1984* 71
    - 1. The Second Report of the Companies Law Revision Committee — Company Law 72
    - 2. The Companies (Amendment) Ordinance 1984 74
  - *Phase 3: Work of the Standing Committee on Company Law Reform: 1984 to the Present* 75
    - 1. Major Preoccupations of the Standing Committee 77
    - 2. Major Difficulties Encountered by the Standing Committee 78
    - The Role and Organisation of the Companies Registry 80
- The Legislative Framework of the Companies Ordinance 81
  - *Core Company Law: the Formation, Operation and Termination of a Company* 81
    - 1. Formation of a Company 83
    - 2. Operation of a Company 83
    - 3. Termination of a Company’s Existence 86
  - Non-Core Company Law Matters 86

**Singapore** 86
- Introduction 86
- Historical Background 87
- Significant Provisions of the Singapore Companies Act 88
  - Directors and Officers 88
Part 1

Introduction
Part 1

Introduction

This International Survey of company and corporate law regimes in a number of jurisdictions was prepared for the Review of the Hong Kong Companies Ordinance. The United Kingdom, several Commonwealth jurisdictions, the United States, South Africa, Hong Kong, Singapore and the People’s Republic of China have been chosen for consideration. In addition, shorter sections on the European Union, France, Germany and Bermuda have been added.

Purpose of the Survey

Background to the Review

This Survey is a response to suggestions and comments from several quarters. Hong Kong lawmakers are at a crossroads. The Survey is designed to provide necessary information against which important issues may be assessed. For example, the one person company, also known as the single shareholder corporation, has long been available in many jurisdictions. Some jurisdictions have a separate legal regime for small or closely-held businesses. The thorny issue of the ultra vires doctrine has been eliminated with no adverse consequences in many parts of the world. Although the Hong Kong Companies Ordinance Review is not necessarily proposing the adoption as a model for Hong Kong of any of the regimes described, other jurisdictions may provide solutions or approaches which could be usefully adapted to the Hong Kong business environment.

The purpose of the Survey is also very much informative: it deals with how companies and corporations are governed in other jurisdictions; how the major issues associated with corporate activity are dealt with elsewhere; what the major differences are in approach from one jurisdiction to another; and how different historical developments have affected current structures.

International Trends

As well, the Survey gives some indication of dominant trends worldwide with respect to company law. With the rapid internationalisation of financial and commercial activity in recent years, there has developed an increasing interdependence of domestic legal regimes.

This interdependence has led to greater understanding and awareness in the major commercial jurisdictions of non-domestic legislative approaches and solutions. The
result has been a greater willingness to consider the domestic application of what would otherwise have been considered unsuitable "foreign" notions. There has been a notable convergence in the legal approaches to commercial problems. The degree of convergence internationally varies from one area of commercial law to another. The domestic regulation of capital markets (securities regulation, for example) has been subjected to strong pressures to conform to international standards. Companies law on the other hand, has not been subject to the same degree of pressure. Nonetheless, the internationalisation of commercial activity has promoted the cross-fertilisation of company law concepts. Europe, for example, has looked to America's one-person corporation, while America has looked to European-style legal personality for partnerships. The People's Republic of China, it would seem, has looked everywhere.

Scope of Survey

Of necessity, this Survey has had to be selective and the discussion that follows does not purport to be exhaustive. And legislative activity never ceases. The Survey is based on reasonably current public information about each jurisdiction, in some cases supplemented by personal interviews with knowledgeable authorities in the jurisdiction. Some parts of the Survey may be less current than others but we hope this will not detract from their utility.

United Kingdom

As the United Kingdom has been the source of Hong Kong companies law for 130 years, we have assumed familiarity with UK companies law principles and have dealt primarily with more recent developments there.

Commonwealth

The major focus of this Survey has been on Commonwealth jurisdictions given that they share common legal traditions with Hong Kong. However, despite their common roots in UK law, there has been considerable divergence and evolution in Commonwealth regimes over time.

Australia

Of all the jurisdictions surveyed, Australia has maintained the closest links with the United Kingdom. However, the legal regime introduced in Australia has had to be modified from a model developed in a unitary state to one more appropriate for Australia's federal system. In the area of corporations legislation in Australia, there is currently a major simplification project under way which may result in significant divergence from UK legislation.
Canada

Some twenty-five years ago, Canada decided to break away from the UK model in companies law and look, in large part, to the Model Business Corporations Act in the United States. Given the degree of economic and commercial integration which has taken place in North America since that time, the decision to do so was prescient if not inevitable. Still, the case law and certain aspects of the statutory regime in Canada retain elements of UK companies law, most notably in the area of minority shareholder protection. As well, unlike the major Canadian jurisdictions for incorporation, certain smaller provincial company law regimes retain, to a greater or lesser degree, older UK influences.

New Zealand

Although lacking the same geographic imperative as Canada, New Zealand has recently made a similar decision to break away from the UK model. The New Zealand Law Commission, in its 1989 and 1990 reports, recommended a radical departure from the UK Companies Act in turning to North American regimes for inspiration. The resulting legislation has been criticised as having lost its integrity during the legislative drafting process, and now represents a somewhat uneasy compromise of the North American and UK models.

South Africa

South Africa, once again a member of the Commonwealth, is a mixed jurisdiction, its legal system combining elements of Roman-Dutch civil law and English common law. As in many other Commonwealth countries, the UK Companies Acts had long provided the inspiration for company law in South Africa.

The particular interest of looking to South Africa in this Survey is the generally successful experience which South Africa has had with the implementation of its Close Corporation Act, introduced in 1984. The legislation, a unique combination of different legal systems, nonetheless is closer in inspiration to American models than any other. It now accounts for nearly five times as many incorporations as all other forms combined.

United States

With its great diversity of 50 state corporation acts, model laws, abundant judicial interpretation and wealth of critical commentary, the United States must be considered in any survey of this nature. Given the vastness of the subject, we have confined our comments to the (Revised) Model Business Corporations Act (1984), and references where pertinent to its predecessor, the Model Business Corporations Act, as well as Delaware and New York law, with an aside or two on California.
Introduction

Continental Europe

Although we had originally decided to exclude continental European systems from the scope of the Survey (on the basis that they were too far removed from the current regime in Hong Kong), we have reconsidered this decision in light of their influence on recent developments in both the United Kingdom and the People’s Republic of China. We have thus included some brief observations on France, Germany and the European Union’s project for a pan-European company law, the societas europea.

Asia

Hong Kong

The Companies Ordinance is one of the largest and most complex pieces of legislation in Hong Kong. In structure and approach, its 19th century origins are still very much apparent. Although amendments have been ongoing in an effort to adapt the Ordinance to changing times, it remains the case that the last major review of the Ordinance was implemented over ten years ago (in 1984) based on a 1973 Report of the Companies Law Revision Committee; it was only then that the Ordinance was brought broadly into line with the UK Companies Act 1948. In Part 6 we examine in detail the legislative history and current framework of the Companies Ordinance.

Singapore

We have chosen to include Singapore in our Survey for two reasons. First, Singapore, like Hong Kong, shares a British heritage for its Companies Act. Secondly, in terms of the significance of its commercial and financial activity, regional location, size, etc, it is the jurisdiction most directly comparable to Hong Kong. Singapore launched a review of its Companies Act in July, 1995, for much the same reasons this Review was undertaken.

People’s Republic of China

The People’s Republic of China implemented a Companies Law in July 1994. Given its very recent introduction, there has not yet been extensive analysis of this new legislation which is available in English. The creation of a companies law in the PRC is an event of historic proportions in the commercial world. Although not suggested as a model to be followed in Hong Kong, in the present political context, it is important to be aware of developments taking place on the mainland.

Bermuda

Bermuda is the jurisdiction of choice for incorporation of approximately 40 per cent of Hong Kong listed companies. Although greater study will be devoted later in this
Review to the recent phenomenon of overseas incorporation, a brief exposition of Bermuda companies legislation is included here.

**Jurisdictions Not Considered**

There are no doubt other interesting comparisons which could be made and other jurisdictions at which to look. To a certain extent the decision to end here is an arbitrary one. Why not Japan? Why not Taiwan? Wouldn't Delaware, given its importance, merit separate consideration on its own? Why not the British Virgin Islands? We recognise the limitative nature of this endeavour, but would like to keep this report to manageable and readable proportions, while still permitting enough analysis to be useful. This does not in any way preclude consideration of developments in other jurisdictions as the Review progresses. For example, we would fully expect to consider Delaware law in greater detail in the fourth stage of the Review (Directors Duties; Corporate Governance) and Bermuda and the British Virgin Islands in the fifth stage of the Review (Foreign Corporations).

**Aspects Examined**

Given the breadth of the Survey, the examination of each legal regime will of necessity be cursory. We propose to give a brief legislative history indicating the sources of the companies or corporations laws in each jurisdiction, the direction which they have taken over time and their main characteristics. We hope to highlight distinctive features (such as the close corporation in South Africa) as well as similarities and points of convergence among the various regimes. In keeping with the Terms of Reference of the Review, we will touch in particular on the reach of companies law, corporate formalities, shareholders' remedies, directors' duties and the treatment of foreign corporations.
Part 2

The United Kingdom
Part 2

The United Kingdom

Introduction

A Period of Transition and Instability

Company law in the United Kingdom over the last fifteen years has been going through a difficult period of transition and instability. Nearly a dozen major statutory initiatives associated with companies law have been introduced or attempted. Despite this agitated level of legislative activity, the underlying structure and conceptual basis of UK companies law has not been reconsidered. The last comprehensive reviews of UK companies legislation date from the days of the Cohen Committee Report (1945) and the Jenkins Committee Report (1962). The UK legislation is showing the marks of decades upon decades of legislative accretion.

The Views of the Commentators

Legal commentators following developments in companies law in the United Kingdom have been harsh in their assessment. The state of the legislation, some hold, is such that it undermines its very purpose.


In comparing UK companies law to North American regimes, Professor Sealy, writing in 1984, was scathing in his criticism of Parliament, the judiciary and the process of reform in the United Kingdom. Parliament continues unwittingly to add to the existing complexity and formality of the legislative regime without consideration for the burdens and costs imposed; the judiciary takes a narrow and technical view at odds with commercial expectations; and the process of reform itself is flawed by “our myopic attitudes and cheeseparing approach to research and fact-finding” (L S Sealy, Company Law and Commercial Reality (London: Sweet & Maxwell, 1984) at 71).

But Parliament in this country seems concerned only to add to the formalities, to increase checks and balances and votes and consents, seemingly indifferent to the burden and delays and the extra cost that those requirements impose on commerce — costs which ultimately fall on us all. The courts take a similar line. It is not difficult to find instances, many quite recent instances, where the judge has sent the parties away to get another consent or class vote, or has
exercised a discretion in a way that is bound to bring new uncertainties to the conduct of business, or in the name of "equity" has imposed fetters on the shareholder's freedom to vote, with the result that what ought to be a simple democratic process is inhibited from taking its natural course, or has found some technical or procedural difficulty all-important, when on a broader view it wouldn't really matter a whit (*ibid* at 7).

Professor Gower has stated that by 1985 UK companies legislation "was in a worse state than at any time this century" (*L C B Gower et al.*, *Gower's Principles of Modern Company Law*, 5th ed (London: Sweet & Maxwell, 1992) at 51). He laments the fact that the United Kingdom no longer provides the model for company law to the Commonwealth. His "sad conclusion" is that the UK is unlikely to provide a model in the future.

Nor can it be said that our company legislation has not reacted to changing conditions. Legislation which grew from 212 sections and three schedules in the Companies Act 1862 to 747 sections and 25 Schedules in the Companies Act 1985 cannot be accused of stagnation. [fn.A more legitimate criticism is that it has grown excessively; no other country's legislation goes into such detail.] But if one looks at the major developments this century and at the problems that these have thrown up, it is difficult to avoid the conclusion that there has been a reluctance to recognize their implications for Company Law and that, when those implications have been recognised, the reaction has been to add to the existing framework without ever re-examining its foundations to ensure that they are still sufficiently sound to bear the weight of the expanding superstructure (*ibid* at 70).

Gower's observations are echoed by other commentators.

*The Views of the Law Society*

One of the harshest critics of the UK Companies Act has been the Law Society. The Law Society's Standing Committee on Company Law deplores the "lack of overall strategy for company law". In its 1991 paper, *The Reform of Company Law*, the Committee is unsparing in its criticism.

In a significant number of cases, as a result of the shortcomings to which we have referred:
- legislation fails to achieve its objectives;
- legislation is unduly complex and obscure;
- the manner in which the legislation is brought into force leads to confusion as to the state of the law; and
- there is unacceptable delay.

The result is a waste of time and money as the business community and its advisers try to come to terms with changing legal requirements (The Law Society (UK), Company Law Committee, Memorandum, *The Reform of Company Law* (July 1991) at 11).

The Law Society admits that modern company law deals with complex issues and that company legislation will reflect this complexity, but "complexity is not the same as obscurity" (*ibid* at 6).

The following factors are identified as sources of the current problems in UK company law: a piecemeal approach to reform "on an ad hoc and isolated basis" (*ibid* at 5), changes inspired "partly by political enthusiasm and partly as a reaction to particular
events” (ibid) and the lack of scope for a more considered and longterm view of the underlying objectives of company law.

Partly as a result of the piecemeal approach to reform to which we have referred, company legislation has increased both in complexity and length. Although a crude measure, it is worth recording that the first edition of Butterworths Company Law Handbook (the edition immediately before the Companies Act 1980) contained 462 pages, while the latest edition contains 3,544 pages. In fact, the increase is greater than that. As a result of the encroachment of the Financial Services Act into many areas of company law, to obtain an accurate comparison it would be necessary to include the huge volumes of subsidiary legislation resulting from the rules of such bodies as the SIB, the SROs, the RPBs and the RIEs (ibid at 6).

Certainty in commercial relations, according to the Law Society, has been the main victim of this unfortunate situation in the UK. “It is also important that there should be no major areas of uncertainty in our company law, because of the waste of time and money involved in attempting to resolve uncertainty. To the extent that there are uncertainties in company law, the attractiveness of the United Kingdom as a centre for inward investment may be diminished” (ibid at 4).

To this difficult situation has been added the complicating factor of compliance with European Commission Directives on Company Law. UK company law is being influenced by the legal systems of other Member States in the European Union “which are radically different from ours” (ibid at 6). Harmonisation is not necessarily undesirable; the concern expressed by the Law Society is more to the effect that these foreign influences are being exerted at a time when the domestic law is in a state of disarray.

Harmonisation will inevitably lead to some degree of influence by foreign laws, but from the United Kingdom perspective the situation could be much improved if resources were available to take a more positive and reforming lead in the area of company law within Europe, particularly in the early stages before the momentum has built up to introduce what, from the United Kingdom standpoint, are potentially deleterious changes (ibid).

Although the pressures of compliance with European Commission Directives are often identified as the culprit in explaining the difficulties in the UK, this is only a partial explanation. The “haphazard” approach to company law reform in the UK is an equally important contributing factor. Rather than adopting a conceptual approach like other jurisdictions, where existing concepts and structures may be replaced with new ideas, the UK approach has been to make technical amendments. The result is cumbersome and inefficient solutions which prove, more often than not, to be half measures; the problem addressed is not really solved and associated difficulties remain in place. (For a more detailed discussion of the different approaches to company law, see E Jacobs, “Conceptual Contrasts — Comparative Approaches to Company Law Reform” (1990) 11 The Company Lawyer 215). The Law Society has looked to several other jurisdictions for guidance in its efforts. Although there is “no one model procedure . . . there is a considerable amount of activity and development, underlining the need for a similar concentration of effort in the United Kingdom” (The Law Society (UK), supra at 21).
In looking for approaches and solutions to these difficulties, the Law Society Committee, in particular, endorsed the aims of the New Zealand Law Commission on Company Law Reform:

A good system of company law should:
- provide a simple and cheap method of incorporation and company organization which is flexible enough to meet the needs of diverse organisations
- clearly identify the duties and powers within the corporate structure in an Act designed for use by directors and shareholders and not just lawyers and accountants
- provide for better accessibility to company law by setting up the Act as the statement of first recourse in identifying rights and duties within the company
- ensure that regulation to prevent abuse is appropriate (that is to say, directed at the abuse of corporate structure or limited liability) and is commensurate with the risk of abuse so as not to frustrate the economic and social benefits of the company form (ibid at 4).

To this list might be added that a good system of company law should state the purposes for which incorporation might be sought and the advantages to be gained. Satisfactory solutions to the problems of UK companies law are not within easy reach. Although the Department of Trade and Industry has instituted a “rolling” programme of company law reform in response to the Law Society’s criticism, it may be many more years before there is the concentrated effort urged by the Law Society. In the domestic area, financial market reform and insolvency legislation, given the circumstances of the last decade, have absorbed all the legislative effort thrown at them. Company law reform has been reactive at best, ineffective at worst.

Recent Legislative History

The earlier history of companies legislation in the United Kingdom may be found in Part 6, where it is examined in relation to its influence on companies law in Hong Kong.

The Period 1948 to 1983

The Companies Act 1948 was the last real UK model for the Commonwealth world. Between 1948 and 1967, there was virtually no legislative activity in the United Kingdom in the area of companies law. The pace of legislative activity then picked up with no less than five Companies Acts enacted between 1967 and 1985 as well as the European Communities Act 1972.

The Companies Act 1948

For many years, the UK Companies Act 1948 could be called the great mother of companies law, serving as the model and inspiration for companies acts across the Commonwealth. The 1948 Act was primarily a consolidation of the Companies Act 1947 (which enacted many of the recommendations of the 1945 Cohen Committee Report) and the Companies Act 1929 (the previous major consolidation).

The outstanding feature of the 1948 reform was its emphasis on the public
accountability of the company. The valued privilege of balance sheet secrecy was made available only to so-called “exempt private companies”, while other private companies, in particular those in which shares were held by public companies, had to publish their balance sheets. Generally, recognised principles of accountancy were given statutory force and had to be applied in the preparation of the balance sheet and profit and loss account (Schedule 8 of the 1948 Act). Group accounts were required for inter-connected companies and, in principle, professional standing was demanded of the auditor, whose independence vis-a-vis the directors was strengthened.

Further, the 1948 Act extended the protection of minority shareholders (introducing the statutory oppression remedy of section 210) and widened the Board of Trade’s power to order an investigation of a company’s affairs. For the first time, the shareholders in general meeting were given power to remove a director before his or her term of office expired, although such removal might constitute a breach of the contract of service with the company or be contrary to the company’s articles.

It is a tribute to the Cohen Committee that their recommendations stood the test of time; the next major amendment to the Companies Act did not occur until 1967 (although the cynical may suggest political impotence as the underlying reason for legislative inaction). In the interim, imitation being the highest form of flattery, the 1948 Act was picked up, in some cases virtually word for word, in many Commonwealth jurisdictions.

The Companies Act 1967

The 1967 Act was the first stage in the implementation of the recommendations of the Jenkins Committee, which presented its report in 1962. The Committee took the view that, on the whole, the existing law worked well, and consequently few of its recommendations involved major changes in the law, except in relation to the disclosure of information by companies. The 1967 Act adopted, and in some respects considerably extended the recommendations of the Committee as to disclosure. The concept of the exempt private company, introduced by the 1948 Act, was eliminated. All limited companies were required to file full accounts, but certain companies were empowered to register as unlimited companies so as to avoid this requirement. Further information was required in the accounts, and the directors’ report became a document of prime importance. More stringent provisions were imposed in relation to directors’ interests in the company; such interests had to be disclosed as well as certain substantial shareholdings. The powers of the Department of Trade to investigate the affairs of a company were again extended.

European Communities Act 1972, section 9

When the UK joined the EEC, it had to give effect to the First Directive on Harmonisation of Company Law which had already been approved by the Council of Ministers on March 9, 1968. This was attempted by section 9 of the European
Communities Act 1972. The main change which this measure introduced into company law was that it restricted the *ultra vires* doctrine in favour of persons who contracted with the company in good faith. This was the first step taken in the long road of adapting UK companies law to the requirements of the European Union. Appendix I is a table of EC Directives which have been implemented by UK legislation with respect to company law.

*The Companies Act 1976*

The 1967 Act did not implement the greater part of the Jenkins Committee recommendations; it was somewhat less than a half measure. The 1976 Act attempted to remedy a variety of defects which had become evident in the application of the Acts of 1948 and 1967. The 1976 Act did not implement major changes to UK companies law; rather it was one more stage in the incremental process of adaptation and adjustment. It strengthened the requirements of public accountability and those relating to the disclosure of interests in the shares of the company. As regards the latter, it reduced the time limits and the amounts of notifiable transactions. Three notable innovations were introduced by the 1976 Act. First, it was made a criminal offence for a director of the company knowingly or recklessly to make a false statement to the auditor. Secondly, a company with shares admitted to listing on the Stock Exchange was given the right to compel the registered holders of its voting shares to disclose the beneficial interests in those shares (later, by the 1981 Act this power of the company was extended to all public companies). Thirdly, the court was given power to disqualify a person who was found to be persistently in default of the requirements of the Companies Acts from being connected with the management of a company. The disqualification provisions were also considerably extended by later legislation.

*The Companies Act 1980*

With the advent of the 1980s, the pressures from the European Commission intensified and the pace of legislative change in the area of companies law in the UK accelerated. The Companies Act 1980 was a major measure of company law reform and gave effect to the Second EEC Directive on Company Law Harmonisation in the United Kingdom.

The 1980 Act altered the structure of company law in the UK. Before this Act the public company was the residual form of the company and the private company was a variation of that form. The 1980 Act reversed this position. The private company became the residual form and a company was a public company only if it satisfied the specified requirements provided by the Act, the most important of which was a fixed minimum capital and shares paid up to at least one-quarter of certain accounts. Generally speaking, the 1980 Act tightened up the rules on capital by introducing controls on “stock watering” (the practice of issuing shares for inadequate non-cash consideration) and restricting the circumstances under which a dividend could be paid thereby overturning a number of common law authorities (section 39 of the 1980 Act).
Insider dealing was made a criminal offence. The shareholders were given a right of preemption in the case of new issues of shares in specified circumstances. In response to findings of malpractice revealed by a number of Department of Trade investigations in the 1970s, dealings between the directors and their companies became greatly restricted and financial maximum limits were introduced for such dealings. The directors became obliged, in the performance of their functions, to bear in mind the general interests of the employees of the company. Moreover, the common law rule in *Parke v Daily News Ltd* [1962] 2 All ER 929 (Ch D) prohibiting *ex gratia* payments to redundant employees was expressly abrogated. Admittedly this latter decision was only of symbolic importance, given the passing of the Redundancy Payments Act 1965. The protection of minority shareholders offered by section 210 of the 1948 act was extended by enabling them to petition the court for relief if their position was unfairly prejudiced. Throughout the 1980s this particular reform generated much litigation, with the result that the position of minority shareholders in the UK was greatly improved.

*The Companies Act 1981*

Hard on the heels of the Companies Act 1980, and for the same reasons (compliance with EEC Directives) came the Companies Act 1981. The 1981 Act gave effect in the United Kingdom to the provisions of the Fourth EEC Directive on Company Law Harmonisation and introduced other important changes. For the purpose of accounting and disclosure, companies were divided into small, medium-sized and “other” companies and their disclosure requirements were differentiated accordingly. The law relating to the names of the companies was simplified by the abolition, in principle, of the approval of the name by the Department of Trade. The register of business names was replaced by a more informal system, in order to save public funds.

Whereas the 1980 Act tightened up the law on company capital, this legislation relaxed controls. For example, a company was authorised, subject to certain conditions, to issue redeemable equity shares or to purchase its own shares. This undermined the old established prohibition against such practices laid down in *Trevor v Whitworth* (1887) 12 App Cas 409, a prohibition which had been codified by section 35 of the 1980 Act. An inconvenient decision of the courts relating to the operation of the share premium account was also abrogated.

The provisions relating to the disclosure of interests in shares and investigations into shareholdings and the affairs of the company were strengthened. The public company was accorded “a right to know” who the beneficial owners of its shares were. In order to enforce this entitlement, public companies were given the right to apply to the courts for a “freezing order” over disputed shares. The criminal liability of persons concerned in fraudulent trading was extended to cases in which the company was not in the course of winding up.
The Period 1985 to the Present

The companies legislation currently in force in the United Kingdom dates from 1985, when Parliament attempted a fresh start by consolidating the statutory provisions that were then operative into one major act, the Companies Act 1985, and three minor ones, the Company Securities (Insider Dealing) Act 1985, the Company Director Disqualification Act 1986 and the Companies Consolidation (Consequential Provisions) Act 1985. The Companies Act 1985, an enactment of 747 sections and 25 schedules, did not survive long intact; the Insolvency Act 1985 (almost entirely repealed and replaced by the Insolvency Act 1986) superseded nearly a third of it with sweeping new provisions. Further changes were made by the Financial Services Act 1986 and the Companies Act 1989. The Companies Act 1989 contains 216 sections and 24 schedules.

The Companies Act 1985

The Companies Act 1985 did not contain new law; its aim was to present existing law in a more accessible format. Whether it was successful in this aim is open to question but the failure to introduce reforms prior to consolidation has evoked a volley of criticism. No sooner was the 1985 Act enacted than it began to undergo continuous major and minor surgery.

The Recharacterisation of Company Law

Prior to 1986, the various UK Companies Acts contained provisions dealing with, *inter alia*, the insolvency of companies and the regulation of securities. However, it was thought that the companies legislation did not adequately deal with these areas, leaving gaping holes and regulating them in a manner which lacked fluidity and organisation.

1. Financial Services Act 1986

The Financial Services Act 1986 was designed to place the traditional arrangement of voluntary self-regulation of practitioners in financial services into a statutory framework. Recommendations to that effect were made by Professor Gower in Part I of his Report entitled *Review of Investor Protection* which was published in 1984. This Report was followed by a White Paper, *A New Framework for Investor Protection*, which was issued in 1985. The Financial Services Act 1986 sought to implement the proposals of this White Paper.

The Financial Services Act 1986 repealed and replaced the Prevention of Fraud (Investments) Act 1958 by a detailed and sophisticated system of regulation of those professionally engaged in investments services. It repealed and replaced other "prospectus provisions" of the Companies Act and amended a number of its other provisions, particularly in relation to take-overs. This led to a major, and desirable, reclassification of subject matter, distinguishing company law from securities
regulation (Gower's Principles of Modern Company Law, supra at 52). By enacting the Financial Services Act 1986, the UK joined other common law countries which have long recognised that securities regulation is distinct and separate from traditional company law concerns. The Act primarily deals with public issues and take-overs.

Prior to the implementation of the Financial Services Act 1986, there were many deregulatory developments in the City. However, deregulation led to a massive increase in conflicts of interest and conflicts of duty as well as an increased risk of abuse. These problems were exacerbated by the increasing number of individual first-time direct investors who came into the market as a result of the government’s privatisation measures and the widening range of investments marketed by banks and building societies (L C B Gower, “Big Bang and City Regulation” (1988) 51 Modern Law Review 1).

The Financial Services Act 1986 aims at regulating “investment” in the broadest sense. It is founded on two main principles. First, no person may carry on investment business in the UK unless he or she is either duly authorised or an exempted person. Authorisation is normally obtained by membership in a recognised self-regulatory organisation. Secondly, there is voluntary self-regulation within a framework of state supervision. The supervisory body is the Securities and Investment Board (SIB). The Act lays out a series of offences: for investment advertisements by unauthorised persons; for misleading statements made to induce someone to enter into an investment agreement; and for creating a misleading impression as to the market in, or price of, investments if done deliberately in order to induce someone to, among other things, make a disposition of an investment.

The regime under the Financial Services Act 1986 which deals with the methods of flotation of companies, was to regulate both listed securities (Part IV of the Financial Services Act 1986) and unlisted securities (Part V of the Financial Services Act 1986). However, Part V of the Financial Services Act 1986 dealing with unlisted securities never came into force; the prospectus regime as governed by the Companies Act still applies to these securities. The delay in implementation was originally due to the belated adoption of all the relevant EC Directives and the decision to conduct a thorough review of Part V of the Financial Services Act 1986. It has recently been decided to simply repeal Part V and proceed instead by way of regulation.

The Public Offers of Securities Regulations . . . implementing the EC Prospectus Directive . . . are about to be laid before Parliament . . . When the Regulations come into force (expected to be in early June), public offers of securities in the UK will be regulated by three sets of provisions, depending on their nature; the new Regulations, the Financial Services Act 1986 and the Listing Rules (H Creamer, “The Prospectus Directive — A New Regime for Public Offers” (May, 1995) PLC at 25).

The Regulations have now been implemented.

2. The Insolvency Act 1986

Prior to the enactment of distinct insolvency legislation, insolvency had been seen as a branch of company law, divorced from the bankruptcy law relating to individuals.
The Insolvency Act 1985, which implemented to a large extent the report of the 1982 Cork Committee (as revisited in 1984 by a Government White Paper), made major reforms to the law of both individual bankruptcy and the insolvency and winding up of companies. On the very day the Insolvency Act 1985 came into force it was replaced by the Insolvency Act 1986, a consolidating enactment which repealed and reenacted the Insolvency Act 1985 and the bankruptcy provisions of the Companies Act 1985 (other than those relating to the disqualification of directors and a few other provisions). While maintaining two distinct regimes, the Insolvency Act 1986 reduces the differences between the rules and procedures governing the bankruptcy of individuals from those applicable to the insolvency of companies. Essentially, one of the purposes of the Insolvency Act 1986 was to simplify and modernise the cumbersome, complex and archaic multiplicity of proceedings which existed prior to the Insolvency Act 1985, with a view to harmonising the law and practice relating to individual and corporate debtors.

If anything, the reforms were over-enthusiastic, at least according to Professor Gower. Too much was taken out of the Companies Act.

It is, perhaps, anomalous that members' voluntary winding up of solvent companies should be dealt with in the Insolvency Act; it might have been better if that had remained in the Companies Act (or, failing that, if the Insolvency Act had been entitled the Bankruptcy and Winding Up Act). But it is an advance to have recognised the essential unity of bankruptcy and insolvent liquidation . . . (Gower's Principles of Modern Company Law, supra at 52).

3. The Company Directors Disqualification Act 1986

Arising from reconsideration of the winding-up provisions of the Companies Act and the new insolvency regime, the Company Directors Disqualification Act 1986 consolidates all the provisions empowering the courts to disqualify "miscreants" from acting as directors or being concerned in the management of companies. Such provisions had previously been split between the Insolvency Act and Companies Act. This Act fully regulates who may act as a director, and applies to all persons directly or indirectly involved in the promotion, formation and management of a company, liquidators, administrators, and receivers. It applies to both solvent and insolvent companies.

The Companies Act 1989

It is an indication of the unsettled state of UK companies law that the 1985 consolidation was so quickly followed by yet another major revision in 1989. As with the other recent amendments, much of the Companies Act 1989 is dictated by the European Commission. And, as with Part V of the 1985 Act, Part IV of the 1989 Act, although enacted, will never see the light of day. The scope of the 1989 Act is not restricted to company law per se, nor to amending the Companies Act 1985. It contains a ragtag assortment of provisions: Part III reforms the procedural aspects of Department of Trade and Industry investigations; Part VI deals with competition law, a surprising component to find in a piece of companies legislation; Part VII with a situation of
insolvency in the financial markets to which the general law of insolvency no longer applies; Part VIII amends the Financial Services Act 1986 (restricting the right to bring an action for breach of the Act to "private investors"); Part IX authorises the Secretary of State to abandon the age-old system of requiring a written instrument to record evidence of title to or transfer of a security (in anticipation of the now abandoned TAURUS paperless transfer system). If this were not a diverse enough patchwork, a few afterthoughts are lumped together in Part X and the Schedules.

What may have been the most significant part of the 1989 Act, Part IV, a major revision of companies charges, will also never see the light of day. The Part was never implemented, unforeseen complications having arisen, and early in 1995 the Department of Trade and Industry announced that it was once again revisiting the entire subject. It is easy from a distance to point to the flaw in the conception of Part IV. The continued characterisation of an area of law such as security interests (which has taken on a life and commercial significance of its own) as "company law" seems doomed from the start.

As to companies law reform per se, Parts I and II of the 1989 Act deal with accounts and audits and Part V pertains to various other matters. Part I of the 1989 Act inserts a new Part VII into the 1985 legislation and remodels the law on company accounts. Amongst the more notable changes here are the right of public companies to submit summary financial statements to their shareholders rather than full accounts and the new rules on consolidated accounts which now encompass "subsidiary undertakings" (a considerable widening of the former concept of a "subsidiary"). Part II modifies the law on company audits and auditor qualifications. A Financial Reporting Council is established to introduce and police new accounting standards.

Part V is in effect the first tranche of innominate reforms. An attempt was made to cast off two old chestnuts of UK company law, the ultra vires rule and the prohibition on an action for damages by members. It seems that the ultra vires doctrine will not die; the provisions introduced (including those on the related constructive notice doctrine) have been roundly criticised as inadequate to achieve their ends (see, eg, ibid at 175 seq). Also of practical importance are the changes which herald the introduction of an "elective regime" for private companies by permitting them to opt out of some of the more formal requirements of the Companies Act. As far as public companies are concerned, the reduction of the share interests disclosure threshold to three per cent (to be notified now within two days) should facilitate defence operations by target companies.

Recent Trends in UK Companies Law

There is no doubt that a precipitating factor in the high level of legislative activity in the UK has been the necessity of compliance with numerous European Commission Directives in company law and related areas (see Appendix I). This has resulted in the predictable collision of two very different legal traditions; the English common law and the code-based European civil law.
The difficulties of integration of European Commission Directives go beyond simple translation of certain civil law concepts into the common law and reconciliation of differing substantive provisions. A major stumbling block has been the traditional dominance of the German corporate model at the level of the European Commission. Germany has been quite aggressive in promoting its corporate law as the model for all Europe. This includes a concept of co-determination or worker participation in corporate management which is very much at odds with the UK tradition. The opposition in the United Kingdom to the German model has been as much on political grounds as on incompatibility with the integrity of the UK legal regime governing companies.

The pressure which the necessity for compliance with European Commission Directives has put on the UK companies law regime has manifested itself in other ways as well. It may be ultimately responsible for the “unbundling” of UK companies law which occurred in the 1980s as well as the heightened tension in the UK between statutory and non-statutory norms.

Despite the “lack of overall strategy for company law” in the UK (which the Law Society has identified), the imposition of European Commission Directives to a certain extent did prompt reclassification of some areas of UK companies law. The legal regimes upon which the European Commission Directives are largely drawn are much more conceptually rigorous in their structure than the UK Companies Act which, for decades, has served as a compendium of commercial law.

The enactment of the Insolvency Act 1986 and the Financial Services Act 1986 left “gaping holes” in the Companies Act, as matters formerly dealt with in the Companies Act were taken over by the new legislation.

It has, however, also led to a major, and desirable, reclassification of subject-matter, distinguishing Company Law from Insolvency Law and from Securities Regulation . . . it is an advance to have recognised the essential unity of bankruptcy and insolvent liquidation and, accordingly, that Company Law should concentrate on the life, rather than the death and interment of companies . . . Even more important are the implications of the Financial Services Act. Many other common law countries have long recognised that what most of them call Securities Regulation is a distinct and important subject . . . We, however, had treated it, in so far as we recognised it at all, as an unimportant adjunct to Company Law. That has changed . . . (Gower’s Principles of Modern Company Law; supra at 52–53).

With the spinning out of insolvency and securities from the Companies Act, consideration was also given to creation of a North American-style personal property security regime as recommended in the Diamond Report on Charges. This stand alone regime would have replaced Part IV of the Companies Act 1985. This initiative has stalled and the UK Government has announced that Professor Diamond’s recommendations will not be taken up.

A second major indirect effect of the imposition of European Commission Directives on UK company law may very well be the heightened tension between statutory and non-statutory norms in the United Kingdom. The continental European legal model is very much one of “written law”, “le droit écrit”. Legal norms find their
expression in comprehensive codifications (for which the European countries are justly famous) and individual statutory pronouncements.

This has not traditionally been the English way. Even the Companies Act 1985 is only a consolidation (as opposed to a codification) and, even at that, only of the “greater part of the Companies Acts”. The Act is supplemented by later statutes such as the Companies Act 1989. Company law also continues in large measure to rely on common law principles as they have been developed by the judiciary. Finally, non-statutory “rules” continue to play an important role in company law; for example, the Take-over Code which assumes voluntary compliance; stock exchange listing rules which now have a “quasi-statutory” nature under a delegation of authority from the Treasury; and “guidelines”, such as those proposed by the Cadbury Report, which remain discretionary. The area of directors’ duties is a prime example of the complex interplay of these various statutory and non-statutory elements. This complexity is increasingly hard to justify and very much at odds with the continental European approach of codification and “written law”. Even in other common law countries, especially Canada and the United States, statutory norms predominate in the area of corporate and securities law.

As to the future direction of UK companies law, Gower is not optimistic:

It seems inevitable that developments in our Company Law over the next 25 years will follow much the same pattern as that of the past twenty five. Reforms will be piecemeal without any review of the basic structure and with a marked reluctance to tackle fundamental problems except to the extent forced upon us by the EC. The latter’s initiatives will result in major changes and if these are to be to our liking it behoves us to play a more constructive role in the preparatory stages of Community legislation than we generally have in the past. Domestically inspired changes to our companies’ and related legislation are likely to be restricted mainly to technical matters, to the removal of flaws which have come to light in the legislation of 1985–86, and to the closing of loop-holes revealed by scandals as yet unforeseen. Our company legislation will continue to increase in length and, since changes in our style of legislative drafting are most unlikely, will become still more complex and opaque. But cheer up: all this should provide grist to the mills of company lawyers (ibid at 78).
Part 3

The Commonwealth
Part 3

The Commonwealth

Australia

Introduction

The Australian Corporations Law is a huge, complex statute, running, literally, into thousands of sections. For constitutional and political reasons, Australia being a federal state, the Corporations Law fits and operates within a very complex legislative framework of state and federal law. According to the Chief Justice of Australia, “Oscar Wilde, the supreme stylist, would have regarded our modern Corporations Law not only as uneatable but also as indigestible and incomprehensible” (A Mason, “Corporate Law: The Challenge of Complexity” (1992) 2 Australian Journal of Corporate Law 1). The complexity has spawned its own legal literature speculating on its sources (I Ramsay, “Corporate Law in the Age of Statutes” (1992) 14 Sydney Law Review 474).

The past twenty years have been ones of ferment and intense legislative activity in corporations law in Australia, and times are still unsettled. Complexity in corporate law statutes, however, may have reached its limits in Australia. A major initiative, the Corporations Law Simplification Program, was announced in October 1993 and has been rapidly producing proposals and draft legislation.

There are several factors, which, working together, have resulted in the legislative situation in Australia being more complex than even in the UK. The first factor has been the use of UK companies legislation itself as the basic model for Australian corporations law. As in many other Commonwealth jurisdictions, the UK Companies Act 1862 and the 19th century UK legislation that followed were very influential in the development of Australian companies law and their outlines are still apparent.

Most of the colonies passed legislation modelled on the English Companies Act 1862 and this formed the basic legislation for a long time. Later amendments in England that were prompted by review committees inspired similar amendments in Australian jurisdictions. There was a large measure of uniformity, if only because the various local legislatures simply adopted what had been passed in England (H A J Ford, R P Austin and I M Ramsay, Ford’s Principles of Corporations Law, 8th ed (Sydney: Butterworths, 1997) at 45).

Over time, variations appeared in response to local circumstances, but the continued use of the UK model has left Australian company law with many of the same difficulties as the UK legislation (see Part 2, above).

As local divergences began to appear, so did other changes in the legislation arising “from the emergence of new ways of fund-raising and dealing in securities” (ibid at 45). In a federal country where companies law was governed at a state level, the pressures for uniformity at a national level in the development and regulation of capital markets
resulted in efforts to “federalise” companies law in the 1960s and 1970s. In developing a securities regulatory regime within a companies law framework, Australia ran into nearly insuperable constitutional difficulties, of a kind which do not exist in a unitary state such as the United Kingdom. The brief legislative history below outlines the struggle which ensued and which now, happily, seems to have reached a point of resolution.

Australia has also, befitting its stature as a mature member of the Commonwealth, been highly attuned to legislative developments both in the United Kingdom and elsewhere, especially to developments with respect to capital markets. The Corporations Law is sprinkled liberally with alphanumeric amendments dealing with such matters as electronic clearing of securities, netting, continuous disclosure, insider trading, repurchase agreements, and so on. Such responsiveness to modern developments comes at a cost, however, as it adds to the already impressive bulk of the Corporations Law.

A further complicating factor (in addition to the constitutional complexity and perhaps arising directly out of the “federalisation” exercise) is the monolithic nature of the Corporations Law. It is an omnibus statute, and despite its “corporations” title (which might suggest a more focused North American approach), it retains the pre-1986 UK company law structure, combining charges, securities regulation, insolvency and corporate law in the same legislation. There is certainly a “convenience” argument in favour of this approach. In writing on “dismembering” the Australian Corporations Law, Dean Simmonds comments:

... one may legitimately ask, then why go to the trouble of breaking up the Corporations Law in the first place? The distinctions I am calling for, after all, correspond to Chapters or Parts in the statute which can be kept distinct. Modern lawyers should be used to thinking in functional terms, and do not need separate statutes to ensure that they make sensible distinctions.

Further, there is no denying the significance of securities regulation and personal property security law to corporations. It might be argued that having the law on these topics, at least so far as it concerns corporations, together in one statute with “core” corporations law, would safeguard us against losing sight of how that “core” law is often misleading when read without account for the wider context (R Simmonds, “Dismembering the Corporations Law and Other Law Reform: Should Something More be Added to the Law Reform Agenda?” (1995) 13 Company and Securities Law Journal 57 at 61).

But, quite apart from the fact that this monolithic approach results in a statute that weighs over 2.3 kilograms (in the Butterworths 1996 softcover edition), there are persuasive arguments militating in favour of separate statutory treatment of these different areas of commercial law:

I would respond that categories guide thought, and that we should use the best categories to hand. Company law is too wide a category to cover the three fields here. The Corporations Law and recent reform directions in Australia contain, in my view, evidence of the trouble to which sub-optimal categories can lead... By covering securities regulation and personal property security law along with the internal ordering of the corporation, we are making it unnecessarily hard for ourselves to keep the various policy strands of those areas apart. If we want better law in each of these areas, we need to have them in different statutes, if not under different regulatory arrangements (ibid at 61, 63).
Despite these obvious difficulties, there are valuable lessons to be learned from Australian company law, in the largest sense, and from the rethinking which is proceeding there apace. Certainly, from an administrative point of view, the functioning of the Australian Securities Commission, which has oversight of the Corporations Law, and the high degree of computerisation of administration of the legislation may be instructive. One caveat, though, is that the Australian Securities Commission has wide-ranging regulatory powers and an interventionist role, in part modelled on the United States Securities and Exchange Commission, an expensive undertaking. The current process of simplification of the legislation is also of considerable interest as it promises to make a break with the Australian tradition of legislative complexity.

**Legislative History**

**Period prior to the draft Companies Bill 1961**

In Australia, prior to the adoption by the various colonies of the UK Joint Stock Companies Act 1844, private companies generally operated as unincorporated deed-of-settlement joint-stock companies. Public utility companies were either incorporated by Royal Charter, or were conferred with powers to sue and be sued in the name of an officer by private act. Most of the colonies passed legislation based on the British Companies Act 1862, which was subsequently modified over the years (H A J Ford, R P Austin and J M Ramsay, *Ford’s Principles of Corporations Law*, 8th ed (Sydney: Butterworths, 1997) at 45).

The state of Victoria seems to have been a hotbed of innovative company legislation during the late 19th century. The “no liability” mining company was developed in 1871, while compulsory auditing and financial information provisions were enacted as early as 1896. However, these provisions applied only to publicly traded companies; private companies, to which the new requirements did not apply, were defined as proprietary companies, which are still a viable form of business organisation today (*ibid*).

The no liability company was developed in the speculative area of mining investment. It was first provided for in the Mining Companies Act 1871. At the time, mining concerns, which formed companies limited by shares, sometimes found it difficult to recover unpaid calls of share capital. Shareholders often bought their stakes under fictitious names and would simply abandon their holdings if the venture proved less than fruitful. The noteworthy aspect of the no liability company is that a member who does not pay calls as made forfeits his shares. Although the memorandum of association of a no liability company had to state that acceptance of shares did not constitute a contract to pay calls or contribute towards the payment of the company’s debts, a no liability company could nevertheless contract around this. The no liability form was briefly made available to all companies in the Companies Act 1896 (Vic), but as companies in other areas of business failed to adopt it, it was once more confined to mining companies by further legislation in 1910 (*Ford’s Principles of Corporations Law*, 7th ed, 1995 at 136–137).
The proprietary company is one area where the State of Victoria actually acted before the United Kingdom. The United Kingdom did not specifically legislate for private companies until the Companies Act 1907, eleven years after the Victorian Companies Act 1896. Essentially, a proprietary company is a small private company. This form of business organisation is intended for a small number of investors (from a minimum of one to a maximum of fifty not counting employee members) who do not intend to offer shares to or borrow from the public, and who want the company to be able to restrict share transfers. This form was adopted by most other Australian jurisdictions, and now most Australian companies are proprietary companies. No liability companies may not be proprietary companies.

The proprietary company offered several advantages over a public company which made it more attractive to certain investors: membership at incorporation had to be at least two as compared to five for a public company, the minimum number of directors was two as opposed to three, there was no obligation to hold statutory meetings or make statutory reports, there were fewer limitations on the qualification and appointment of directors, lower quorum, and the like. Finally, it could be converted into a public company by lodging a special resolution with the Australian Securities Commission (ASC) and amending its memorandum.

As interstate commerce grew, the need for uniformity of companies legislation began to make itself felt. Unfortunately, Australia’s constitutional division of powers precluded the Commonwealth from acting decisively in this field. As will become apparent below, the resulting need to coordinate legislative activity and delegate powers in order to achieve national legislative uniformity has been the single dominant theme in the recent development of Australian company law.

Victoria’s Companies Act 1958 was the model for the 1961 draft Companies Bill. The draft Bill was an attempt to provide a pan-Australian model for state legislation, as the growing divergence between the states’ companies legislation had begun to pose a problem for companies operating on a national scale. Between 1961 and 1962, each of the states passed Companies Acts based on the draft Bill. The Malaysian Companies Act 1965 and Singapore’s Companies Act 1967 were also based on the draft Bill. As well, non-uniform but similar Marketable Securities Acts were enacted in the states and territories between 1966–71 (ibid at 45–46).

*Period following the Draft Companies Bill 1961*

The failure of several heavily indebted companies in the early 1960s provided the impetus for the enactment of the Companies (Public Borrowings) Act 1963. In 1967 the Eggleston Committee was formed to study the quality of shareholder protection provided by the uniform Companies Act. Over 1971 and 1972, following the committee’s recommendations, legislation on accounts and auditing, disclosure of takeovers and large shareholdings, insider trading, and special investigations was enacted, although New South Wales’ insider trading provisions differed from those in the other states (H A J Ford, R P Austin and I M Ramsay, *Ford’s Principles of Corporations Law*, 8th ed (Sydney: Butterworths, 1997) at 46–47.)
In the late 1960s, a mining boom and associated allegations of improper trading practices led to the formation of the Senate Select Committee on Securities and Exchanges in 1970. Its final report was published in 1974. However, on the State level, in response to the same problem, New South Wales, Victoria, Queensland, and Western Australia enacted Securities Industry Acts, inspired in large part by the British Prevention of Fraud (Investments) Act. As well, the Labour Party had come to power at the Commonwealth level and before the Select Committee had presented its report, it had already prepared the Corporations and Securities Industry Bill. This new bill was inspired in part by US securities legislation, the British Companies Bill 1973, and the Eggleston and Select Committees. It was primarily concerned with securities-related aspects of company law; other aspects, such as formation, winding up, and management of companies under Commonwealth legislative authority were to be dealt with by the National Companies Bill. However, Labour lost office in 1975, before any of these bills could be passed (ibid at 47–48).

The First Cooperative Scheme

During the same period, the Labour governments of New South Wales, Victoria and Queensland formed the Interstate Corporate Affairs Commission (ICAC), which was to handle the companies and securities administration for the three States. Following the election of a Labour government in Western Australia, that State brought itself under the aegis of the ICAC as well (ibid).

Following this initiative, the coalition of Liberal and National members that replaced the outgoing Commonwealth Labour government proposed an Australia-wide cooperative scheme. Under this scheme, the Commonwealth would enact model companies and securities legislation in its jurisdiction, and the States would then pass legislation enacting it as law within their jurisdictions. The Commonwealth and the States entered into a formal agreement on the proposed cooperative scheme on December 22, 1978.

The scheme aimed to establish uniform companies and securities legislation at the State and Commonwealth level. Authorities under the purview of the National Companies and Securities Commission (NCSC) were to be responsible for the uniform administration of this legislation. The NCSC was to be supervised by a Ministerial Council made up of federal and state ministers. The Ministerial Council was also responsible for law review and the requesting of amendments where necessary. It was to be assisted in the task of review by the Companies and Securities Law Review Committee, which was responsible for research and reporting on regulation when requested to do so by the Council.

Following the formal agreement of 1978, the Commonwealth Parliament passed the following Acts:
- The National Companies and Securities Commission Act 1979
- The Companies (Acquisition of Shares) Act 1980
• The Securities Industry Act 1980
• The Companies and Securities (Interpretation and Miscellaneous Provisions) Act 1980
• The Companies Act 1981
• The Futures Industry Act 1986

The States and the Northern Territory passed legislation which applied the scheme Acts "to the exclusion of" existing State Legislation (the scheme Acts applying, of course, directly to the Australian Capital Territory). Amendment was to be driven by the Ministerial Council, which could request the Commonwealth Parliament to amend the law. Amendments, once they passed both Commonwealth-level Houses, would automatically be adopted by the States. Failing this, the States could adopt the proposed amendments. Neither State nor Commonwealth could unilaterally amend the laws.

From the date of the Northern Territory's entry into the scheme in 1986, largely uniform law was in force throughout Australia. The NCSC handled policy, while delegating to the state-level authorities most of the routine administrative work (the unusually high degree of intergovernmental cooperation caused some initial problems). However, its wide-ranging discretionary power, notably in the area of takeovers, earned it some criticism. As well, the scheme itself had certain flaws. Due to the state-level administration of the Scheme Acts, inconsistencies and some duplication arose in the regulation of companies with nation-wide activities. As well, the administrative bodies lacked sufficient resources to properly execute their investigative and prosecutorial functions. Thus, although an improvement over the situation which preceded it, the cooperative scheme of the 1980s was still somewhat flawed (ibid at 48–49).

**The National Scheme**

Labour regained power on the Commonwealth level in 1983, and began acting towards the Commonwealth's taking over altogether the field of companies legislation. In 1988 a series of measures designed to operate without state legislation or cooperation was put before the Commonwealth Parliament. The main component was the Corporations Bill, which was to replace the Companies (Acquisition of Shares) Act 1980, the Companies Act 1981, and the Securities Industry Act 1980. In addition, the Australian Securities Commission Bill replaced the NCSC with the ASC. This was the largest legislative package since Federation, and was described as "a single truly national regulatory regime that can guarantee a sound and well-regulated environment for corporate activity" (*Australian Corporations Law* (Sydney: Butterworths 1994) at 1/94).

It had been clear from the beginning that the States would challenge these measures on constitutional grounds, and in the test case, in *NSW v Commonwealth* (1990) 169 CLR 482, the High Court found that the national scheme exceeded the Commonwealth Parliament's legislative authority.

Following this decision, on June 29, 1990, the Commonwealth and the States
reached the Alice Springs Agreement. Under this agreement, uniform legislation based largely on the Labour government's unconstitutional proposed package was to be enacted by the Commonwealth for the Australian Capital Territory, amended so as to allow the States and the Northern Territory to adopt it. From the constitutional point of view the scheme is quite interesting being extremely interconnected and interreferential. Each law is dependent upon the others for either substance or applicability (see R P Austin, "An Introduction to the Corporations Law" (1991) 12 Australian Corporation Law Bulletin 141 at 144–154). Details of it are outlined in Appendix II. The new federal, rather than national, scheme was designed to provide a single national corporate affairs authority in the form of the ASC but simple, it is not.

In order to put the Alice Springs Agreement into effect the Commonwealth passed a series of statutes which attempted to: (1) "federalise" company, securities and futures laws; (2) nationalise the administration and enforcement of these laws; (3) create a structure of civil liability; and (4) in keeping with the times, deregulate the industry.

The new "National Scheme" became operational January 1, 1991. "Corporations Law" is a misnomer. To a large degree, the statute is old-fashioned UK-style companies law (and not North American-style corporations law, the distinction between the two being discussed in Part 4 below) to which has been added a comprehensive and highly detailed securities law regime which has very little in common with traditional companies law. The Corporations Law, for example, regulates the securities exchanges and their members, the futures exchanges, clearing houses, securities dealers, and investment advisers.

Barely was the ink dry on the Corporations Law in 1991 than the first Corporate Law Reform Act 1992 was enacted. Among other things, it included an amended statutory duty of care for directors, regulated financial transactions involving public companies and their related parties, and substantially revised the insolvent winding up provisions.

Shortly after this, the current major initiative in corporate law in Australia, the Attorney General's Corporations Law Simplification Task Force, was announced to review the entirety of the Corporations Law. This, at least originally, was seen as an exercise in form over substance. Dean Simmonds has described it as reform "that seeks to make the law more intelligible to its intended audience by recasting it in what is perceived to be better language. The focus is not the content of the law — so important to modernisation — but rather the way that the content is conveyed" (Simmonds, supra at 58).

**General Trends and Developments**

There is no doubt that the ambitious Corporations Law Simplification Program in Australia is the current focus of all corporate law developments there. The complexity of the Australian Corporations Law had reached the limits of tolerance. The Simplification Program appears to be a response to a failed initiative, the Close Corporations Act 1989, and the unacceptable level of legislative complexity in the Corporations Law.
The Close Corporations Act 1989 was enacted but never proclaimed, in part because it shared the same constitutional infirmities of the Corporations Act 1989 which had succumbed to a challenge in the courts. The Close Corporations Act 1989 had its origins in a Companies and Securities Law Review Committee initiative "to recommend a simpler and cheaper form of corporate structure for entrepreneurs, with due regard to their particular needs and without burdening them with statutory requirements which are not significant under the circumstances" (Australia, Companies and Securities Law Reform Commission, Report to the Ministerial Council on Forms of Legal Organisation for Small Business Enterprises (September 1985) at 3).

In structure, the entity proposed demonstrated many similarities with the South African close corporation: a minimum of one and a maximum of ten members; only natural persons as members; no directors; inability of such corporations to act as a trustee or a holding company. The Parliamentary Committee subsequently charged with reviewing the Close Corporations Act 1989 agreed with the "widely held view that the Corporations Law is complex and that, as a result, small businesses run the risk of inadvertent non-compliance with its many requirements. The Committee also doubts the utility of the filing requirements which small companies must observe. The returns are rarely referred to and are of dubious value to creditors or others interested in the company" (Australia, Joint Statutory Committee on Corporations and Securities, Close Corporations Act 1989 (December 1992) at 13).

In addition to the constitutional difficulties, the Close Corporations Act also foundered on the shoals of its own inventiveness. Australia was not quite ready for one person corporations and the elimination of such traditional corporate structures as the board of directors. The successful South African experience apparently did not entirely allay the apprehensions surrounding these innovations. But in recommending "the introduction of a new corporate form, the private company, within the existing Corporations Law [which] would adopt the best features of the proposed close corporation while eliminating those that were the subject of extensive criticism" (ibid at xii), the Committee shifted the focus of simplification efforts to the Corporations Law as a whole.

The Corporations Law Simplification Task Force attempts to practice what it preaches. In its initial publication, the December 1993, Plan of Action, the Task Force outlined its objectives in remarkably simple and concise language: simplification of content, clarification of drafting and comprehensive consultation (Australia, Corporations Law Simplification Task Force, Plan of Action (December 1993)). With respect to simplification:

Action to simplify the content will concentrate on those sections of the law where policies:
- are unclear or uncertain or no longer relevant
- do not cater for the needs of small business
- place undue regulatory burdens on business
- thwart the efficient operation of the law
- do not achieve their objectives on technical grounds

The objective is to streamline the law, procure consistency and coherence, strip away unnecessary complexities, maintain effective protection for investors, and bring significant cost benefits
both to business in complying with the law and to relevant authorities in administering it (ibid).

The "central objective" of the Simplification Program, according to the Task Force, is "a law capable of being understood by its users" (ibid).

The legacy of Canada's Dickerson Report (R W V Dickerson, J L Howard and L Getz, Proposals for a New Business Corporations Law for Canada (Ottawa: Information Canada, 1971)), as filtered through the recent New Zealand companies law reform, shines through these objectives, even to the consideration of the "restructuring of the core company law Chapters" of the Corporations Law. In Stage 2 of the program, the "general emphasis for the Task Force will be to complete the core company law provisions in Chapters 2, 3 and 4 of the Corporations Law. The Task Force will then turn to the Chapters in the Corporations Law which deal with the securities and futures markets" (Australia, Corporations Law Simplification Task Force, Plan of Action — Stage 2 (August 1994)).

Legislation has appeared remarkably quickly. The "First Corporate Law Simplification Bill 1994" was introduced December 8, 1994 and passed October 17, 1995. "[T]he Bill prepared by the Task Force will streamline the law, achieve greater consistency and remove unnecessary complexities" (First Corporate Law Simplification Bill, Exposure Draft (July 1994) at 2). The first thing the Bill does is repeal the Close Corporations Act 1989.

What else does it do? It addresses a variety of securities and corporate law issues: it simplifies the share buyback provisions for public companies; adopts in modified form some of the provisions of the Close Corporations Act 1989 (for example, it recognises two kinds of proprietary corporations, small and large; it permits single director/single member corporations although not adopting the boardless close corporation concept); it reduces the financial reporting obligations for smaller companies; it strengthens the accountability of larger companies; it abolishes five of the registers now kept by companies and eliminates duplication with information available through the ASC; it introduces a small business guide which summarises in one place all the rules most important for smaller companies.

The Second Corporate Law Simplification Bill was released for comment June 29, 1995 and according to the Attorney-General for Australia, "represents the most comprehensive rewrite of the underlying principles of company law since the UK Companies Act was first adopted in Australia in the 1860s... The Second Bill will cover a much wider area than the first. It will include the provisions on forming a company, share capital, accounts and audit, company meetings, company names, annual returns and defunct companies. Once this Bill is passed most of the core company law areas which impact particularly on small business will have been simplified" (Attorney General for Australia, News Release 64/95, (29 June 1995)). Despite the cloak of "simplification" and changes in form not substance, Australian law is undergoing, as the Attorney-General correctly points out, a "comprehensive rewrite of the underlying principles".
In brief, among other changes, the Second Bill proposes the following:

1. Registration and basic features of a company:
   - single stage incorporation process
   - rules governing internal affairs will be in the statute and articles (i.e. a constitution) will be optional
   - no liability companies and companies limited both by shares and by guarantee will no longer be available as a form of incorporation
   - a common seal will no longer be obligatory
2. Meetings
   - members holding at least 5% of the votes will be entitled to call a general meeting
   - meetings by use of electronic communication devices will be facilitated
3. Share Capital
   - shares will no longer have a par value
   - capital reductions will no longer require court confirmation and must be fair and reasonable to all shareholders
   - financial assistance must not result in a material deterioration of the company’s financial position (without shareholder approval)
4. Accounts and audit
   - accounting rules will be matters for accounting standards
   - improvements in quality of directors’ reports to members
5. Annual Returns
   - over half the items in annual returns will be deleted
   - electronic filing will be facilitated

A quick glance at the outline of the Second Bill leaves little doubt as to a major source of its inspiration: recent changes to companies law in New Zealand which in turn were based on changes recommended 25 years ago in Canada.

The Simplification Program has been proceeding very rapidly in Australia, which may indicate both the intensity of the crisis in Australian corporate law and also a considerable amount of political will. The worry, expressed by some commentators is that despite the best of intentions, the confusion of some conceptual issues may be counterproductive to the program (for example, see Simmonds, supra).

It may also be easier to apply a “plain English” approach to the more prosaic issues of holding a general meeting of shareholders than to more exotic issues of company share buybacks. The characterisation of technical securities law issues as corporate law has tested the mettle of the finest “plain English” experts. In any event, a very current and informative process is underway in Australia.

Canada

Introduction

Like the United States and Australia, Canada is a federal state with a multiplicity of corporate statutes. Unlike the United States, there is a federal corporations statute, the Canada Business Corporations Act (CBCA), as well as corporate legislation in each of the 10 provinces. Upon implementation of the CBCA in 1975, a deliberate and fairly
successful effort was made to harmonise the provincial statutes to the new federal regime in Canada. Nova Scotia and British Columbia resisted the change to the federal model, but over time both have incorporated many features of the CBCA, with British Columbia, in particular, evolving into an “anomalous hybrid” (B Welling, Corporate Law in Canada, 2d ed (Toronto: Butterworths, 1991) at 39).

Again unlike the United States, there is no federal securities regulator in Canada. Although Canada has adopted securities regimes which are very much American in concept and approach (and, with the advancing state of economic integration in North America, daily becoming more so), each province has its own securities law regime. Sporadically, there are calls for a national or federal securities regulator in Canada, but to date informal efforts at coordination and harmonisation have proved adequate to regulate Canada’s capital markets.

Over the last twenty years, regional variations have crept back into the harmonised provincial corporate statutes but overall they remain remarkably similar to the CBCA in general structure and detail. Some provincial legislatures have been more responsive to change than others and have renewed their corporate statutes with greater regularity than the federal government. This has resulted in some divergence in detail.

One of the driving forces behind a reassessment of corporate law in Canada has been the aggressiveness with which securities regulators have appropriated to themselves issues more traditionally characterised as corporate law. Ontario, Canada’s lead commercial jurisdiction, has attempted to consolidate its position as Canada’s business centre by coordinating the development of its securities laws and its corporate statute, the Ontario Business Corporations Act (OBCA). Ontario has produced a slick and efficient corporations regime. “Indeed, in Ontario’s case, the province prides itself on the fact that a certificate of incorporation can be issued in 20 minutes!” (J Ziegel, “The CBCA — Twenty Years Later: Where Do We Go From Here?” in Corporations at the Crossroads (Paper presented at the Meredith Lectures, McGill University, Montreal, Canada, 1995) [unpublished] at 6 [hereinafter Zeigel-Meredith Lectures]). Developments in Ontario are now exerting an influence on the federal CBCA. For purposes of this discussion, however, the CBCA will be the focus.

When the CBCA was implemented, it was considered to be revolutionary in many respects.

The Canadian approach has abandoned old concepts and substituted new ones specifically designed for their purpose . . . First the Canadian approach results in short, straightforward provisions that lead directly to the heart of the matter . . . It is not just a question of legislative style. It is a question of the approach to reform. The Canadian approach is a truly reforming one. The old law is cut away and new law grafted in . . . In Canada the root of the problem in the underlying concepts has been recognised and a solution supplied on the conceptual level (Jacobs, “Conceptual Contrasts — Comparative Approaches to Company Law” (1990) II Company Lawyer 215 at 219).

The CBCA has aged well; it still appears remarkably fresh after twenty years and has required very little “maintenance” by way of statutory amendment.

When the 20th century history of Canadian corporations law comes to be written, the drafting and enactment of the Canada Business Corporations Act in 1975 will surely be hailed as a
major achievement. Federal corporations law in the preceding hundred years had been quite undistinguished. It was almost entirely derivative with no clear underlying philosophy, stodgily drafted, and haphazardly patched up periodically when someone persuaded the government of the day that something needed to be done. It was also badly dated in most respects by the time the Trudeau government commissioned the three wise men — Robert Dickerson, Leon Getz and John Howard — to draft a new statute from scratch.

The CBCA had all of the virtues its predecessors lacked. The drafters had a clear conception of what they wanted the new Act to look like and they pursued a series of well-defined and clearly articulated goals. They endorsed a strong dose of enablingism with respect to incorporation procedures and dispensed with formalism where it served no useful purpose. They embraced a principled scheme of corporate governance and combined it with a strong affirmation of non-excludable obligations to which officers and directors were subject. They were conscious of the vulnerability of minority shareholders and sprinkled the Act liberally with substantive and remedial safeguards for their protection. No less important, the Act was drafted in commendably clear language and crisp sentences. The exposure draft was accompanied by a commentary volume clearly explaining the drafters’ goals and what the various provisions were designed to accomplish (Zeigel-Meredith Lectures, supra at 1).

The CBCA, and the Dickerson Report which preceded it, continue to influence reforms in jurisdictions as diverse as South Africa, Singapore, Australia and New Zealand where concepts introduced by the CBCA and time-tested in Canada are now making their appearance.

The CBCA has been complemented over the last twenty years by a broad range of judicial decisions. According to John Howard, one of the original members of the Dickerson Committee:

Although frequently surprised, I have never been disappointed by judicial interpretation and application of the CBCA. Indeed, I consider the recent decision of Mr Justice Farley in Wittlin, an oppression case, to be judicial law making at its best. Instead of taking on the almost impossible task of determining fair value, the court compelled the parties to resolve their conflict under a modified “shotgun” procedure, applying a process solution that is apparently fair, clearly effective and, above all, practical. It reflects the best intentions of the creators of the CBCA (J Howard, “Opening Remarks” in Corporations at the Crossroads (Address at the Meredith Lectures, McGill University, Montreal, Canada, 1995) [unpublished]).

Historical Background

Given its traditionally strong British accent, it is useful briefly to trace the course which Canadian corporate law has taken in arriving at the point where it now provides a model for much of the Commonwealth world. The first half of the 19th century in Canada was “a period of wide experimentation with the corporate form” (Welling, supra at 45).

Canada’s first general Act of incorporation came in 1850. It covered “any kind of Manufacturing, Ship Building, Mining, Mechanical or Chemical Business”. This statute was an early example of the Canadian legislative tendency to learn from American experience in business matters. General incorporation Acts had spread through the United States since 1811, following the lead of New York, where incorporation was obtained by filing with a public official a charter prepared, within legislated limits, to the organizer’s own specifications. This easy method of
incorporation was copied by Canada, in preference to the complex procedures under the English Joint Stock Companies Act of 1844 (ibid at 46).

After this brief flirtation with American concepts, Canada returned to British sources for its companies legislation, but curiously, to an older form of incorporation than that just adopted in the United Kingdom. The predominate form of incorporation in Canada for over one hundred years was to be “a throwback to the English system prior to 1720” (ibid at 49), the discretionary letters patent model. As noted above, a regional variation of the UK-style memorandum and articles of association lived on in British Columbia which later became “trapped and isolated . . . when most of the rest of Canada modernised during the 1970s” (ibid).

The winds of change began blowing in Canada in 1967, when Ontario completely reformulated its corporate law, discarding the letters patent model. In doing so it did not look to existing UK law. “The English model, then 125 years old, was rejected as being outdated as well. An entirely new type of corporate constitution was created, combining the American-model statute with some innovative statutory remedies” (ibid at 50).

Among other things, letters patent incorporation was replaced by US-style incorporation by registration, one-person corporations were permitted, the ultra vires doctrine (of much less concern in a letters patent jurisdiction, in any event) became virtually irrelevant, pre-incorporation contracts were regularised, directors’ duties partially codified, insider trading regulated and statutory derivative actions permitted (see J Ziegel et al, Cases and Materials on Partnerships and Canadian Business Corporations, 3d ed (Scarborough: Carswell, 1994) at 101–102). It is important to note that, concurrently with the rethinking of corporate law in Ontario, major reforms to the regulation of securities markets were also implemented. Although their formulation differed, these reforms were directly inspired by US securities laws. The work begun in Ontario was continued and refined by the Dickerson Committee which proposed the federal CBCA a few years later. “Ontario paid the CBCA the ultimate compliment by withdrawing its own newly-minted Business Corporations Act and replacing it with the federal vision in 1982” (Ziegel-Meredith Lectures, supra at 3–4).

The sources of the CBCA were for the most part American. The most important contribution of UK law was the oppression remedy (based on s 210 of the UK Companies Act 1948, although a deferential nod of the head was made to Professor Gower for his work on the 1961 Ghana Code). Looking back after 20 years, one of the original members of the Dickerson Committee recollects:

It is enormously difficult to attribute to the CBCA any one source of law. From Gower’s Ghana Code the task force members acquired inspiration in the sense of questioning, as Gower had done with undoubted credibility, every single concept, jettisoning those that had outlived their usefulness, saving some, and synthesizing ideas from several sources to address current problems. From the [US] Model Business Corporation Act, the draftsmen extracted the whole structure, system of formalities and administrative law precepts. From the Uniform Commercial Code we derived the share transfer system, which rightly characterizes a share certificate as a special form of negotiable instrument. From various Commonwealth laws we synthesized the oppression remedy, complementing it with the derivative action as developed in Delaware and New York. And from working closely with the Canadian Institute of Chartered Accountants,
then led by its Executive Director, Doug Thomas, we developed what was probably the most original and most contentious part of the CBCA, the part dealing with corporate finance. Although very controversial, deleting the concept of par value was only a minor step. Far more significant were two other CBCA characteristics. The first was to discard conceptual labels and to characterize corporate securities as Protean instruments along a broad spectrum of attributes that can be adapted at will to meet market needs. The second was to delete all accounting disclosure standards from the act and, instead incorporate by reference into the CBCA the measurement and disclosure standards of the CICA Handbook. That eliminated a great deal of statutory verbiage, obviated bureaucratic regulation of the accounting system as under the SEC’s Regulation S-X, and assigned to an experienced self regulatory organization the obligation to maintain a system of necessarily dynamic accounting standards.

After 20 years of acceptance, those seem like trivial victories, but at the time they appeared to be, if not heresy, potential show stoppers in the political arena (Howard, supra at 4–6).

The Dickerson Report, which had been published in the form of draft legislation with accompanying commentary, was adopted by the legislature virtually unchanged as the CBCA. The existing Canada Corporations Act had not been comprehensively amended since 1934. Over a three year transition period, the application of the Canada Corporations Act to business corporations was phased out.

What had the Dickerson Report recommended that so changed Canadian corporate law? It is interesting to note what the Report considered to be “minor” reforms and why:

**Minor Reforms:**
- incorporation by designating number ("scarcely profound but useful")
- recognised validity of pre-incorporation contracts ("simple and long-overdue")
- recognised one person corporation (did away with a " tiresome, unrealistic and easily avoided bit of legal dogma")
- law of dividends ("clarify . . . a mass of confusing case law")
- permitting corporations to purchase their own shares ("relax a troublesome prohibition")
- change in method of incorporation from letters patent to registration (not a "basic change").

Some of the major reforms recommended, in the view of the Dickerson Committee, were the following:

**Major Reforms:**
- codification of directors’ duties and liabilities ("principles . . . more or less well developed in case law")
- codification of corporate dissolution (goal was to "rationalise")
- continuance and discontinuance provisions (permitting corporations to "transfer their place of jurisdiction")
- new regime for transfer of corporate securities ("eliminate expense and delay")
- new regime for rights and duties of auditors ("long neglected")
- shareholders’ remedies ("most significant and far-reaching")

In addition to their major and minor reforms, the Dickerson Report notes a variety of miscellaneous recommendations:

**Miscellaneous Reforms:**
- elimination of mandatory authorised capital; now may be unlimited ("much confusion in the past")
- elimination of par value ("utterly useless idea")
prohibition of partly-paid shares ("removes all kinds of difficulties")
non-voting shares ("shares may be of different classes, with different terms and conditions attached")
elimination of corporate objects and powers (to "reflect commercial reality") and elimination of the doctrines of ultra vires and constructive notice ("little more than a playground for the legal scholar")
no distinction between private-public corporations ("distinguished on functional rather than on doctrinal grounds")
legitimation of unanimous shareholder agreements ("allow closely-held corporation . . . to operate, in effect, as a partnership with limited liability")
elimination of mortgage register for registration of charges ("useless")

This checklist is instructive. Many of these "revolutionary" concepts are now common-place and have guided or are now guiding reform elsewhere.

General Observations and Trends

Industry Canada, the governmental ministry responsible for the CBCA, is currently in the process of conducting the first comprehensive review of the CBCA since its implementation in 1975. It is telling, and a fitting homage to its drafters, that the issues under consideration are primarily technical and a matter of updating and coordinating the legislation with developments elsewhere.

The major area of activity in the last twenty years which has had an impact on the CBCA has been securities regulation. The inexorable march of Canadian securities regulators into the domain of corporate law has meant that where overlap exists, the CBCA has been overtaken and surpassed. The federal government must now decide whether to leave certain areas of corporate law regarding public shareholders entirely to the securities regulators or to harmonise the CBCA so as to avoid regulatory conflict. The primary areas at issue are the regulation of take-over bids, shareholder communications, and insider trading and reporting.

The second major issue which is under consideration is the private corporation. The Dickerson Committee decided to abolish the distinction between private and public companies. There have been pressures to revisit this decision. Several factors may be responsible for this. The prevalence of "going-private" transactions in the last decade has focussed attention on the rights of minority shareholders and the nature of the private corporation itself. The unanimous shareholder agreement, the mechanism chosen by the Dickerson Committee to permit "incorporated partnerships", has, according to some commentators, not been as successful as it might have been given the statutory ambiguities associated with it. Several possibilities are being investigated: the "integrated" close corporation known in the United States (see Part 4, below); a separate legislative scheme which would eliminate boards of directors but restrict members to natural persons (such as in South Africa); or expansion and refinement of the unanimous shareholders' agreement.

Finally, the duties and liabilities of directors, in Canada as elsewhere, have been the subject of intensive debate. Corporate governance issues have been in the spotlight with a report of The Toronto Stock Exchange (the "Dey Report") following on the heels of
the well-known Cadbury Report in the United Kingdom. However, no changes of major significance with respect to directors are under consideration in the context of the review of the CBCA. Financial assistance provisions may be repealed, tightened-up or a disclosure-based approach adopted. Canadian residency requirements for directors of CBCA corporations are being reconsidered. Some technical amendments with respect to liability for unpaid wages and a good faith reliance defence are in the works, as well as provisions for the advance of defence costs and expansion of indemnity provisions for directors.

All in all, the current review of the CBCA represents no more than minor tinkering and readjustment of well-conceived and successful legislation.

**New Zealand**

**Introduction**

Following the pattern set in other Commonwealth jurisdictions, the United Kingdom Companies Act 1948 was the watershed for New Zealand companies law. As it had in the past, New Zealand enacted companies legislation in 1955 that "was almost an exact copy of the United Kingdom Act of 1948. The following of English precedent has been a tradition of New Zealand company law since the first Act of 1860" (New Zealand Law Commission, *Company Law — Reform and Restatement, Report No 9* (June 1989) at 8). The enactment of the New Zealand Companies Act 1955 was the last time New Zealand would follow the UK tradition in companies law without question.

**Historical Background**

From its inception in 1860 up to and including the Companies Act 1955, New Zealand company law had closely followed that of the United Kingdom. The New Zealand Companies Acts of 1933 and 1955 were modelled on the United Kingdom's Acts of 1929 and of 1948, respectively. The pattern of reform during that period was aimed mostly at technical update and at keeping in tandem with the United Kingdom and the rest of the Commonwealth (G J Shapira, "Introduction" in *Morison's Company and Securities Law*, Vol 2, *Companies Commentary Precedents* (Wellington: Butterworths, 1995) A/1 at A/6).

In 1968, the Special Committee to Review the Companies Act, chaired by Mr Justice Macarthur (the Macarthur Committee), was appointed. The 1972 Macarthur Report did not have a dramatic effect on New Zealand company law. The Committee did not attempt any major reappraisal of the Act against fundamental principles, but rather concentrated on correcting specific problems that had arisen over time. The main sources of the Report were the UK Jenkins Committee Report of 1962 and the Australian Uniform Companies Act of 1961. In its final recommendations, the Committee saw no need "to make fundamental changes in the framework of the Act" (*ibid*).
The first major break with the UK legislative tradition came in 1978 with the separation of securities law from companies law. The Securities Act 1978 came into operation in 1983.

Previously, when a company wished to raise funds, either by way of a share issue or debenture offer, the procedure it had to follow was regulated by the companies legislation then in force, ie, the Companies Act 1955. A characteristic of companies legislation, past and present, is that it is entity based. It is designed to regulate the activities of those entities called companies.

The Securities Act, however, was not drafted to regulate any specific kind of legal entity. Rather it is directed towards the activity of fund raising, thereby automatically bringing within its ambit all legal entities (ie, natural persons, unit trusts, partnerships, corporate bodies) which seek to engage in fund raising. (A Beck and A Borrowdale, Guidebook to New Zealand Companies and Securities Law, 5th ed (Auckland: CCH, 1994) at 145).

This distinction between entity-based companies law and activity-based securities regulation is very much North American in inspiration and informs all North American corporate and securities legislation.

The New Zealand securities legislation was drafted in response to a particular scandal which the Companies Act 1955 prospectus provisions (because they were "entity-based") failed to prevent. A huge regulatory gap had existed which only activity-based securities regulation could fill.

The notorious collapse of Securitibank provided the impetus for the legislation ultimately enacted as the Securities Act 1978. In particular, it was a matter of great concern that Securitibank’s activities in soliciting investments from the public were apparently not caught by the prospectus provisions of the existing law.

The Securities Act has created the Securities Commission and provided a structure for regulating fund raising (ibid at 146).

Once an activity-based securities law regime was put in place, the course of future legislation was largely set, the distinction between core company and securities laws being the guiding principle in ensuing developments.

Since the enactment of the Securities Act 1978, there has been an attempt to separate New Zealand core company and securities law. Both financial reporting . . . and takeovers are considered to be securities law matters, but ones that have direct relevance to the Companies Act (D Wishart, "Overseas Notes — New Zealand" (1991) 9 Company and Securities Law Journal 419 at 420).

The excising in 1978 of "securities law" from the Companies Act 1955 was the first, determinative step towards adoption of North American models in other areas of New Zealand law. Future companies law reform along North American lines became virtually inevitable. And, when legislators looked to North American models of companies law, they naturally considered the utility of North American models in other areas of the law.

The reform stage leading directly to the Companies Act 1993 began in September 1986. The Law Commission was asked by the Minister of Justice "to examine and review the law related to bodies incorporated under the Companies Act 1955 and to
report on the form and content of a new Companies Act”. The Commission’s mandate clearly called for a complete overhaul of company law (Shapira, supra at A/7).

One of the main goals of the Commission was to render New Zealand company law more intelligible and accessible for lawyers and non-lawyers alike. The 1955 Act, besides being complex and dense in form, contained only part of the law relating to company regulation. Some of the major company rules, for example directors’ duties, were not contained in the statute but had to be discerned from case law, which in many important respects was difficult to understand and at times contradictory.

To remedy this situation, the Commission set out to lay down the main rules governing company law in one statute. The Commission believed that the new Companies Act should be concerned with what it termed ‘core company law’, that is, the formation, operation and termination of all companies. According to this philosophy, the statute should contain basic company law applicable to all companies; whereas, legal requirements applicable only to some companies — for example, listed companies — should be imposed through specific legislation, and as such, be superimposed upon the core company law base contained in the Companies Act.

Despite mild assertions that the draft company law being proposed was not “based on any one overseas model”, it remains the case that the “(US) Model Business Corporations Act [was] of great assistance, as was the work of the Dickerson report which preceded the Canada Business Corporations Act” (New Zealand Law Commission, Company Law Reform: Transition and Revision, Report No 16 (September 1990) at xvii).

Report No 9, Company Law — Reform and Restatement, appeared in 1989. It proposed a dramatic rupture with the UK tradition in company law. As with the Gower Code and the Dickerson Report, the New Zealand Law Commission approached the company law reform exercise from a conceptual point of view, and not one of tinkering with the old ideas. Eminent company law expert, Professor Sealy, compared the significance of the legislation proposed to the introduction of limited liability in 1855:

Last year, the New Zealand Law Commission published a Report containing proposals for a major overhaul of company law — perhaps the most radical reappraisal of this branch of law that has been put forward anywhere in the Commonwealth (including the UK) since limited liability was introduced in 1855; certainly a document to be ranked with the Gower report (Ghana, 1961) and the Dickerson report (Federal Canada, 1971) for its rigorous analysis and forward-looking approach (LS Sealy, Remarks (Commonwealth Law Conference, 1990) quoted in Report No 16, supra at xvi).

It is only proper to disclose that Professor Sealy, a fellow of Gonville and Caius College, Cambridge, is a New Zealander.

In 1988, New Zealand and Australia had formally agreed to harmonise their business laws and, at the time of Report No 9, Australia was still very much within the thrall of the UK model. The New Zealand decision to make such a radical departure in its companies law needed careful consideration and justification in this context.

. . . . [The Law Commission believes that the present Australian legislation does not provide an acceptable model for company law reform. It is outdated and dense in form. While we do not
see harmonisation as requiring replication of the law in detail, the difference between what we propose and the existing Australian system goes well beyond detail. To follow the Australian companies legislation would preclude the major reforms proposed in this report of abolition of par value and nominal capital and the introduction of a better and more principled system of director accountability and shareholder remedy. It is the view of the Law Commission that there is little point in bringing in a new Companies Act if it does not achieve these reforms (Report No 9, supra at 11).

New Zealand decided to press on with its reforms despite the gap which this would create between Australian and New Zealand companies law. The Commission felt that although a high degree of harmonisation was desirable in the regulation of capital markets (ie, securities law), in the area of companies law the arguments were not as compelling. Again, inspiration for this decision came from North America where there is one federal securities regime in the United States (replicated at state level) but great diversity in state corporations law. The soundness of this decision is evident in the very recent Australian Corporations Law Simplification Program which is now, implicitly or not, taking its lead from the New Zealand legislation. Again, imitation is the highest form of flattery.

The New Zealand Department of Justice took a more cautious approach when it assumed responsibility for preparing the Companies Bill. The Law Commission’s draft was retained as the basis for the new legislation, but many details were altered, often to keep the proposed law closer in line with traditional positions. Among the notable changes introduced by the Department of Justice and substantively carried forward in the 1993 Act were those dealing with shareholder voting, directors’ duty of care and the company constitution.

The provision proposed by the Law Commission that a shareholder while voting does not owe a duty to the company was not carried over into the Bill. This reinstated the general law, allowing shareholders to vote in their own interests but also requiring them to vote in the interests of the company in certain cases.

The characterisation by the Commission of the directors’ duty to act in good faith and in the company’s best interest as “a fundamental duty”, and as based on an objective standard, was not carried forward. The Bill provided that the director had to act in good faith in what the director believed to be the best interests of the company. A provision requiring directors to act for a proper purpose, not recommended by the Law Commission, was added. In addition, a provision requiring directors not to let the business of the company be carried on recklessly was substituted for the proposal of the Law Commission requiring the directors not to risk insolvency unreasonably.

Although the statutory division of powers stating all rights and obligations of the company, its directors and shareholders was accepted, the Parliamentary Committee felt that the courts would inevitably be called upon to adjudicate in disputes where neither the new Bill nor the company’s constitution would provide a solution. Consequently, it was believed that a reaffirmation of the traditional contractual relationship between the shareholders, the directors, and the company was necessary. The Committee believed that such a reaffirmation would allow judges to fall back, in cases of doubt or statutory
void, on the old common law jurisprudence based on contractual analysis of a company's constitution as embodied in a memorandum and articles of association. The contractual relationship was reaffirmed in s 31(2) of the 1993 Act, which reads as follows: "The constitution is binding, in accordance with its terms, between the company and each shareholder, and among the shareholders." From a conceptual point of view, s 31(2) was the most significant mistake committed in translating the Law Commission's vision into reality.

The Companies Act 1955 left the distribution of power between the shareholders and the company to the memorandum and articles of association, which constituted a binding contract. Enforcement of rights and obligations between the shareholders and the company, and the shareholders inter se, rested on a contract analogy importing notions of contractual rights and privity. The contractual basis of the association also allowed maximum freedom for distribution of powers in the company, which could be determined by the incorporators subject to minimum mandatory statutory requirements (G Shapira, "Shareholders Actions and Remedies" in Morison's Company and Securities Law, Vol 2, Companies Commentary Precedents (Wellington: Butterworths, 1995) L/1 at L/2). The system was then given statutory recognition by s 34 of the 1955 Act which provided that, subject to the provisions of the act:

the memorandum and articles shall, when registered, bind the company and the members thereof to the same extent as if they respectively had been executed as a deed by each member and contained covenants on the part of each member to observe all the provisions of the memorandum and of the articles.

According to the Law Commission, this section was "entirely unsatisfactory, in that it did not assist in making the rights and obligations in a particular context easy to understand. It created the fiction of a contractual regime which was then overlaid by statutory provisions which imposed obligations and powers outside the "contract", including the power to alter the contract without the consent of all" (Report No 9, supra at 40).

In contrast to the 1955 "contractarian model", the Canadian legislation on which the 1993 Act was meant to be modelled has been described as "a statutory division of powers model" (Shapira, supra at L/2). Each corporate participant (directors, officers, and shareholders) is assigned certain rights and obligations by statute. The statutory constitution provides a system of enforcement based on the status of the individual corporate participants qua shareholder, qua director, qua officer. Each participant is given an extensive list of statutory remedies to which he or she has access because of the participant's status. The corporate constitution is not a contract. A participant demanding redress under the corporate constitution is not called upon to show some breach of the company's "contract" infringing upon a personal right.

A major criticism of the legislation, as finally enacted, was that the Justice Department's draftspeople did not understand the new conceptual underpinning of the draft legislation proposed by the Law Commission and so compromised the integrity and coherence of the legislation by adhering to older UK constructs.
The thrust of the Law Commission Report was to recommend changes in the fundamental ideas on which company law is based. We have discussed much of this in an earlier note... but have not emphasised the radical nature of the recommended change in the model of the internal organisation of the company adopted by the legislation.

The Companies Act 1955 (and current Australian legislation) adheres to the “contract” theory of the relations between shareholders, and shareholders and the company: the company is the result of the arrangements of those shareholders between themselves. This informs the language of incorporation, of shareholder rights, maintenance of capital and so forth. This the Law Commission recommended be changed to the Canadian (and before that, United States’) idea of “status”. To pervert Maine, the move is from contract to status.

The idea of “status” accepts the fact that incorporation needs no explanation. All that law has to do is determine the rights, duties, liabilities and obligations of the parties involved in the corporation. Thus various statuses are defined and their rights etc provided. The contractual base of the company is relegated to being an outmoded means for defining these matters.

Once the idea of “status” is accepted, much of the surplus company law may be cut away and some of the old conundrums solved. That to which directors’ duties are owed may be defined, as may the precise ambit of managerial discretion. The rule in Foss v Harbottle may be cast away. The corporate constitution may be seen to be enforceable without opening the floodgates (Wishart, supra at 422).

General Observations

The New Zealand Companies Act 1993 came into effect July 1, 1994. For a transitional period, it will operate concurrently with the 1955 statute which will finally be phased out July 1, 1997. New companies must incorporate under the 1993 Act and existing companies must, before the 1955 Act vanishes, reregister under the new Act. Even so, for this transitional period the 1955 Act has been pruned and modernised so as not to create great disparities in application with the 1993 Act. In the essentials, the two acts have been harmonised.

This is not to say that the transition to a new companies law regime has been an entirely smooth and happy one. David Wishart speaks of the “damage inflicted in its difficult birth” (Wishart, supra at 422) in terms of the conceptual inconsistencies introduced by the legislative drafting which could not shake off the UK heritage. Wishart looks to the New Zealand courts to “accept the thrust of the Companies Bill as it was intended” (ibid) but has reservations about the treatment which the legislation may receive at the Privy Council.

We cannot, however, be so certain of the Privy Council. The question is whether it will look to the vastly different conceptual base of the Companies Bill, or whether it will stick to the time honoured ideology of contract. If the latter, the major part of the effort that has gone into the Companies Bill will have been wasted (ibid).

These concerns may be mitigated to the extent that New Zealand is currently reviewing appeals to the Privy Council.

Whether Wishart’s fears will prove groundless is yet to be seen. There is no doubt, however, of the extent of change which the Companies Act 1993 has already wrought in the New Zealand legislative landscape. An entirely new infrastructure for commercial
law has emerged to provide support for the Companies Act. In 1993 alone, there appeared the Financial Reporting Act 1993 (establishing an accounting standards board, giving legal force to accounting standards, requiring issuers of securities to the public to prepare audited financials and stipulating the financial reporting requirements for such issuers); the Receiverships Act 1993 (replacing Part VII of the 1955 Act and creating a regime applicable to a wider class than just corporations); the Takeovers Act 1993 (establishing a panel for the purposes of recommending a Takeovers Code which would then have force of law); and the Companies (Registration of Charges Act) 1993 (replacing the charges provisions of the 1955 Act on an interim basis pending implementation of the comprehensive personal property security regime).

In addition, in keeping with the decision to adopt a North American model for Companies Law, it has become virtually inevitable that other complementary regimes will follow. For example, if, in following a North American corporate law model, the provisions on “Charges” are removed from the Companies Act, what replaces them? The Law Commission answered in its Report No 8, A Personal Property Securities Act for New Zealand:

The Committee believes that the introduction of a Personal Property Securities Act in New Zealand, based on the Canadian and United States models, and consistent with major reforms now being recommended in the United Kingdom by Professor Diamond, will mean that New Zealand will not only provide a lead in the adoption of standardised procedures between Australia and New Zealand but also play a significant role in harmonisation between the Australasian jurisdictions and their major trading partners in Canada, the United States and the United Kingdom. (New Zealand Law Commission, A Personal Property Securities Act For New Zealand, Report No 8 (1989) at 8–9).

It is early yet to determine the ramifications and ultimate success of New Zealand’s new legislation. An initial assessment, based on Australia’s obvious interest in the directions which New Zealand has taken, would indicate that a corner has been turned in company law in Australasia.

South Africa

Introduction

The law of present day South Africa is Roman-Dutch, modified to some extent by the reception of English law (H R Hahlo and E Kahn, The South African Legal System and its Background (Cape Town: Juta, 1968) at 330). The term Roman-Dutch law, coined by Simon van Leeuwen in the seventeenth century, signifies a form of civilian, continental law which was received in Northern Europe during the fifteenth and sixteenth centuries. This reception marked a watershed in the development of European legal history and created a clear dividing line between the continental and English legal systems. Unlike its present day civilian brothers, Roman-Dutch law has remained unaffected by the wave of codifications which took place in the aftermath of the French revolution (see generally Hahlo and Kahn, supra at 563).
Roman-Dutch law was the law of the province of Holland. As the wealthiest and most powerful of the Netherland provinces, Holland exercised a predominant influence in the affairs of the Dutch East India Company, the company which founded and administered the first colony on the southern tip of the African continent on behalf of the Republic of the Seven Provinces in 1652.

Despite the fact that Roman-Dutch law was abolished in Holland in 1809 and replaced by the Napoleonic Code in 1811, it lived on in the Cape colony. When the Dutch colony came under British rule in 1795, the principle, articulated by Lord Mansfield in *Campbell v Hall* (1774) 1 Cowp 204 at 209 with regards to conquered colonies, was applied: the laws of a conquered colony continue in force until provided for otherwise by British authorities. This helped to assure the survival of Roman-Dutch law under British rule. The government, administration and judicial machinery were nonetheless set up along English lines, and English civil and criminal procedure, as well as the law of evidence, were largely adapted. Finally, English commercial and company law were also introduced.

Although there were areas where the influence of English law was minimal, such as the law of persons and successions, English legal rules and holdings began to be used more and more as persuasive material where Roman-Dutch law was silent or ambiguous. Unlike the similarly fated civilian jurisdictions of Quebec and Louisiana, where the enactment of civil codes helped to stem the flow of the incoming common law tide, no such codal breakwaters existed in South Africa. Company law was one of the areas in which the English common law made its greatest headway.

After the establishment of the Union in 1910, a civilian backlash against English law gained momentum as the years went by. However, today it is being recognised more and more by doctrinal writers and the courts alike that a non-codified civilian system, such as the one found in South Africa, might in fact derive more assistance from the non-codified common law of England than from the codified civilian systems of the continent (see generally Hahlo and Kahn, supra at 592).

**Historical Background**

Until relatively recently, the company law of South Africa developed along the same lines as that of the United Kingdom. The Joint Stock Companies Limited Liabilities Act 23 of 1861 of the Cape colony was based on the English Limited Liability Act of 1855. The Cape Companies Act of 1892, which replaced the 1861 Act, was based on the English Companies Act of 1862. Law 1 of 1891 was largely a carbon copy of the UK Directors' Liability Act of 1890. The Cape legislation in turn was adopted by the Orange Free State and Natal. After the Union of 1910, the provincial company statutes continued to apply. They were replaced in 1926 by the Union Companies Act, which was amended from time to time along the lines of the latest English legislation.

It was not until 1973 that South African Company law began to go its own way with the adoption of the Companies Act of 1973, the fruit of the labours of the Van Wyk de Vries Commission (1963). The process of drift away from the English model was
accelerated with the adoption in the United Kingdom of the European Communities Act of 1972 and its successors. Nevertheless, the Companies Act of 1973 remains very much UK-style memorandum of association legislation, with all of the related trappings.

The most significant example of the different roads recently taken by UK and South African lawmakers is the adoption in 1984 of the South African Close Corporations Act. This new legislative direction was inspired by the UK Green Paper on A New Form of Incorporation for Small Firms, itself based on a memorandum (Cmd 8171) written by Professor Gower. Ironically, although this new direction was warmly received in South Africa, it was never implemented in the United Kingdom. Despite recent developments, UK cases continue to be referred to as persuasive authorities in many areas of South African corporate law (H R Hahlo, South African Company Law through the Cases (Cutter Cape Town: Juta, 1984) at 16).

South African Close Corporations Act 69 of 1984

The South African Close Corporations Act has proved to be one of the most remarkable innovations in South African company law. This special legislation for the incorporation of small companies combines many of the attributes of partnership with the corporate attributes of legal personality and limited liability.

Unlike the experience in the United States (see Part 4, below), the South African Close Corporation legislation appears to have been singularly successful. “The acceptance of the concept of the close corporation is borne out by the large number that have been formed in the nine years since the Act became operative, almost three hundred thousand close corporations compared to approximately sixty thousand companies of all types and forms” (J J Henning, “Closely Held Corporations: Perspectives on Developments in Four Jurisdictions” (1995) Journal of Contemporary Roman-Dutch Law 100 at 101).

One of the differences noted by the commentators between the US experience and that of South Africa has been the South African emphasis on simplicity. The Statutory Close Corporation Supplement to the Model Business Corporation Act and the acts following it have been criticised in the United States as “so cumbersome that lawyers are afraid to use them”. This is conceded by the draftsmen of the Supplement: “To a large extent, the statutory framework for close corporations will inevitably be somewhat complex because the provisions must be drafted around the existing corporate statutes and case law” (S J Naudé, “The Need for a New Legal Form for Small Businesses” (1982) 4 Modern Business Law 5 at 11).

The purpose of the South African Close Corporations Act was to provide a simple, inexpensive business entity for a single person operation or that involving a small number of persons. No restriction is placed on the size of the business or undertaking, merely on the number of participants (no more than ten who must generally be natural persons). It was envisaged that a successful business of a close corporation should not outgrow its legal form. The system was carefully designed to appeal to both the unsophisticated business person (who simply adopts the statutory regime) or
sophisticated business people who can alter the statutory regime by agreement. And, unlike partnership, there is no requirement that the entity be used for profit.

The impetus for creation of the separate regime for close corporations in South Africa sprang from frustration with the complexity of the existing UK-inspired South African Companies Act of 1973 and its unresponsiveness to the needs of small businesses. "It is known that sham compliance with formalities, like the drafting of notices and minutes of meetings that never took place, is common practice. This is a waste of money and skilled manpower. Moreover, the fact that this sham compliance has not given rise to serious prejudice does not prove that the 'system works'. It rather shows that the formalities concerned are meaningless. Sham compliance also fosters disrespect for the law" (Naudé, supra at 6).

The decision was made to create a separate statute rather than amend the existing Companies Act. This decision was influenced in large measure by a similar approach in continental Europe, where separate regimes exist for typically bigger and smaller businesses (see discussion of the German GmbH and French SARL in Part 5, below). The goal was to achieve "the greatest possible simplicity" and "an attempt to build the required flexibility into the Companies Act could only exacerbate the problem by an inevitable overall increase in complexity" (ibid).

Although the approach was inspired by continental Europe, the models were not the GmbH or the SARL. "Guidance was sought in modern Corporation Acts (for instance the Canada Business Corporations Act of 1975), various partnership codes and Professor Gower's 'The Incorporated Private Partnership Bill' in the Final Report of the Commission of Enquiry into the Working and Administration of the present Company Law of Ghana (1961)" (ibid at 12).

The South African Close Corporation may startle a traditional company lawyer. There are no shares and no board of directors. Incorporation is effected by registration of a single document. Capital maintenance requirements have been abandoned in favour of solvency and liquidity tests. The close corporation has the capacity and powers of a natural person; there is no room for application of the ultra vires doctrine or constructive notice. There is a simple statement of fiduciary duties of members and the negligence standard of care. One person corporations are possible. All members must actively participate in the business and have equal rights to do so (although these provisions may be waived). There must be annual accounts prepared by an accountant. It is not necessary that the accounts be audited by an auditor.

The legislation has done away with the multitude of criminal offences and administrative duties under the Companies Act.

This is a significant defect of the Companies Act, which bristles with sections creating purely technical offences, which are sometimes difficult to explain, and in many cases rarely, if ever, enforced. Criminal law is a blunt and largely ineffective instrument for ensuring that technical or administrative duties imposed in an act like the Companies or Close Corporations Act are complied with (ibid at 16).

Self-enforcement has replaced criminal sanctions; the rules are few, but if they are not followed, members incur personal liability.
General Observations

The South African close corporations legislation has been looked to by other jurisdictions in Africa, and most recently Australia and Canada. In South Africa itself the expectation was that the new concepts introduced by the Close Corporations Act would spread to the existing Companies Act. This may not have happened as quickly as expected but the hope survives "that various innovative concepts of the act that have survived the proving grounds of competitive corporate practice during the past decade, constitute a convenient and readily available blueprint for the imaginative and speedy reform of important areas of South African company law" (Henning, supra at 101).
Part 4

The United States
Part 4

The United States

Introduction

The United States is undoubtedly one of the richest sources of legislation, case law and debate about corporations. There is no federal corporations statute as such (although there has been debate in the past as to its desirability). Each state has its own corporate law regime which has resulted at times in competition among states to attract incorporations (a phenomenon about which a lively literature has developed).

State incorporation has produced a wide diversity of legislation and experimentation in the corporate form. The situation is not, however, as chaotic as might be implied by the existence of fifty or so different corporate laws operating in the same country. There are several mitigating factors promoting harmonisation, cooperation and, in some cases, uniformity across the United States.

The first is the ever important federal Constitution; although there is no express federal jurisdiction to govern incorporations, under the very broad interstate commerce clause a myriad of federal legislative provisions apply to state incorporated entities. In this way, uniformity of standards and treatment in certain areas is assured: anti-trust, bankruptcy, securities, among others. In addition, the court structure is such that the so-called “diversity jurisdiction” of the federal court system may catch commercial litigation, thus developing a body of federal case law applicable to corporations. And the famous “full faith and credit” clause of the US Constitution assures recognition of state legislation and case law from one state to another.

Perhaps the most significant of these federal laws applicable to corporations is the federal securities regime. In the 1930s, in reaction to the stock market crash of 1929, the federal government enacted a series of securities statutes in the interests of public investor protection. The agency created to administer this legislation, the Securities and Exchange Commission (SEC), grew to be one of the most powerful administrative agencies in the world. Although there have been jurisdictional battles between the SEC and state legislatures over where the lines are drawn between corporate law matters and securities law matters (in the realm of takeovers, for example, during the 1980s), it remains the case that many areas of overlap respecting shareholders have been preempted by SEC action. Thus many matters characterised as “company law” elsewhere have been characterised in the United States as securities law and taken out of the orbit of the state legislatures. Some commentators even speak of a “growing body of ‘federal corporation law’” (H Henn and J Alexander, Laws of Corporations, 3d ed (St Paul: West Publishing, 1983) at 7).

A second harmonising factor has been the existence of model statutes. These serve
variously as uniform acts or as drafting guides which may be customised by each individual state.

A Uniform Business Corporation Act was sponsored in 1928 and adopted by a few states. It was renamed the Model Business Corporation Act in 1943 and then withdrawn in 1958. It was supplanted in 1946 by the American Bar Association Model Business Corporations Act (MBCA) which was revised almost annually after that. During the 1960s, the “march of American state corporation law became a march toward uniformity (D Branson, “Countertrends in Corporation Law: Model Business Corporation Act Revision, British Company Law Reform, and Principles of Corporate Governance and Structure” (1983) 68 Minnesotta Law Review 53 at 57). By 1977, 34 of the 50 states had adopted MBCA statutes (see ibid). In 1984, the Model Business Corporation Act was itself supplanted by the Revised Model Business Corporation Act (RMBCA) (the “revised” was recently dropped but is retained here to distinguish it from its predecessor). A large number of states adhere to one or the other Model Acts. As of 1993, 22 states closely followed the RMBCA. As the product of the American Bar Association (Section of Business Law), the RMBCA is a good indicator of many of the current debates being held among American practitioners and scholars alike.

The third stabilising factor in corporate law in the United States has been the emergence of a small number of “lead jurisdictions”. Delaware, New York and California literally lead rather than follow the Model Acts. The drafters of the Model Acts, at a distance, pick up on trends and innovations in the lead jurisdictions.

Although not itself a state of great commercial activity, Delaware is well-known for its management friendly legislation and as home to the “Fortune 500” corporations in America. Its detractors accuse it of having turned incorporation into an industry in and of itself. Defenders of Delaware cite it as providing a “national law” for large public companies by providing a highly responsive statute, sophisticated practitioners and administrators, and a knowledgeable and specialised judiciary. “New York is generally recognised as the leading business law jurisdiction in the United States, and it rivals Delaware for prominence as a corporate law jurisdiction” (J MacKerron, “Variety of Choice in the Corporate Law ‘Menus’ of the Great Lake States” (1994) 71 University of Detroit Mercy Law Review 469 at 471). California, like New York, being a jurisdiction of great commercial activity, has developed its own unique corporate law regime, which in some respects represents a much more invasive or regulatory approach to governing corporations.

**Historical Development**

Unlike “gas” and “petrol”, the distinction between a corporation in America and a company in the United Kingdom is not one of terminology alone. Thanks to the American Revolution, the corporation in America branched off very early from its UK roots and followed a different conceptual and evolutionary path. United States corporations are distinct from and do not historically find their origins in the 19th
century joint stock company. The statutory regime applicable to American business corporations developed rather from the special charter or special act corporations, which started to appear shortly after the American Revolution.

For historical reasons, there is a joint stock association or company recognised in the United States but it is of little significance. “In American jurisdictions, the joint stock association is generally an unincorporated business enterprise with ownership interests represented by shares of stock. These companies, no longer a very prevalent form, were recognised at common law, but they are now subject to some statutory regulation” (Henn and Alexander, supra at 109).

In the decade following the Constitution, some 200 more business corporations were incorporated in the United States under special acts of state legislatures. Fears of crown and [sic] monopoly made this a jealously-guarded legislative function. Corruption and bribery of the state legislators and the inefficiency of the system, coupled with the impact of the Industrial Revolution, called for a change. The special charters, however, provided generalized patterns for the resulting state corporate statutes (ibid at 25).

Corporations incorporated under a “general corporation law” (Delaware’s is still called this) are thus to be distinguished from corporations incorporated by “special” legislative act. Persons could incorporate under these general incorporation statutes, which began to appear between 1795 and 1837, without special legislative favour. “Beginning near the end of the 19th century, all American jurisdictions except Connecticut, Massachusetts, New Hampshire and, of course, the District of Columbia, ratified constitutional provisions prohibiting special incorporation and requiring incorporation under general law” (ibid at 26).

The implications of the very different origin of the American corporation (as opposed to the United Kingdom company) go beyond historical interest. The corporation in America has never been a quasi-partnership entity requiring a “contract” among its “members” for its existence: there has thus been no impediment to the acceptance of the one person corporation; filing and incorporation formalities have been minimised; and the ultra vires doctrine never really took root.

**General Characteristics of US Corporate Law**

Given the diversity of corporate law regimes in the United States, it is with temerity that one makes generalisations. The Model Acts and the lead jurisdictions, however, have provided definition to US corporation law:

In drafting a new corporate statute it is necessary to determine what goals the statute is designed to achieve. Traditionally, the watchwords of the Model Act have been “flexibility” and “modernization”. From this perspective, corporation statutes should be designed to assure efficiency and economy of management and to avoid unnecessary costs. In contrast, some academics have criticized most modern corporation statutes on the ground that they are too “permissive” — that they do not provide adequate protection for interests other than incumbent corporate management. This view would make the basic goal of corporation statutes the “protection of shareholders” or “strong” regulatory goals (R W Hamilton, Corporations, 4th ed (St. Paul: West Publishing, 1990) at 179).
Although commentators detect a strong management orientation in the RMBCA (and point to Delaware as the major influence), the original thesis of the Model Acts "was to attempt to preserve in proper balance the interests of the public, corporations, shareholders, and management, and not to seek to attract local incorporations" (Henn and Alexander, supra at 200).

However, the [MBCA] has been revised from time to time and came to include alternative provisions (eg, preemptive rights, cumulative voting, nimble dividend provision) and optional provisions (eg, share rights and options, emergency bylaws, removal of directors, actions by directors without a meeting, provisions relating to actions by shareholders, amendment of articles of incorporation in reorganization proceedings, merger of subsidiary corporation) (ibid).

A certain amount of controversy exists with respect to the current RMBCA, whether it pursues 'flexibility' and 'modernization' too aggressively, at the cost of 'shareholder protection' (Hamilton, supra at 180). There has been a decided weakening of traditional shareholder protections and the elimination of substantive or other mechanisms providing shareholders with control over corporate entities: presumptive cumulative voting for directors has been eliminated; directors are given much more latitude in the declaration of dividends; there are no automatic preemptive rights. There is a lowered threshold for shareholder approval of amendments to the articles of incorporation and standards have been lowered for interested directors' contracts (see generally Branson, supra).

This trend toward lessened shareholder protections should not, however, be viewed in isolation; it may, in fact, be more a product of the recharacterisation of areas of corporate governance as matters more properly subject to the oversight of securities regulators. The protection of public shareholders is the preserve of a powerful regulator in the United States, the SEC, which has in recent years implemented measures designed to promote greater accountability of management of public corporations to shareholders. In addition, despite what some commentators have seen as an "irreversible" trend (following Delaware's lead) towards "permissiveness" in corporate statutes in the United States, Delaware has "come a long way towards protecting the rights of shareholders and promoting the fundamental concept of corporate accountability" in its application of the business judgment rule and its interpretation of duties owed by majority to minority shareholders (R C Ferrara and M Steinberg, "The Interplay between State Corporation and Federal Securities Laws" (1982) 7 Delaware Journal of Corporate Law 1 at 3).

The MBCA was, until relatively recently, representative of corporate mainstream resistance to increasing managerial discretion at the cost of statutory regulation of corporate governance. This Act, first published in 1946, was largely modelled on the Illinois Act of 1933. It set relatively high minimum standards limiting managerial discretion, maintained a certain level of shareholder protection by way of affirmative commands and definite prohibitions, and held corporate directors and officers to relatively high standards of conduct and procedure.

The person who first noted the laissez faire shift in course of the MBCA was Professor Eisenberg (Branson, supra at 57). The RMBCA has gone even further than its
predecessor in mimicking the manager-friendly, Delaware-style corporate statutory model, a model which until recently was so criticised and even satirised by mainstream spokespersons (cf, for example, M A Eisenberg, "Law for Sale: A Study of the Delaware Corporation Law of 1967" (1969) 117 University of Pennsylvania Law Review 861 portraying the Delaware Legislature as bumbling and manipulated by the big corporate interests of the Delaware Bar).

This gradual change of character on the part of the MBCA-RMBCA has been characterised as one from middle-of-the-road and mildly mandatory in nature to enabling in the extreme. Critics believe this has had a negative impact on minority shareholder rights.

A useful comparison of the lead jurisdictions, New York and Delaware, to the RMBCA has recently been published which indicates that, on the whole, there are greater similarities than differences between jurisdictions in the United States (see MacKerron, supra). MacKerron has recently demonstrated that corporate statutes in the United States, both state and Model legislation, have experienced such a degree of convergence that today they are on the whole much more alike inter se than they are different (MacKerron, supra at 516). Any one Act should therefore be largely representative of the others in general theme and outlook. Based on MacKerron’s work, Appendix III is a survey of the major provisions of the RMBCA, with references to the corporate legislation of Delaware and New York.

General Observations

The debates and trends of the last fifteen years in US corporate law have been well-documented: the era of hostile take-overs and leveraged buy-outs, pitching management against shareholders, giving rise to defensive tactics and provoking jurisdictional battles between state legislators and the SEC; going-private transactions raising issues of abuse of minority shareholders; the rise in prominence of the institutional investor; corporate accountability, to shareholders and to a wider range of constituents; measuring executive compensation against performance. For purposes of this summary, the following observations are necessarily selective.

According to one commentator, “[f]lexibility has become pandemic” in US corporate law (Branson, supra at 71). Rather like a US supermarket, there are a staggering number of choices available, even within any one state regime. The corporate statutory regimes have been likened to partnership laws where the statute provides a default regime in the absence of express choice in the articles, bylaws or shareholders agreements.

Although the United States is noted for its public widely-held corporations, as elsewhere, in absolute terms, closely-held corporations predominate. Various legislative experiments have been conducted with respect to creating special or adapted legislative regimes for close corporations. Not all have been considered successful. Florida enacted the first such statute in 1963 but repealed it in 1975; most of its provisions were then absorbed by the general corporation statute.
The RMBCA has a Model Statutory Close Corporation Supplement which accompanies but does not form part of the RMBCA. As in many of the other regimes applicable to close corporations (New York and Delaware, for example), an election to "opt-in" to the close corporations regime must be made under the Model Law. A close corporation under the Model Law cannot have more than 50 shareholders. The Model Law regime permits a close corporation to dispense with the board of directors or to restrict the directors' discretion by means of a shareholders' agreement.

Professor Hamilton surmises that "(a) close corporation statutes may not be really needed, or (b) that attorneys are very cautious about trying new and untested devices" (Hamilton, supra at 555). The requirement that a corporation voluntarily choose close corporation status (rather than such status automatically attaching to corporations meeting the eligibility criteria) may account for the relative unpopularity of the regimes in the United States. An alternative approach has been to include in the general corporation law provisions which automatically apply to all corporations with less than a specified number of shareholders or which have not made a public offering.

It is hard to generalise about the structure of close corporations in the United States as they vary widely. There are provisions dispensing with the board of directors; permitting shareholders to manage the business of the corporation directly; provisions relating to improving remedies for deadlock and dissension; share transfer restrictions; simplification of the internal structure of the corporation; the ability to dispense with bylaws, annual meetings and any requirement that a document be executed by more than one person on behalf of the corporation (see Hamilton, supra at 554). Delaware specifically validates any agreement, bylaw or provision in the articles that treats the operation of the close corporation as a partnership (Delaware General Corporation Law, s 354). After all is said and done, however, it may very well be that specialised regimes are not overly attractive in the United States because of the degree of flexibility accorded corporations as a matter of course under the general corporations statutes.

Another specialised regime that has emerged very rapidly in the United States (to the point where virtually every state has adopted such a regime or is in the process of considering one) is that applicable to limited liability companies. The limited liability company (LLC) is a tax-driven hybrid form of business enterprise, essentially a "company formed by members under statutory authority with legal personality and limited liability" (R Raizenne, "Hybrids and Joint Ventures" in Corporations at the Crossroads (Paper presented at the Meredith Lectures, McGill University, Montreal, Canada, 1995) [unpublished]). For tax purposes in the United States, an LLC is treated like a partnership (with the flow-through effect of accounting for profit and loss). Members are "permitted to consolidate their respective shares of the income, losses and other deductions of the LLC in computing their incomes under the [tax] Code, thus both eliminating the potential for double taxation as earnings are distributed by the entity to its members and permitting members to shelter income from other sources using losses and other deductions of the LLC" (ibid at 23).

Of all the states, California may have the most idiosyncratic corporations law, especially in its treatment of foreign corporations.
California exercises its legislative jurisdiction over foreign corporations, by applying more of its domestic corporation provisions to foreign corporations than does any other state. Among the more regulatory California provisions which apply, "to the exclusion of the law of the jurisdiction" of incorporation are those requiring annual election of directors by cumulative voting, permitting removal of directors by shareholders without cause or by court proceedings, defining the directors' standard of care, imposing liability on directors for cash or property distributions to shareholders unlawful under California law, spelling out permissible indemnification for directors and officers, limiting cash or property distributions to shareholders, imposing liability on shareholders who receive unlawful distributions, providing for the sale of assets and mergers, innovating the concept of 'reorganizations' and providing for dissenters' rights" (Henn and Alexander, supra at 220–21).

Not all foreign corporations in California are subject to these provisions; those listed on a national securities exchange are exempted as well as those which do not meet tests indicating a substantial number of resident California shareholders and creditors.

Finally, despite the sheer mass of US corporations and the diversity of their form, the increasing internationalisation of commercial transactions is influencing corporate structure and governance. According to certain commentators, this trend is resulting in more convergence with foreign models.

Stress from international competition reveals weaknesses in some American firms, presses American firms to change and makes us wonder whether international competition is not just among firms but also among forms of organization... Competition also partly substitutes for effective corporate governance (M Roe, "Some Differences in Corporate Structure in Germany, Japan and the United States" (1993) 102 Yale Law Journal 1927 at 1994).

According to Roe, regimes as different as the American, German and Japanese are starting to look a little more like each other. The 1932 Berle and Means paradigm of separation of ownership and control in large US corporations through fragmented and widely held share ownership is changing. That such a pattern of shareholding arose at all may have been indicative of a "local custom", and one which will pass, rather than "the result of an inevitable economic evolution" (ibid at 1936).

The rapid rise in the importance and influence of the institutional investor in the United States is a prime factor. This tendency will only gather momentum as the fragmentation of financial institutions in the United States (a legacy of the 1930s Glass Steagall and McFadden Acts) diminishes and there will be greater concentration of share ownership. This trend is already apparent in the smaller American firms where the levels of concentration of ownership are beginning to approach those typically found in Germany and Japan (ibid at fn 22).
Part 5

Continental Europe and the European Union
Part 5

Continental Europe and the European Union

Introduction

Modern commercial associations in Continental Europe have long roots going back, as much of the civil law does, to Roman law and the medieval law merchant. The two principal concepts from which they have developed are the commenda and the societas. Each of these concepts has also, more indirectly, exerted an influence in the development of common law business associations.

The commenda was one of the earliest formalised systems of commercial joint enterprise, combining aspects of a partnership and a financing transaction. The most significant characteristic of the commenda was its early acceptance of the notion of limited liability, permitting a passive investor to provide capital to an enterprise with the assurance that his liability was limited to the capital advanced.

The commenda was extremely popular in Italy and in France from the 12th century on. In England, however, the commenda never really caught on, although there is some evidence that it was used. One possible explanation is that, unlike the situation on the Continent, the courts of common law and equity eventually assumed jurisdiction over commercial law, whereas outside of England commercial law remained under the jurisdiction of the commercial courts and the law merchant, which recognised the commenda.

In civil law countries, the commenda developed into the société en commandite which appears to this day in the legislation of many civil law jurisdictions. It received legal definition in France for the first time in a Royal Ordinance of 1673, and was further refined in the Code de Commerce of 1808 (J Boileau, Société en commandite (Montréal: Hautes études commerciales, 1945) at 18–24). Some 100 years later the société en commandite was the inspiration for the common law limited partnership legislation which was introduced in England in 1907.

The modern idea of the company as a separate legal entity may also be traced to the Roman societas, an association of persons with legal rights and duties independent of its individual members. The societas was a consensual contract formed when the parties had reached agreement on the “essentialia”: these were the pooling of resources and the pursuit of a common, profitable goal. Each partner was obliged to make a contribution, whether of capital, other property or labour, and to share in the profits and losses of the societas (see P H J Thomas, Introduction to Roman Law (Deventer: Kluwer, 1986) at 109–110). In both the common law and the civil law, the societas developed into the modern concept of general partnership.
The societas (which in fact took several different forms) had a direct influence on
the development of corporate law as well as in the civil law:

The modern civil law of the European continent derived its corporation practice from the
model of these special types of partnerships. The very name of the continental institution most
resembling a corporation—société anonyme, sociedad anonima, societa anonima—indicates
it, and societas in the modern codes, generally included both our partnership and our corporation
(M Radin, Handbook of Roman Law (St Paul: West Publishing, 1927) at 271).

Where the civil law and the common law diverge is with respect to the concept
of legal personality, which is much more readily attributed in civil codes
to unincorporated associations such as partnerships. The concept of legal persons
("les personnes morales") is much more established and pervasive in civil code
countries, where it includes a broader class of commercial and non-commercial
enterprises. Thus, generally speaking, although the primary attributes of the modern
"company", limited liability and separate legal personality, are a relatively recent
development in common law jurisdictions, they have a long and venerable history in the
civil law.

In viewing corporate entities in Continental Europe today, several general
considerations of an historical nature should be kept in mind. The first is the distinction
between civil law and commercial law which developed early in the 19th century. The
first modern civil code appeared in France in 1804 (dealing primarily with persons,
property and obligations) and was followed in 1807 by a commercial code dealing with
a variety of commercial matters. The early formulation of a commercial code had
several consequences.

There developed a proliferation of specialised business entities the characteristics of
which were detailed and set out in a comprehensive manner in the codes. In countries
with a strong tradition of public record keeping, these entities were created by public
registration. In keeping with the specialised nature of the commercial entities created,
dispute resolution was dealt with by specialised commercial tribunals organised under
the commercial codes.

The early codification of these business entities in the 19th century is to a certain
extent responsible for modern criticisms directed at them. Rigidity of structure, over-
emphasis on formalities of constitution, and the perpetuation of anachronistic 19th
century concepts (especially as concerns capital structure) have been cited. The
proliferation of specialised forms of entity has been attributed to the lack of flexibility in
existing statutory regimes.

In addition, a different weighting developed for the interests of the various
"constituencies" within the orbit of the corporate entity. Perhaps in response to an
inadequately developed codal regime for the granting of security interests, structural
mechanisms for the protection of creditors developed in the corporate law and were
buttressed by civil law property concepts.

Germany, in particular, used structural mechanisms within the corporation to
balance the interests of employees with those of shareholders. And, given the
predominance of majority controlled public corporations in Europe, the necessity for
according minority shareholders statutory protections was recognised through exceptions to the principle of shareholder democracy.

Most recently, the emergence of a unified Europe has forced a reconsideration of the fundamentals of European corporate law, juxtaposing the common law traditions of United Kingdom company law against the very different traditions of continental Europe. The point of greatest conflict has been the establishment of a pan-European form of business entity, a supra-national corporation or company, the societas europea. At the national level, harmonisation of corporate law regimes is proceeding apace through the implementation of European Commission Directives, in which the influence of American corporate law concepts, such as the one person corporation, is increasingly apparent.

The following discussion is, of necessity, not exhaustive. Rather it serves merely to highlight some of the more significant aspects of modern French and German corporate law as well as the proposed societas europea.

France

The various forms of business enterprise in France may be governed by the Commercial Code (largely superseded now by other legislation), the Civil Code and, in particular, the Law of July 24, 1966 and the Decree of March 23, 1967 (referred to generally here as French Company Law). Together with traditional forms of incorporation and partnership, there have been more recent innovations, some of which have been picked up by the European Commission for pan-European use. And, as elsewhere in the European Union, French Company Law has been subject to the harmonising influences of European Commission Directives.

Historically, the two main forms of incorporated entity in France were the société anonyme (SA) or “corporation” and the société à responsabilité limitée (SARL) or “limited liability company”. Unlike the SA, the SARL has a limitation on the number of members and restrictions on transfers of interests in it. It corresponds roughly to the concept of a “private company” under UK law, although it is closer in substance to a registered partnership. As the regulatory, reporting and filing requirements applicable to each entity have converged to a great degree over time, the distinctions between the two forms of incorporation have become less significant.

Société Anonyme

In some respects, the SA still retains many of the formalities of its 19th century origins; in others, for example, its exclusive use of book-entry securities, it has been brought quite up-to-date. SAs may be quoted or unquoted. A quoted SA has securities listed on a French stock exchange and offered to the general public; it is subject to separate listing, prospectus and other requirements. All SAs are created by registration with the Commercial Court in accordance with the formalities of French Company Law. They are subject to the provisions of the Commercial Code and the jurisdiction of a specialised tribunal, the Commercial Court.
There are many technical formalities associated with incorporation as an SA, some of rather ancient vintage: a minimum of seven shareholders who may be individuals or other legal entities; a minimum legal capital of FF250,000 of which one-quarter must be paid in at the time of incorporation; a minimum legal par value of shares must be set out in the articles of incorporation. Unlike many common law jurisdictions, the corporation does not have perpetual duration but rather a maximum term of 99 years.

Shareholder protection is provided primarily through the capital structure and the control exercised by the general meeting of shareholders. Non-voting shares are entitled to priority dividends of a fixed amount. There are restrictions on the creation of non-voting shares and on the percentage of capital which they represent (25%). Directors and officers may not hold non-voting shares. Authorised but unissued shares are not permitted. Limitations are placed on inter-related shareholdings. Shareholders must approve dividends and certain other corporate actions. In certain circumstances, unanimous shareholder approval is required. Shareholders are given the power to liquidate the corporation if the value of the net assets falls below a certain threshold. Shareholders can remove directors without notice, cause or indemnity.

Largely as a result of the harmonisation efforts of the European Commission, dominated in this respect to a large degree by Germany, the SA's board structure is fairly complicated with two different options being available. The first option is a board of directors (conseil d'administration) fairly comparable to that in Anglo-American company law, although the rules applicable to its composition are more rigid. There must be a minimum of three and maximum of twelve directors who may be individuals or legal entities; the chairman (president) of the board must be an individual; all members must hold qualifying shares in the corporation; the maximum term is six years (except for first directors). Employees may be members of the board of directors although there are restrictions on their numbers.

The chairman of the board is responsible for operational management and has broad powers. The board may also appoint a general manager (directeur général or DG) who is not necessarily a board member but who has the same powers as the chairman with respect to third parties. Larger SAs can have up to five DGs.

The second option shows more of the influence of the German model. The corporation is managed by a two-tier board, a directorate under the control of a supervisory council. The supervisory council resembles fairly closely the board of directors in structure and function except that it controls the directorate. The directorate may have one to five members (who need not be shareholders). It has broad powers to act and submits quarterly reports to the supervisory council. There can be no overlapping membership between the supervisory council and the directorate.

Employees may be members of the directorate but not of the supervisory council. All enterprises in France of a certain size must have a labour-management committee (comité d'entreprise), which serves as the mechanism for worker participation in corporate management (again, of German inspiration). The labour-management committee has the right to be informed and consulted on major changes to the business and the conditions of employment.
Société à Responsabilité Limitée

The SARL, often translated as the limited liability company, has a simpler structure than the SA. It may have no fewer than 2, and no more than 50 members; in the event its members exceed 50, it must convert to a SA. The minimum capital (FF50,000) must be fully subscribed at incorporation and there is a minimum par value of FF100 per share.

In structure, the SARL more closely resembles an incorporated partnership. It does not have shares as such but rather book entry ownership interests which are termed participations in capital (parts sociales). No share certificates are issued and there is a prohibition on the public offering of securities. Although the ownership interests may be freely transferable among members and their representatives, transfers to third parties require the consent of the majority of members representing at least three-quarters of the share capital. Statutory buy-out provisions apply in the case of refusal to authorise the transfer.

Managers, named in the articles or appointed by the members, have very broad powers which cannot be limited in relation to third parties. All decisions except approval of financial statements may be made by the members in writing. A super-majority vote of the members is required to amend the articles of incorporation.

Other Corporate Forms

Reflecting a more generalised trend towards acceptance of one-person corporations, member states of the European Union have been enacting legislation to permit this form of incorporation. In France, it is possible to create an EURL (entreprise unipersonnelle à responsabilité limitée) having all the same characteristics of an SARL except that there is a sole shareholder.

The legal nature and status of joint ventures in France is much clearer than its murky counterpart in common law jurisdictions. There are several forms of statutory joint venture available in France, ranging from pure partnership structures, to hybrid entities combining aspects of legal personality with aspects of partnership (the GIE, groupement d'intérêt économique, which itself served as the model for the pan-European GEE), to the very recent “simplified corporation” (SAS — Société anonyme par actions simplifiées).

Introduced in January 1994 and based on the SA, the SAS is intended to facilitate the formation of joint ventures. It must have at least two shareholders which must be corporations and meet certain size requirements. The management structure is designed to provide great flexibility, being based essentially on principles of freedom of contract. “Collective” management by shareholders may be provided for in the articles of incorporation. Addressing one of the structural weaknesses of alternative joint venture vehicles, the SAS permits greater stability and shareholder cohesion to be built into the articles through various means, such as transfer restrictions and shareholder ouster mechanisms.
Germany

Comparable to the SA and the SARL, but more modern and streamlined in structure, are the two German corporate vehicles, the Aktiengesellschaft or AG (corporation) and Gesellschaft mit beschränkter Haftung or GmbH (private company or limited liability company). As in France, all business entities in Germany are subject to the Commercial Code. In addition, specific statutes, the Corporations Act of 1965 and the Limited Liability Companies Act of 1892, govern the formation of corporations.

Aktiengesellschaft or AG

Although the AG is the vehicle of choice for large public corporations in Germany, it is possible to have a single shareholder AG. The requirement for five founder shareholders has recently been eliminated; there can now be one founder shareholder who appoints the supervisory board and the management board. There is a minimum share capital requirement of DM100,000 of which, as in France, 25% must be paid in at incorporation. All shares have a minimum par value, although it has recently been reduced to a token DM5. The corporation must issue common shares and may issue other forms of share capital. Shares are transferable and usually in bearer form.

The most distinctive features of the German corporation are the dual or two-tier board structure and the mechanisms for worker participation in management. There are two boards, the supervisory board (Aufsichtsrat) and the board of management (Vorstand).

The supervisory board’s function is to supervise, guide and advise management in the best long-term interests of the corporation. It does not have legal powers of direction or ratification as such (unless otherwise provided). In smaller corporations, all representatives on the supervisory board are appointed by the shareholders; in larger corporations, one-third to one-half of the supervisory board representatives are appointed by employees. In any event, shareholder representatives hold the balance of power on the supervisory board. The most important function of the supervisory board is to appoint and dismiss the members of the board of management.

The board of management is responsible for the day-to-day operation of the corporation. There must be at least one member of the board of management.

Shareholders play a potentially larger role in management than in the Anglo-American public company; for example, they vote on appropriation of profits and other management decisions which are submitted to them by the board of management. There may however be limits in the articles on the percentage of the total voting rights that can be exercised by any one shareholder.

Gesellschaft Mit Beschränkter Haftung or GmbH

Although there is no limit on the number of shareholders in a GmbH, the fact that the transfer of shares is restricted and that traditionally it is the form adopted by most
family businesses makes it comparable to the private company of Anglo-American law. Compared to the AG, there are fewer formalities associated with its creation and operation. For example, shareholders are entitled to waive formalities and decision making may take place by means of written resolution.

There is a requirement for a minimum share capital (DM50,000), a portion of which must be paid up at the time of incorporation. Single shareholder GmbHs are permitted.

The management structure is simpler than for an AG, with one or more individual directors (or "registered managers") acting in the place of the AG's board of management. A supervisory board is not required unless there are more than 500 employees.

European Union

In addition to numerous European Commission Directives on Company Law which are striving to harmonise national companies laws in major respects, the European Commission has for the last 25 years been unsuccessfully trying to implement a societas europea, a supra-national, pan-European company law. The model has been the French SA and the German AG, sometimes referred to as a "public limited liability company" or "PLLC".

The structural similarities to the SA and AG are fairly obvious: a minimum capital requirement (to ensure a certain size), par value shares, and 25% of capital to be paid up at the time of incorporation. Since the societas europea represents a compromise of several different national laws, it should not be surprising that certain proposals are controversial: for example, preemptive rights are mandatory (viewed by some as an impediment to capital formation) and multiple voting shares are prohibited. A requirement drawn from national law, that prohibited any one shareholder from exercising more than a certain percentage of votes, was considered and deleted.

By far the most controversial issue has been the extent of mandatory worker participation in management, an issue which pitches supporters of German national law as the model for the societas europea against the United Kingdom. The European Commission strongly supports worker participation in management as a "social right"; others view it as undermining competitiveness in industry. The current compromise provides a choice between a one-tier board or a German-style two-tier board.

The societas europea has still not seen the light of day. It has proved too difficult to establish social and political consensus within the European Union concerning the role of business in the member states. In its present state, the proposal has been criticised as deferring too greatly to national law with respect to matters of basic structure and management, resulting in substantial variation from country to country (see generally, T Blackburn, "The Societas Europa: The Evolving European Corporation Statute" (1993) 61 Fordham Law Review 695). The compromises involved in the formulation of the societas europea may have weakened the initiative's primary purpose (the creation of a form of business organization subject to a uniform European company law applicable directly in all the member states) but it is purported to have exerted a harmonising effect on national laws in areas where consensus did develop.
Part 6

Asia
Part 6

Asia

Hong Kong

Legislative History of the Companies Ordinance

Phase One: The UK Model: 1865–1932

The year 1862 marks the beginning of modern company law in the UK with the consolidation of the various enactments and amendments which resulted in the Companies Act 1862. For nearly fifty years, this statute, with numerous amendments, remained the governing companies legislation in the UK. Towards the end of the 19th century, a practice developed of reviewing, implementing and consolidating all company legislation every 20 years. This process of review and consolidation produced the Companies Acts of 1908, 1929 and 1948, after which the process broke down (see L C B Gower, Gower's Principles of Modern Company Law, 5th ed (London: Sweet & Maxwell, 1992) at 49 (Gower)).

Between 1865 and 1948, “the company law of Hong Kong could, due allowance being made for a few years time lag, be said to be almost identical with that of Great Britain” (Hong Kong, Second Report of the Companies Law Revision Committee — Company Law (12 April 1973) at 1 (the Second Report)). Hong Kong being British territory, the reasons for the similarities in the legislation during this period are fairly obvious.

The UK companies legislation during this period served as a model for many, mostly Commonwealth, jurisdictions, not just Hong Kong. “Unquestionably the limited liability company has been a major instrument in making possible the industrial and commercial developments which have occurred throughout the world” (Gower at 70). The United States had gone its own way somewhat earlier in enacting general incorporation statutes which replaced the practice of incorporation by legislative act.

Great Britain was one of the pre-eminent industrial and commercial powers in the world at this time and its companies legislation was responsive to those forces at work. It was only natural that its Companies Act, in its various formulations, should spread and flourish throughout the British Empire:

The original Companies Ordinance 1865 [HK] followed closely the original Companies Act, 1862, and (leaving aside amending Ordinances) The Companies Ordinance, 1911 [HK], followed the Companies (Consolidation) Act, 1908, and the Companies Ordinance, 1932 [HK], the Companies Act, 1929 (Second Report at 1).

For a period of over fifty years, the development of Hong Kong companies law was effectively frozen as of 1932. The “provisions of the Companies Ordinance, 1932, based
on those of the 1929 Act, were reasonably adequate under local conditions" for several years after the enactment in Britain of the Companies Act 1948 (Second Report at 2).

1. The Companies Act 1862/Companies Ordinance 1865

The UK Companies Act 1862 was a consolidation of prior legislative activity which had occurred over a nearly 20 year period, most significantly the Joint Stock Companies Registration and Regulation Act 1844 (the 1844 Act) and the Limited Liability Act 1855 (the 1855 Act). "Despite subsequent amending and consolidating Acts many of the fundamental features of the 1862 Act have survived down to modern times" (H A J Ford, R P Austin and I M Ramsay, Ford's Principles of Corporations Law, 8th ed (Sydney: Butterworths, 1997) at 43).

The 1844 Act introduced three main principles which have constituted the basis of our company law from that time. In the first place it drew a clear distinction between private partnerships and joint stock companies by providing for the registration of all new companies with more than 25 members [now 20], or with shares transferable without the consent of all the members. Secondly, it provided for incorporation by mere registration as opposed to a special Act or charter; but this it did by a system of provisional registration, which authorised the company to function for certain strictly limited preliminary purposes, followed by complete registration on filing a deed of settlement containing the prescribed particulars and other documents when for the first time the company became incorporated. Thirdly, it provided for full publicity which ever since has been regarded as the most potent safeguard against fraud. It is to this Act, too, that we owe the Registrar of Companies with whom particulars of companies' constitutions, and changes therein, and annual returns are filed (Gower at 39; footnotes omitted).

Thus, the 1844 Act conferred the privilege of incorporation (upon satisfaction of certain registration formalities) and ensured that potential investors and creditors would be able to obtain information from a public source about larger commercial enterprises. The creature created, however, was very much one caught in the process of evolution. The company form was that of the joint stock company, "an association having some of the features of a large partnership but with features from the chartered corporation added to the joint stock company" (Ford's Principles of Corporations Law at 42). The 1844 Act did not, however, provide limited liability for the company's members; rather, in keeping with the quasi-partnership nature of the joint stock company and in a manner similar to that prevailing in certain partnership regimes, the Act required creditors to exhaust their remedies against the company before proceeding against the members.

The issue of limited liability was hotly debated for over a decade before the Limited Liability Act 1855 resolved the issue, subject to subsequent refinements over the ensuing few years. Although originally envisaged as a means of facilitating the raising of capital by large-scale enterprises, its applicability to private companies was established some forty years later in the landmark case of Salomon v Salomon [1897] AC 22.

2. The consolidations of 1908 and 1929 in the UK and 1911 and 1932 in Hong Kong

The UK Consolidations of 1908 and 1929 were faithfully duplicated in Hong Kong in 1911 and 1932 respectively.
Companies (Consolidation) Act 1908. In the years subsequent to the landmark act of 1862, which clearly established limited liability, eighteen related statutes affecting company law were passed in the UK. For example:

- The Directors’ Liability Act 1890 introduced the principle of directors’ liability to pay compensation to persons who had been induced to take shares on the strength of false statements in a prospectus;
- The Companies Act 1900 contained the first provisions relating to the compulsory audit of a company’s accounts; and
- The Companies Act 1907 established the private (as opposed to public) company (with the conditions and restrictions in section 29 of the Companies Ordinance) and exempted such a company from including the balance sheet in the annual return (see generally S W Magnus and M Estrin, *Companies Law and Practice*, 5th ed (London: Butterworth’s, 1978) and T E Cain, *Charlesworth’s Company Law* (London: Stevens & Sons, 1960)).

The existence of these eighteen related acts rendered it a difficult task even for the trained lawyer to know where company law actually stood (see A F Topham and A M R Topham, *Palmer’s Company Law* (London: Stevens and Sons, 1930)). The whole was brought together under one comprehensive enactment by the Companies (Consolidation) Act 1908. In the 1908 consolidation, the government of the day made no effort to make any major substantive changes to company law; its sole objective was to consolidate and re-organise all relevant statutes that affected company law within one statute.

Companies Act 1929. As for the Companies Act 1929, “[It] was primarily a codifying Act but incorporated substantial innovations made in the law relating to companies by the Companies Act 1928. In particular, it provided for the first time for the alteration of objects, and laid down provisions as to the matters to be stated in a prospectus. It also prohibited the provision by a company of financial assistance for the purchase of its own shares and introduced the principle of redeemable preference shares and other matters relating to the capital of a company which are today commonplace. It tightened up the accounting provisions requiring a balance sheet and profit and loss account to be laid before the company every year and regulated the duties of the auditor. It also gave the Board of Trade power to investigate the affairs of a company” (Magnus and Estrin at lxxxv–vii).

Changes in company law made by the Companies Act 1929 were largely the result of recommendations made by the Wrenbury Committee in 1918 and the Greene Committee in 1926. These recommendations were in many ways the precursors of the major changes proposed by the Cohen Committee in 1945. Changes in the 1929 Act aimed primarily at: (1) improving financial reporting in order to better protect shareholders, creditors, and potential investors; (2) strengthening shareholder rights; and (3) reinforcing directors’ duties.

Under the 1929 Act, companies were obliged to keep proper books of account showing financial particulars. Moreover, they were required to keep these books available for inspection at the registered office of the company. Directors were obliged to present a profit and loss account and a balance sheet for the company’s activity at a
general meeting within one year of the holding of its last general meeting. To help ensure independent and accurate financial reporting, directors, officers, and employees of a company were prohibited from auditing the company’s accounts. Furthermore, the auditors of a company were entitled to attend and make statements at its general meeting where accounts prepared by them were to be presented (ibid). Under the Act, a company’s prospectus had to include the profits and dividends made and paid by the company in its last three financial years.

In the interests of shareholder protection, the Act also permitted dissident shareholders holding special classes of shares to apply to a court in order to cancel any variation or abrogation of their rights. As well, the Act required mandatory disclosure of interested director contracts. (See, generally, a series of articles by A Stiebel beginning with, “The Companies Act, 1929” (1929) 73 Solicitors Journal 411).

3. The opening of the gap: the Companies Act 1948 (UK)

The synchronisation of UK and Hong Kong companies law ended almost fifty years ago in 1948 and Hong Kong has been out of step with UK law since then. A “great gap”, as the Second Report put it, opened between company law in Hong Kong and in Britain.

The consolidation of 1948 in the UK incorporated many of the changes recommended by the Cohen Committee which reported in 1945. The Cohen Committee’s terms of reference were “to consider and report what major amendments are desirable in the Companies Act 1929, and, in particular, to review the requirements prescribed in regard to the formation and affairs of companies and the safeguards afforded for investors and for the public interest”. In 1945, the Cohen Committee’s recommendations largely shaped the reforms which led up to the Companies Act 1947. This Committee had two broad overall objectives: (1) to increase financial transparency in corporate affairs; and (2) to strengthen shareholder rights and control over management.

As is well-known, the Committee recommended the abolition of the ultra vires doctrine in relation to third parties, though not against shareholders. “We consider that, as now applied to companies, the ultra vires doctrine serves no positive purpose but is, on the other hand, a cause of unnecessary prolixity and vexation” (Great Britain, Board of Trade, Committee on Company Law, Report of the Committee on Company Law Amendment, Cmd 6659/45 (Chairman: Mr Justice Cohen) at 10). Unfortunately, this recommendation was not acted upon by the government of the day; the virtual abolition of the doctrine in most jurisdictions in the post-war period, even in Great Britain, is indicative of the Committee’s far-sightedness.

A large number of the Committee’s recommendations were concerned with making company financial information more readily available for shareholders and creditors (see “Company Law and Practice: The Cohen Report-I” (1945) 89 Solicitors Journal 473). With regards to the Companies Act 1929, the Committee found that a company could comply with the accounts requirement of the Act but all the same keep unsatisfactory books by ordinary accounting standards. As a consequence, the
Committee recommended that: "Every company shall cause to be kept such books of account as are necessary to exhibit a true and fair view of the state of the company's affairs to explain its transactions" ("Company Law and Practice: The Cohen Report-IX Accounts (I)" (1945) 89 Solicitors Journal 559). To this end, the Committee's report contained an extensive series of recommendations aimed at ensuring that a company's balance sheet should give a true and fair view of the state of affairs of the company. Almost all of these recommendations were implemented by the government.

Moreover, detailed recommendations regarding financial reporting in prospectuses contained in paragraphs 20 to 46 of the Committee's report were embodied in sections 61 to 68 of the Companies Act 1947. Following these changes, a company prospectus had to include the assets, liabilities and losses as well as profits and dividends, not only of the company but also of its subsidiaries. These provisions were aimed at discouraging misleading prospectuses while encouraging informed judgment as to the true value of a company's shares and its overall financial well being ("The Companies Act 1947 — (II)" 97 Solicitors Journal 616).

Following the Committee's recommendations, the Companies Act 1947 empowered shareholders in many regards: it guaranteed the holding of annual meetings; it allowed shareholders to initiate propositions at those meetings; it allowed for shareholder removal of directors; and it allowed courts greater flexibility in fashioning remedies for minority shareholders in the face of majority oppression.

Ultimately, the oppression remedy in its later formulations may very well be the most important legacy of the Cohen Committee. To strengthen minority shareholders in resisting oppression by the majority, the Cohen Committee proposed alternatives to winding up as the remedy for minority relief. Section 9 of the Companies Act 1947 permitted any member of a company who complained that its affairs were being conducted in an oppressive manner to apply to the court by petition. If the court was of the opinion that the complaint was justified, it was empowered to fashion any remedy it saw fit in order to remove the grounds of the complaint. For example, the court could make an order regulating the future conduct of the company's affairs or order the buy-out of minority shareholders (see "The Companies Act 1947— (VIII)" 98 Solicitors Journal 102).

The Cohen Committee's work ensured publication of most of the facts of interest to shareholders, and brought about great improvements in the presentation of company accounts so as to enable intelligent investors to form a better judgment of share values. Furthermore, it established what are now considered basic shareholder rights. Whatever one's opinion of the Committee, its work had a substantial impact on the evolution of company law. Many of its recommendations set the benchmark for subsequent reform in major Commonwealth jurisdictions. Many of the Cohen Committee's recommendations appeared in the 1948 UK consolidation but Hong Kong did not, as it had in the past, immediately pick up on the new UK companies legislation of 1948.
Phase 2: A Period of Legislative Stasis 1932–1984

Between 1932 and 1984, a period of over fifty years, although there were many amendments to the Hong Kong Companies Ordinance, few were of major significance. The most important amendments concerned prospectuses (1972) and accounts (1974). The provisions concerning accounts mirrored those contained in sections 147 to 156 of the Companies Act 1948, and sections 3 to 5 of the Companies Act 1967, as recommended by the Cohen and Jenkins Committees respectively.

There may be any number of reasons to account for this lack of legislative initiative, the most obvious being that the existing companies law regime was adequate to meet the demands put on it. Companies law regimes are not necessarily continuously in a process of renewal and regeneration. The modern company or corporation is a remarkably stable and, at the same time, flexible instrument. Once the basic mechanisms for incorporation are in place, companies law regimes can work without oiling for a considerable length of time.

Professor Tyler points to the instability of the political and social situation in Hong Kong in the years between 1948 and 1962 as being responsible for the failure to pick up on the 1948 legislative amendments in the UK (see E L G Tyler, “Hong Kong’s Companies Legislation Review” (December 1994) at 22 et seq [unpublished]). By 1962, however, the provisions of the 1932 Hong Kong Companies Ordinance, considered for many years to be “reasonably adequate under local conditions,” were starting to show their age. In addition, “local conditions” had changed dramatically.

These conditions have, however, since undergone great changes, and it has been clear for many years that the relatively simple provisions of the [1932] Ordinance are no longer adequate, especially in view of the vastly increased participation by members of all classes of the population in the ownership of public companies. There are therefore a great many changes which must now be made in company law in order to provide a sound basis for the proper management of the Colony’s corporate enterprises, and effective safeguards for the protection of all those who invest in them (Second Report at 3).

In light of these changes, a Companies Law Revision Committee was appointed by the Hong Kong Government in April 1962 to “consider and make recommendations as to the revision of the Company Legislation of Hong Kong, and in particular to recommend as soon as possible whether legislation for prevention of fraud in relation to investments is required and if so, the form which it should take” (Hong Kong, First Report of the Companies Law Revision Committee — The Protection of Investors (24 June 1971), at v (the First Report)). In keeping with the specific concerns evinced in its mandate with respect to investor protection, the Committee’s first report, published in 1971, was entitled The Protection of Investors. Two years later, in 1973, the Second Report on general companies law appeared.

Eleven years separated the creation of the Companies Law Revision Committee and publication of their Second Report on Company Law in Hong Kong. During this period the Committee was overtaken by a “constant succession of new developments” (First Report at vi). At one point the work of the Committee was suspended due to the
mounting pressure of work in the Registrar General's department, which was "seriously aggravated by the collapse of two banks at the beginning of 1965" (First Report, ibid) and the pending enactment of companies legislation in the UK as a result of recommendations by the Jenkins Committee in 1962. The Jenkins Committee had been assigned the task "[T]o review and report upon the provisions and working of the Companies Act, 1948, the Prevention of Fraud (Investments) Act, 1958, except in so far as it relates to industrial and provident societies and building societies, and the Registration of Business Names Act, 1916, as amended; to consider in the light of modern conditions and practices, including the practice of take-over bids, what should be the duties of directors and the rights of shareholders; and generally to recommend what changes in the law are desirable." (Board of Trade (UK), Report of the Company Law Committee (June 1962) at 1).

When reconstituted in 1968, the Hong Kong Committee turned to a detailed examination of the UK Companies Act of 1948 and 1967, in effect spanning twenty years of legislative developments in the UK. A further complication to the traditional practice in Hong Kong of swallowing UK legislation virtually whole was the fact that the UK Companies Act 1967 implemented only a small number of the recommendations of the Jenkins Committee. In addition, ancillary legislation was being spun off in the UK at a fairly furious rate. Thus the Hong Kong Companies Law Revision Committee was thrown into a full-blown exercise in law reform.

1. The second report of the Companies Law Revision Committee — Company Law

The recommendations of the 1971 First Report (most of which dealt with the prospectus requirements) were, with some modifications, enacted by the Companies (Amendment) Ordinance 1972 and the Protection of Investors Ordinance. The Second Report dealt with all other aspects of the Companies Ordinance.

The Second Report was not a conceptual overhaul of the Companies Ordinance; rather it was a detailed section-by-section tune-up, the Companies Act 1948 serving as the point of reference.

With a few exceptions we have dealt with topics in the order in which they appear in the Companies Act, 1948. This order is, we acknowledge, far from being strictly logical, but it has been convenient for us and will, we think be convenient for most professional readers and the draftsman charged with the responsibility of drafting the required legislation (Second Report at xiii).

Each section of the Ordinance was considered in light of (1) the recommendations of the Cohen Committee on the corresponding provisions in the UK Companies Act 1929; (2) changes made by the UK Companies Act 1948; (3) the recommendations made by the 1962 Jenkins Committee on the 1948 Act; (4) changes made by the UK Companies Act 1967; and (5) local considerations. The dominant influence, by far, was the UK Companies Act 1948.

The recommendations were detailed and extensive. The summary of the recommendations alone ran to 204 paragraphs. Many of the recommendations were
non-controversial, of a housekeeping or fairly technical nature designed to bring the
Ordinance into line with the 1948 UK statute. For example, it was recommended that the
Registrar of Companies should be given a discretion to extend the statutory period for
holding an annual general meeting.

Other recommendations were of far greater significance, reflecting the major
changes introduced by the 1948 UK Act and the debates of the time. Some of these
recommendations have still not been implemented. Although the Cohen Committee in
1945 had recommended abolishing the doctrine of ultra vires, the later Jenkins
Committee had retreated somewhat from this position and the Second Report
recommends following the more nuanced position of the Jenkins Committee. The
adoption of the unfairly prejudicial remedy for shareholders, introduced by section 210
of the 1948 UK statute, was recommended for Hong Kong as an alternative to the more
drastic application for winding up and made its appearance in 1978. Detailed changes,
based on the 1948 Act, to the contents and form of company accounts were
recommended. With respect to overseas incorporated companies, the Committee
recommended empowering the Hong Kong court to wind up such a company if there
were assets in the territory.

The Second Report, following the Jenkins Committee, recommended a statutory
statement of the basic principles underlying the fiduciary relationship of directors
towards their companies:

- a director of a company should observe the utmost good faith towards the company in any
  transaction with it or on its behalf and should act honestly in the exercise of his powers and
  the discharge of the duties of his office;

- a director of a company should not make use of any money or other property of the company
  or of any information acquired by virtue of his position as a director or officer of the company
to gain directly or indirectly an improper advantage for himself at the expense of the company
(Second Report at 30–31).

This recommendation has proved fairly controversial and is still under
consideration in Hong Kong. Similarly, the recommendation that insider dealing be
made a criminal offence has not been adopted. Hong Kong has preferred instead to set
up a tribunal system with administrative sanctions.

These statements are indicative, however, of the concern of the Committee for fair
dealing and the prevention of fraud.

In our comments on some of the penalties recommended we mention that there is perhaps a
tendency to treat some types of fraud less seriously than they deserve, and that persons
committing them are sometimes let off lightly on the strength of previous good character. In
many cases, however, the money lost by creditors or investors is the product of years of hard
work and self-denial, and we are most strongly of the opinion that anyone who sets out
deliberately to cheat people of their savings should be dealt with very severely, especially if
they have enjoyed, or still have the prospect of enjoying, the fruits of their knavery (Second
Report at 49).

This concern, of course, is consistent with the original mandate of the Committee to
"consider and make recommendations as to the revision of the Company Legislation of
Hong Kong, and in particular to recommend as soon as possible whether legislation for prevention of fraud in relation to investments is required . . .” (quoted in the First Report at vi).

The Committee had at the outset of the Second Report expressed reservations as to the appropriateness of continued unquestioning emulation of UK legislation in Hong Kong:

We recognize that there are considerable advantages in Hong Kong’s following closely the British law: this certainly makes things easier for lawyers and accountants since they thus obtain the benefit of the authoritative guidance of standard textbooks and decisions of the Courts in Britain, and since it is confusing for those who have qualified in Britain to find that what they have learned there is not applicable here. Nevertheless, conditions in Hong Kong are in many respects very different from those in Britain. What is best for Britain may therefore not always be best for Hong Kong (Second Report at 5).

Despite this circumspection, the Committee’s recommendations demonstrated heavy if not exclusive reliance on the UK legislative experience. The practicalities of legislative drafting prevailed and the Committee, as in the past, recommended adoption of UK legislative provisions with little or no modification.

Obviously, if our recommendations are accepted a completely new Companies Ordinance will be required, and we appreciate that the drafting of this will be a major undertaking . . . Fortunately, in many cases it will be possible for the draftsman to adopt provisions of the Companies Acts 1948 and 1967 with little or no modification (Second Report at 331).

2. The Companies (Amendment) Ordinance 1984

Between publication of the Second Report on Companies Law in 1973 and the enactment of many of its recommendations, another eleven years elapsed.

The Companies (Amendment) Ordinance 1984 has been described, only a little unfairly, as a ‘great leap forward to 1948’. In the main it does, belatedly, implement the remaining recommendations of the Second Report of the Companies Law Revision Committee published in 1973 which had largely recommended the implementation in Hong Kong of the changes made to English company law in 1948 with some variations to reflect the views expressed by the Jenkins committee in 1962 and local conditions. While some of these recommendations had already been carried into effect by various amendments, the great bulk of the recommendations (even those of a technical nature) had remained outstanding while the government struggled with the drafting problems raised by implementing the huge number of changes needed to carry the proposals into effect (C Bates, “The Companies (Amendment) Ordinance 1984” (1985) 15 Hong Kong Law Journal 167 at 167).

The process of ‘tuning-up’ the Ordinance section by section was, inevitably, long and painful.

Unfortunately, the legislative world did not stand still during this time. As Bates points out in his monograph, four new Companies Acts were enacted in the UK between the publication of the Second Report and implementation of most of its recomm—
endations in 1984. Bates’ assessment of the 1984 Amendment Ordinance was to the
effect that technical changes, although welcome, had not addressed major substantive
problems:

It is to be hoped that the amendment ordinance has cleared away the major backlog of technical
changes of this nature and that future reforms will concentrate on substantive areas where
reform is more clearly needed. Areas of more immediate concern which might be considered
are further methods to discourage nominee directors, a general review of ways to promote
greater disclosure of information to shareholders and creditors . . . , greater powers for liquidators
to set aside preferential transactions and transactions at an undervalue, and a review of the
efficacy of securities regulation and investor protection as it applies to new instruments such as
commercial paper and certificates of deposit (ibid at 113).

Phase 3: Work of the Standing Committee on Company Law Reform: 1984 to the
Present

One of the most oft-quoted statements in the Jenkins Committee report has been
that finality in companies law cannot be expected (see Second Report at 4). Taking this
observation into consideration, the Second Report, as its very last recommendation,
suggested that “there should be a Standing Committee to advise on amendments
required to the Companies Ordinance as and when experience has shown them to be
necessary” (ibid at 53). The Standing Committee on Company Law Reform was set up
in early 1984 by the Hong Kong Government and continues its work today.

Professor E L G Tyler of City University of Hong Kong is a current member of the
Standing Committee and has provided a succinct description of its constitution and
activities:

The Standing Committee is chaired by a High Court judge and consists of approximately 20
members, including the ex-officio members who are currently the Registrar of Companies, the
Official Receiver, the Commissioner of Banking [now the Monetary Authority] and a
representative of the Financial Services division [now Financial Services Branch]. The non-
official members represent the interests of the legal, accountancy and banking professions,
company secretaries, the Securities and Futures Commission, the Monetary Authority, etc,
academia, and business interests generally. There are several senior executives representing
major businesses in Hong Kong on the Committee. There is a full-time legally qualified secretary.
The Committee meets monthly or less frequently on a Saturday morning. It has never been the
practice of the Committee to initiate business nor to seek to review the Companies Ordinance
as a whole or basic principles of company law. Rather it is reactive to particular problems put
to it, which may come from the Registrar of Companies or the Official Receiver or a Government
Department or some interested member of the public. Usually the issues considered involve a
fairly narrow and discrete point of law as can be seen from the Committee’s Annual Reports
(Tyler, supra at 25).

The Standing Committee is very much an extension of the original Companies Law
Revision Committee and continues its work of detailed, point by point consideration of
the Ordinance, the fairly narrow and discrete points of law referred to by Professor
Tyler. Its mandate is to ensure that the Companies Ordinance remains responsive to the
day-to-day needs of the business sector and the community at large.
In this respect, many of the recommendations of the Standing Committee have been acted upon. The Committee monitors closely legislative developments and proposals in the UK in an attempt, as has been the practice in the past, to keep the Ordinance in line (literally, line by line) with the UK. The Companies (Amendment) Ordinance 1991 is probably of greatest significance; it implemented the current provisions concerning financial assistance, redeemable shares, purchase by a company of its own shares and distribution of profits and assets. With the exception of the financial assistance provisions (where they are applicable in Hong Kong to public companies, listed or not), the actual wording follows that of their equivalent in the UK Companies Act 1985.

Given the level of legislative activity and debate in the UK in the past 15 years, trying to keep abreast of developments in the UK is no mean feat. Between 1980 and 1989, for example, there were nearly a dozen pieces of major companies-related legislation in the UK: two major initiatives prompted by EC Directives, the Companies Act 1980 and the Companies Act 1981, as well as the Companies (Beneficial Interests) Act 1983; a partial consolidation in 1985, the Companies Act 1985 as well as the Companies Securities (Insider Dealing) Act 1985, Business Names Act 1985 and the Companies Consolidation (Consequential Provisions) Act 1985; the Company Directors Disqualification Act 1986; the Companies Act 1989 (consisting of 216 sections and 24 Schedules, again prompted by EC Directives); and the Financial Services Act 1986 and the Insolvency Act 1986. In addition to the difficulty of adapting increasingly complex and divergent UK legislation to the Hong Kong environment, there is the added complication of a series of stalled or compromised initiatives in the UK which have left the Standing Committee and Hong Kong legislators at an impasse.

Quite apart from the practical difficulties of attempting to stay abreast of a multitude of legislative developments in the UK, there is the even more difficult question which has arisen in the Standing Committee as to the appropriateness of following the UK model at all. This is not a new question and was raised in the very opening paragraphs of the Second Report in 1973. Increasingly, reference has been made in the Standing Committee to legislative initiatives in other jurisdictions, Australia, South Africa, the United States and Canada.

The Standing Committee has not confined its discussions to narrow technical issues. Especially given the increasing internationalisation of commercial activity and its significance to Hong Kong, the major debates and discussions in the area of company and commercial law worldwide have come before the Standing Committee. This fact, and the difficulties of continued reliance on UK legislation, are largely responsible for the Review of the Companies Ordinance now under way. The Standing Committee, already labouring under an increasingly heavy agenda, does not by its nature possess the resources to deal with issues arising from more fundamental developments and structural changes in the commercial world. For this reason the Standing Committee recognized the need for a broad review to be conducted on a full-time and concentrated basis (see Hong Kong, Standing Committee on Company Law Reform, Document No. 100–5).

It is difficult to overestimate the importance of the Standing Committee’s work over
the last ten years; it is equally difficult to appreciate fully the complexity and enormity of its task.

1. Major preoccupations of the standing committee

During each year of its existence the agenda of the Standing Committee has grown longer. Although not intended to be exhaustive, the following discussion highlights certain recurring issues before the Standing Committee over the last ten years, many of which have been carried over for consideration from year to year. Certain issues have found a resolution; others have only recently leapt to prominence.

**Charges.** Part III of the Companies Ordinance, “Charges”, has come before the Standing Committee in virtually every year since the Committee began meeting. Charges is an archaic and highly unsatisfactory area of the law in Hong Kong (as it is in other jurisdictions where it has not been modernised and rationalised). The situation with respect to charges is a prime example of the difficulty of following a UK model in the current legislative environment in the UK. In Hong Kong, legislation based on proposed UK legislation was on the point of being enacted. Because of vacillation on the part of the UK (the result of which has been that the Department of Trade and Industry there has essentially gone back to the drawing board), the proposed legislation in Hong Kong was orphaned, and did not proceed.

**Directors.** In the past decade, the duties, liabilities and conduct of directors have been the object of intense scrutiny around the world. It is no surprise, then, that the Standing Committee has devoted a considerable part of its energies to looking at the legislative framework in which directors must act. In keeping with recommendations of the Jenkins Committee and the situation in other jurisdictions, a statutory statement of directors’ fiduciary duties was considered and legislation introduced but ultimately passed on to the Institute of Directors, primarily at the behest of the Law Society. Liability insurance for directors and the liability of non-executive directors were considered by the Committee as well as the grounds for disqualification of company directors. Issues involving shadow directors, nominee directors and corporate directors were also examined. A public index of directors to be kept by the Companies Registrar was recommended. The troublesome issues of the prohibition of financial assistance, the repurchase of a company’s own shares, loans to directors and the distribution of profits, all closely related activities essentially controlled by directors, came up for examination year after year.

**Ultra Vires.** The unloved but remarkably tenacious doctrine of ultra vires came before the Committee on numerous occasions over the last ten years and only now seems to be close to meeting its justly deserved and long awaited demise.

**Financial Disclosure.** The availability and reliability of financial information are arguably the most important safeguards for shareholders. The form and content of the accounts required by the Companies Ordinance are generally acknowledged to be out-of-date and seriously in need of revision. The form and content of accounts have been a recurring issue before the Standing Committee. The debates have consistently argued for a complete revision of Schedule 10 (Accounts). The schedule was introduced in
1974 and raises continuing interpretation difficulties. Ancillary to the issue of the form and content of accounts is the issue of auditors' reports, another matter which has come before the Standing Committee with great regularity.

**Securities Law.** Since 1987, with increasing frequency, issues related to listed companies have come before the Standing Committee. The Hong Kong Stock Exchange and, once it came into existence in 1989, the Securities and Futures Commission, have increasingly participated in the Standing Committee's work. The Standing Committee has looked into prospectus vetting issues, insider dealing, coordination of listing rules with existing provisions of the Companies Ordinance, major and related party transactions, the Takeover Code and mandatory offers, disclosure of interest issues, proxies, clearing and settlement, and options trading, among other things.

**Compliance: Balancing the Burden.** Concerns about compliance with the statutory regime have surfaced in various guises. On the one hand, there is the issue of the regulatory burden of compliance currently placed on small business and the pressures to which the paper burden may be subjecting the Companies Registry. Concerns have also been expressed with respect to the proliferation of criminal and other offences in the Companies Ordinance. On the other hand, there have been serious demands for enforcement, if not creation, of regulatory requirements in the interests of protection of the investing public and integrity of the capital markets. There has been growing recognition of the need for a differentiation in the treatment of small business, private companies and public and listed companies. This is an issue currently under examination by the Hong Kong Society of Accountants.

**Financial Institutions.** Coincident with the rise in importance of Hong Kong as an international financial centre, the Commissioner of Banking, and more recently, its successor, the Hong Kong Monetary Authority, have participated in the deliberations of the Standing Committee. In particular, the extent to which financial institutions generally, subject as they are to the oversight of a regulatory authority, should be exempt from certain provisions of the Companies Ordinance has been discussed. Financial disclosure requirements for financial institutions have been the main issue.

**Overseas Companies.** Various factors, both political and economic, have focused attention on the inadequacy of provisions in the Companies Ordinance dealing with overseas incorporated companies. As the activities of the Hong Kong Stock Exchange and the Securities and Futures Commission have rapidly taken on greater importance, the gaps in the existing regulatory regimes, statutory and otherwise, applicable to overseas incorporated companies have become more apparent.

2. Major difficulties encountered by the standing committee

It is obvious from the Annual Reports that the Standing Committee has encountered several major difficulties over the brief period of its existence.

**Scope of its Mandate.** Modern commercial activity has become highly specialised, extremely complex and inextricably interconnected around the world. The Companies Ordinance, as the repository of much of commercial law in Hong Kong, reflects these
developments; it is one of the largest and most complex pieces of legislation in Hong Kong.

The Standing Committee on Company Law Reform has had, in effect, to cover the entire commercial waterfront: banking, insolvency, securities, security interests, accounting, and white collar crime. This is a tremendous task. Originally envisaged in 1973 in the Second Report as a small committee (of no more than five members), it has mushroomed into one of over twenty members. This has been an inevitable development given the number of the various interests concerned and the need to deploy appropriate expertise to address the issues coming before it. As the agenda of the Standing Committee has steadily lengthened and the size of the Committee increased, speedy resolution of complex issues has become more difficult.

The Difficulties with the UK Model. Undoubtedly, the greatest difficulty faced by the Standing Committee over the last ten years has been the rapidly growing irrelevance of UK legislative models for Hong Kong. Some of the reasons for this have already been discussed above.

Although the centre of intense commercial activity, both domestic and international, Hong Kong is a small jurisdiction with limited legal, legislative and judicial resources. The creation, implementation and maintenance of legal regimes is a time-consuming and costly affair. Hong Kong must borrow and adapt. In the past this was a relatively straight-forward process, aided by the political, educational and professional integration with the UK. This has long ceased to be the case and the difficulties encountered by the Standing Committee in dealing with the Companies Ordinance are indicative of this new reality.

Not only have circumstances in Hong Kong changed. In the area of commercial and companies law, the UK, for its own reasons, has experienced enormous difficulties recently in producing models worth emulating. The UK has been preoccupied with integration of its commercial law with that of continental Europe; it has not been an easy process and has absorbed considerable legislative energies that might otherwise have been devoted to modernisation and rationalisation of its legal regimes.

Companies law itself has been the object of successive and marginally successful waves of amendment over a short period of time, building in complexity and unwieldiness. By 1985, according to Professor Gower, UK “company legislation was in a worse state than at any time this century” (Gower at 51). The UK Financial Services Act 1986, with its intricate regulatory structure, has been roundly criticised; Part V, originally intended to replace the provisions of Part III of the Companies Act 1985, was never enacted. Now both parts have been repealed to be replaced by the Public Offers of Securities Regulations implementing the EC Prospectus Directive. The UK Insolvency Act 1986 was a welcome arrival on the regulatory scene but, according to Professor Gower, the voluntary winding-up of solvent companies should have remained in the companies legislation. The Insolvency Act 1986, although in some respects adopting a radically different approach, was itself to a certain degree influenced by the well-known Chapter 11 protective provisions of the US Bankruptcy Code (see J L Westbrook, “A Comparison of Bankruptcy Reorganisation in the US with the Administration Procedure
in the UK" (1990) Insolvency Law and Practice 86). Moreover, despite the Diamond Report in 1989 which recommended the adoption of a North American-style personal property security regime in the UK, legislative initiatives in this area appear to have stalled.

Even so eminent an authority as Professor Gower recommends looking elsewhere for inspiration in companies law matters:

The major questions still unresolved, and likely to remain unresolved, can really be reduced to one: Has our system of Company Law (evolved in the 19th Century) adapted itself adequately to the needs of the 20th and the likely challenges of the 21st? To suggest that it has not, may seem churlish…[O]ur system of Company Law was, until recently, the model widely followed in the Common Law countries. That leading role has now been taken over by the United States [influencing Canada, Australia and New Zealand] and we cannot hope to recover it (Gower at 70; footnotes omitted).

New Zealand has already looked elsewhere; Australia may as well; Canada did twenty-five years ago.

Given the rapidly changing and uncertain state of much of commercial law in the UK, the Standing Committee in Hong Kong has found itself unable to renew Hong Kong companies law by looking to its traditional sources.

*Interaction of a General Companies Regime with Specialised Regimes such as Banking and Securities.* The last ten years in Hong Kong have seen the emergence of specialised areas of regulation, in particular with respect to financial institutions and securities markets. These areas of specialised regulation now overlap with the older and more general provisions of the Companies Ordinance. The result has been the increasing frequency of intervention by the Stock Exchange, the Securities and Futures Commission and the Monetary Authority in the work of the Standing Committee. This has added to the complexity and sheer volume of matters coming before the Committee.

*The Role and Organisation of the Companies Registry*

The Companies Registry has also been responsive to the rapid changes occurring in the commercial world. In 1993 it assumed "Trading Fund" status; it must now be financially self-sufficient and commercially viable although the Secretary for Financial Services continues to have policy responsibilities for all aspects of the services provided by the Registry.

The Registry’s primary functions are:

- To provide arrangements to allow the promoters of companies, limited partnerships, and trust companies to easily incorporate their enterprises and to register all the documentation required to be submitted by the relevant Ordinances during the lifetimes of their enterprises.
- To capture and hold this documentation as the public record of these enterprises.
- To make the information so held available for inspection by the public.
- To ensure compliance by enterprises and their officers with their responsibilities and obligations under the relevant Ordinances.
To advise the Government on policy and legislative issues regarding company law and other related legislation.

(Companies Registry Report for the Period 1 August 1993 to 31 March 1994, at 6)

This is an ambitious mandate and the Companies Registry is struggling to meet it. In its primary function as a registry, the Companies Registry is coping valiantly with the “paper crunch” generated by recent high levels of commercial activity and the major task of implementing the transition to computerized record keeping. As to its role as a policy advisor, the Companies Registry provides the secretariat to the Standing Committee on Company Law Reform and is contributing to the Review of the Companies Ordinance.

The most difficult part of the Companies Registry’s mandate, however, is compliance and enforcement. Although it is implementing enforcement action at a rapid pace using the new striking off provisions in the Companies Ordinance, it does not have resources at its disposal comparable to those possessed by the Department of Trade and Industry in the UK.

**The Legislative Framework of the Companies Ordinance**

Like Topsy, the Companies Ordinance just grew! The Ordinance is comprised of 17 distinct parts and 15 schedules. The original 19th century outlines are still discernible but have been overgrown with amendments and adaptations to changing times.

Those members of the Standing Committee arguing “forcibly” for the creation of this Review cited the “growing size and complexity of company law” and “the piecemeal nature of the amendments” as the reasons. Over 130 years, the Ordinance has lost its original structure and coherence. Certain parts are now of only historical significance; others are comprised of no more than a section or two; still others have been superseded by regulatory initiatives outside the purview of the Ordinance. The most significant provisions with respect to basic companies law are crammed into no more than three or four parts.

**Core Company Law: the Formation, Operation and Termination of a Company**

Core company law, the provisions dealing with the formation, operation and termination of companies in Hong Kong, appear in Parts I, II, IIA, IV, IVA and V of the Ordinance. There are no separate parts dealing with shareholders generally and their rights, fundamental changes to the company structure, powers and duties of the Companies Registrar, or remedies and offences (although Schedule 12, the result of an amendment in 1990, tabulates all of the offences and the penalties).

The manner of inclusion of Parts IIA and IVA, in 1991 and 1994 respectively, indicates the difficulties now encountered in adopting UK legislation and its incorporation into the Companies Ordinance. Both Parts are virtually identical to provisions adopted in the UK, Part IIA being entitled “Distribution of Profits and
Assets” and Part IVA “Disqualification of Directors”. The provisions with respect to Distribution of Profits and Assets appear as Part VIII of the UK Companies Act 1985 but were in fact introduced somewhat earlier and influenced by the Second Company Law Directive of the EC (see Gower at 244). Disqualification of Directors provisions were introduced in the UK by way of separate legislation, the Company Directors Disqualification Act 1986. “Greater use is now being made of these salutary provisions, which go some way to make up for the fact that no qualifications are required for appointment as a director, by weeding out those who have proved to be glaringly unfit” (ibid at 146; footnote omitted). On the other hand, these provisions have attracted a lot of criticism; they are not considered to be cost effective; and the “big fish” swim free.

Parts IIA and IVA have been introduced to address perceived abuses of the corporate entity, generally impairment of capital, and concerns over the integrity and suitability of directors. Given the divergence, however, which has occurred between the statutory schemes in the UK and Hong Kong, it is no longer possible to integrate UK legislative changes in a coherent way. They must now be dropped in as satellites on their own. Sections 79A to 79P of Part IIA must be cross-referenced to Table A in Schedule 1 in the absence of clear statutory provisions with respect to the payment of dividends and other distributions. Part IVA does not enumerate all causes for disqualification of directors and must be read together with Table A of Schedule 1 as well as the older section 156 dealing with undischarged bankrupts.

Parts IV and V of the Ordinance, “Management and Administration” and “Winding Up”, demonstrate a different difficulty with the Ordinance; both Parts are lengthy, complex and overburdened by decades of legislative accretion. Each tries to do too much in what has become an erratic fashion; and each, in its own way, is paradoxically incomplete. Part V, Winding Up, is comprised of over 130 sections, or roughly a third of the Ordinance. Very little of Part V deals with winding up of a company, strictly speaking; rather, the main thrust of Part V is the creation of a rudimentary insolvency regime. Part V is supplemented by Part X, “Winding Up of Unregistered Companies”, which really deals with ringfencing assets found within the jurisdiction rather than with winding-up.

Part IV, “Management and Administration”, is another mammoth chunk of the Ordinance, comprised of approximately 140 sections of which almost half have been wedged in by way of alphanumeric amendment. It truly represents core company law, dealing as it does with accounts, directors and shareholders meetings, as well as shareholder remedies (such as they are). Again, as extensive and unruly as Part IV is, it is not comprehensive and must be supplemented by reference to other parts of the Ordinance.

Part II of the Ordinance, “Share Capital and Debentures”, despite attempts to modernise it by the inclusion of various provisions with respect to financial assistance, redeemable shares, repurchase by the company of its shares, and the creation of non-voting and disparate rights shares, is still woefully outdated and inadequate to deal with the diversity and complexity of modern financial instruments.

Finally, to end with the beginning, Part I, “Incorporation of Companies and Matters
Incidental Thereto", deals with filing formalities and has changed very little since its inception.

1. Formation of a company

Part I of the Companies Ordinance deals with "Incorporation of Companies and Matters Incidental Thereto". This Part prescribes the procedures involved in incorporation, the memorandum and articles of association, their statutory form and registration. "Private company" is defined, as is "member" or shareholder and the different forms of company (e.g., companies limited by guarantee). The treatment of pre-incorporation contracts and other formalities associated with contracting by a company are dealt with. Very little of real substance in this Part has changed since its original formulation.

The durability of Part I of the Ordinance, as indicated by the relatively few amendments over the years, is deceptive. Certainly, the registration machinery still works, and can still be made to work, as much 19th century machinery can. The real question is whether there is an easier and more cost effective way to achieve the same results, one which can profit from the advances in computerised technology and is more responsive to business needs of this century and the next.

Many of the procedures and filings associated with incorporation are relics of the 19th century which no longer serve a purpose, other than as a reminder of another time and place. The problem runs deeper, however. Continuance of these unnecessary but traditional formalities is beginning to exact a heavy toll. The Companies Registry is struggling with the burden of the mountains of paper which are being generated by the increased level of commercial activity. Added to this is the impossibility of enforcing compliance. The Companies Registry could put its energies to much better and more productive use.

Equally troublesome is the fact that retaining these 19th century structures (which generate such a massive amount of filings) impedes the adoption of simplified incorporation techniques. For example, very few jurisdictions now would quibble with the desirability of permitting the one-person corporation; it is becoming a world standard. There is little utility in persisting in the view that companies are little more than registered partnerships with legal personality and limited liability. In evolutionary terms, in the mid-19th century, that was certainly the case. It is no longer.

Part I is a rockbed of fossilized forms, of interest to the legal palaeontologist. This is the opportunity to weed the living from the dead, and perhaps introduce a new species or two.

2. Operation of a company

Parts II, IIA, IV and IVA together form the "heart" of company law in Hong Kong, dealing with capitalisation, administration, meetings, accounts, directors and officers, reorganisation and shareholders' rights.

*Capitalisation*. Part II, "Share Capital and Debentures", and Part IIA, "Distribution of Profits and Assets", deal with corporate finance matters. Part II includes the original
prospectus provisions, administration of which has now been transferred to the Securities and Futures Commission (which in turn has transferred responsibility to the Stock Exchange in the case of listed companies). Several sub-parts are of more recent origin dealing with the (controversial) financial assistance provisions; issuance, redemption and repurchase of shares by the company; provisions for the creation of different classes of shares (including non-voting shares); and provisions dealing with variation of class rights. Although an effort has been made to update these corporate finance provisions (for example, with respect to the ability of the company to repurchase its own shares and to create non-voting shares), it remains the case that the overall structure of this Part is still very much rooted in the 19th century and does not reflect the diversity and sophistication of modern financial instruments.

Part IIA, on the other hand, is of very recent vintage, dating from 1991, and introduces the concept of distributable profits and assets. The Part prohibits distribution of capital except in certain circumstances and upon meeting certain tests, essentially in the interests of creditors of the company.

Part IIA was introduced to keep the Ordinance in line with the Companies Act 1985, Part VIII. Prior to 1985:

The common law was very largely content to leave the question of the determination of profits available for distribution to companies. A brief summary of the main points illustrating this is worthwhile for the sake of comparison with the position under the Companies Act 1985. A company could distribute profits from current trading subject to deducting only revenue expenses and to setting aside a sum for depreciation in the value of circulating assets; it was able to ignore past trading losses and falls in the value of fixed assets. Similarly, previous years' profits were distributable, regardless of losses, unless capitalised. Furthermore, profits arising on the realisation or revaluation of capital assets were distributable subject to taking account of current trading losses. Arguably the law was not in accordance with good commercial practice, particularly for example in not requiring the setting aside of profit to take account of depreciation in wasting assets and in permitting an unrealised increase in the value of fixed assets to constitute profit available for dividend (A J Boyle and R Sykes, Gore-Browne on Companies, 44th ed, loose-leaf (Bristol: Jordan Publishing Ltd, 1986) at Supplement 18, 13.043).

The provisions of Part VIII of the Companies Act 1985 were themselves a response to a European Commission Directive.

Part II and IIA, “Share Capital and Debentures” and “Distribution of Profits and Assets”, are in need of rationalisation and modernisation. The emergence of sophisticated securities regulatory regimes, the innovations in corporate finance which have so marked the last decades, the complexity of corporate holdings and structures — all these factors point to the need for a rethinking of these Parts. The prospectus provisions of Part II obviously belong to the new world of securities regulation (as do the provisions of Part XII, applicable to overseas incorporated entities).

The mechanical aspects of transfer and registration should be clearly delineated from substantive issues relating to capital structure. Given developments in clearing and settlement, provision must be made for book-entry or uncertificated securities. The need for no par value shares and the rigid categories of share capital and debentures is also open to question.
**Management and Administration.** Part IV, “Management and Administration”, is the most comprehensive part of the Companies Ordinance. It deals with a wide variety of matters, some of which have been fairly extensively updated. Routine matters such as requirements as to publication of the name and registered office, the register of members and the annual return appear in this Part. Certain protections for shareholders, some of more recent origin than others, have been added in this Part by way of adjustments to shareholder communication, voting and resolutions provisions in the context of meetings and proceedings. Rudimentary protection of minority shareholders has been provided in the form of the 1948 UK formulation of the unfairly prejudicial remedy and the mandatory offer following a share repurchase which results in acquisition of 90 per cent or more of the shares of a company.

Reflecting the debates over the changing role and responsibilities of company directors and officers in recent years, the provisions of this Part dealing with directors have been amended in some significant respects. In 1984, amendments were made dealing primarily with situations of potential conflict of interest, such as loans or other payments to directors. A new part, Part IVA, of UK origin has been added to the Ordinance dealing exclusively with the disqualification of directors for fraud involving a company, conviction of indictable offences, persistent breaches of the Ordinance, and so on.

Corporate reorganisations, a complex and important part of modern corporate life, are dealt with in a most summary manner in four sections of a sub-part entitled “Arrangements and Reconstructions” with more detailed provisions appearing in Schedule 9 (Acquisition of minority shares after a successful take over offer). The section with respect to Accounts and Audits and Schedule 10, Accounts, are quite dated and in need of revisions.

Part IV, “Management and Administration”, should be split into its component parts and regrouped in a systematic fashion with Part IVA, “Disqualification of Directors”. A separate Part should address all issues pertaining to directors and officers of a company (keeping in mind that there may very well be distinctions to be drawn between directors of public companies as opposed to private companies). Technicalities such as registered office and name and register of members are better dealt with in a separate part that might also deal with the more mechanical aspects of transfer and registration of securities. Shareholders, their rights and possibly their remedies, merit separate consideration.

Auditing and accounts, too, of such great importance to shareholders, should be dealt with in a separate part. With the development of sophisticated accounting standards, both domestically and internationally, it is time to consider deferring to the professional bodies the setting of standards. There is too much flux and dynamism in accounting standards for there to be great utility in having them frozen in the Companies Ordinance. The Hong Kong Society of Accountants has studied the issue of “statutory backing” for accounting standards and, for the time being at least, has decided to no longer pursue this course of action. Of importance here as well is the overlap with other regulatory requirements, whether applicable to public or listed companies or to
companies forming part of a regulated industry such as financial services. And, finally, is it really necessary to require all private companies to have their accounts audited? Even the UK has relaxed its audit requirements, although not far enough to suit certain commentators.

With respect to investigation powers and procedures, those invoked by shareholders rightfully belong in the part dealing with shareholders; those invoked with coercive effect in the public interest might be better regrouped in a separate part dealing with offences and remedies. Some thought should be given to distilling the substance of the Twelfth Schedule, “Punishment of Offenses under this Ordinance”, which runs on for 16 pages, into more generalised categories of offences and penalties.

3. Termination of a company’s existence

Extensive and detailed provisions exist in Parts V and X concerning winding up, voluntary and involuntary, as well as the provisions of Part VI, Receivers and Managers. Much of these parts constitute, in fact, a corporate insolvency regime which goes beyond the simpler considerations of dissolution and termination of corporate existence.

Non-Core Company Law Matters

The Companies Ordinance is the repository of several areas of commercial law which are ancillary to core companies law, such as registration of charges (Part III), prospectuses (Part II, ss 37–41A, Part XII), and insolvency (Part V, Part VI). In addition there is a miscellaneous assortment of provisions, some of historical interest, with respect to former ordinances (Part VIII), continuance from a former ordinance (Part IX), dormant companies (Part XIA), offences and miscellaneous (Part XIII), evasion (Part XIII A) and saving provisions (Part XIV). Parts VII and XIII both deal with various registration matters and the Companies Registrar. Several parts govern certain aspects of the activities of unregistered companies and overseas incorporated companies (Part X, Part XI).

Certain of these non-core company matters could likely be eliminated from the Ordinance; others may more properly form the basis of a separate ordinance (eg, charges, insolvency). Still others, such as the treatment of overseas incorporated companies or registration details, could benefit from rationalisation if not complete rethinking.

Singapore

Introduction

The Companies Act of Singapore demonstrates an eclectic mix of influences and inspiration. Enacted in 1967, it is directly derived from the Malaysian Companies Act 1965. At the time it was “considered that Singapore’s new law relating to companies
should not be different from the legislation in force in Malaysia in order to facilitate trade and commercial intercourse with and within this region" (A Hicks & W Woon, The Companies Act of Singapore: An Annotation (Singapore: Butterworths, 1994) at I4). Although "the nearest equivalent remains the Malaysian Companies Act" (ibid), there seems now a marked tendency to anticipate, rather than to follow, Malaysian legislation. Commentators in Singapore consider the Singapore Companies Act to be "now very much a local product" (ibid).

Historical Background

The legislative foundation of the Singapore Companies Act is provided by the UK Companies Act of 1948. The outlines of the 1948 UK legislation are still clearly visible in the Singapore Act although the 1948 UK statute was not the model followed directly by Malaysia. Rather, Malaysia in 1965 looked to uniform companies legislation in Australia which appeared in 1961, itself based primarily on state legislation in Victoria.

So, although Malaysia has provided the structure supporting the Singapore legislation, subsequent developments, until quite recently, have been driven primarily by legislative activity in Australia. To the extent that legislative change in Australia itself has been heavily dependent upon developments in the United Kingdom, the ultimate source of much of Singapore’s companies law remained the United Kingdom.


Most of the amendments of the 1974 Act were inspired by the recommendations of the 1962 UK Jenkins Committee on Company Law Reform. Provisions were included with respect to: financial assistance for the purchase of company shares; disclosure of beneficial owners of voting shares and voting arrangements; prohibition on loans to a company or person connected with a director; prior approval of shareholders for the issuance of shares; prohibitions on the disposal of all or substantially all of the undertaking or property of the company without prior approval of shareholders; and, disclosure of interested-director contracts.

The amendments of 1984 did not have a single unifying thread although many dealt with the securities law aspects of the Companies Act, such as rights issues, prospectus signing requirements, and the broadening of the reach of insider trading provisions. A requirement was also introduced that all equity shares in public companies or their subsidiaries carry only one vote per share, irrespective of the amount paid up on such shares. The company limited by both shares and guarantee was abolished. Other new provisions included those governing the conversion of unlimited companies to limited companies and vice versa. Restrictions were placed on director resignations and provisions for automatic disqualification in certain circumstances related to insolvency and non-compliance with filing obligations were added.
In 1987, a major initiative was introduced. A system of judicial management was established, by which companies in financial difficulty could be protected from creditors, rehabilitated and restored to profitability. Although modelled directly on recently enacted UK insolvency legislation, a significant influence was Chapter 11 Bankruptcy Code protection in the United States. The accounting and audit provisions were substantially overhauled to improve disclosure and investor protection and the automatic disqualification of directors of insolvent companies was tempered and replaced by court-ordered disqualification.

In 1993, a system of scripless dealing of shares (uncertificated or book-entry securities) was introduced. Other new developments included the introduction of a statutory derivative action and certain prospectus exemptions. Additional provisions for the disqualification of directors convicted of fraud and certain other offences were implemented.

**Significant Provisions of the Singapore Companies Act**

*Directors and Officers*

There are several aspects of the Singapore Companies Act which are noteworthy. Two directors are still required to form every company, one of whom must be resident in Singapore. Unlike the current situation in Hong Kong, directors may only be natural persons. There is considerable irony in this, given that Singapore looked to the recommendations of the 1973 Report on the Hong Kong Companies Ordinance as well as the Jenkins Report for inspiration in this regard.

With respect to disqualification of directors and disclosure of interests to the company, Singapore looked to recent UK and Australian legislation. The legislative treatment of this issue between 1984 and 1987 demonstrates the tension between two forces in Singapore, one insisting on the tough enforcement of company legislation and the other promoting a more flexible regulatory environment in keeping with Singapore’s image as an international financial centre.

Initially, disqualification on the grounds that a person had been a director of two companies which went into liquidation within five years of one another, and were insolvent at the time of liquidation, was automatic. This was a highly controversial provision (see W Woon, *Company Law* (Singapore: Longman, 1988) at 155). After two and a half years, and perhaps a few hundred disqualifications, the legislature accepted that disqualification should not be automatic but rather pursuant to court order.

On the other hand, automatic disqualification of a director for “persistent default” in filing documents was not changed. The concerns leading to the enactment of this provision were twofold: firstly, 60 per cent of companies in financial difficulties did not file returns in 1984. Their directors would often resign and abandon the company, leaving nobody to whom creditors, shareholders and others who were concerned could turn. By failing to file a change of registered office, the dishonest could elude the pursuit of their creditors and evade the service of notices and summonses. Secondly, directors of
active companies would simply fail to hold annual general meetings, to lay the accounts before members and to file the annual return. They could thus evade their accountability to shareholders.

Singapore has included a statutory formulation of directors’ duties in section 157: “A director shall at all times act honestly and use reasonable diligence in the discharge of the duties of his office”. The statutory duties have not been extended to officers as they have in some other jurisdictions, but there is a broad definition of “director” which includes so-called “shadow directors”, persons “in accordance with whose directions or instructions the directors of a corporation are accustomed to act”. A broader class, which includes officers and agents, is caught by the prohibition against improper use of corporate information. The statutory provisions are expressly stated to be in addition to and not in derogation of any other “written law or rule of law”, thus continuing the applicability of common law and equitable principles.

Section 159 expressly permits directors of a company to have regard to (1) the interests of the company’s employees generally, as well as the interest of its members; and to (2) “the rulings of the Securities Industry Council on the interpretation of the principles and rules of and the practice to be followed under the Singapore Code on Take-Overs and Mergers.” The provision with respect to employees was drafted in 1974 (based on the UK Companies Bill 1973 which was not enacted).

A similar section in the UK Companies Act 1985 is directive in that it creates a duty on the part of directors to have regard for employees’ interests (in keeping with European Commission requirements). The interpretation of the section in Singapore is somewhat muddied by statements in Parliament that section 159 “serves to emphasise the duty that a company has to its employees” (see generally, Woon and Hicks, supra at V 204–205).

The topic of director compensation is also addressed in the Singapore Companies Act, although in a fairly old formulation based on disclosure. Disclosure of directors’ “emoluments” is not obligatory in all cases; rather, it is triggered by a request from either 10% in number of the company’s shareholders or the holders of 5% in nominal value of the issued share capital.

Finally, an audit committee, with members chosen from among the directors and a majority of whom must be non-executive, is mandatory for listed companies. In addition, a company secretary who is a natural person with a principal residence in Singapore is also mandatory, even for exempt private companies. Unlike the situation in Hong Kong, such persons must demonstrate qualifications to hold such a position (s 171).

Shareholder Protections

Like the Hong Kong Companies Ordinance, the statute has no discrete part or section devoted to shareholder rights and remedies; rather, they are scattered throughout the legislation. Several restrictions imposed upon the activities of directors, however, serve to protect shareholders’ interests, some of which have been noted above.
These provisions, for example, require prior shareholder approval for share issues (ss 161) which cannot be deviated from in the articles. There are measures designed to prevent asset stripping by directors, based on both the Jenkins Committee recommendations and later UK formulations of the principle (ss 160–160A). There is also a prohibition on the company making loans to directors and persons related to directors, subject to certain exemptions (ss 162–163). Certain of the exemptions require prior approval of the shareholders in order to be effective and the prohibition itself does not apply to exempt private companies.

With respect to remedies, there is a UK-style oppression remedy which dates back to 1967 but which applies to a broader class than the original formulation; in Singapore both members and debenture holders have standing (s 216).

As mentioned above, a statutory derivative remedy (based on the Canada Business Corporations Act) was implemented in 1993 by section 216A. Although not available for listed companies in Singapore, it is open to a wide class of “complainants”: any member of the company; the minister in certain circumstances; and “any other person, who, in the discretion of the Court, is a proper person to make an application under this section”. Court approval is required to proceed with the action and wide discretion is granted to the court in formulating its order (including an order requiring the company to pay reasonable legal fees and disbursements incurred by the complainant in connection with the action).

Judicial Management and Winding Up

Part X of the Companies Act, Winding Up, and new Part VIII A (introduced in 1987), Judicial Management, both rely heavily on the recent UK Insolvency Act 1986, although there are significant differences. As indicated above, Judicial Management serves either to rehabilitate an insolvent company and nurse it back to financial health or to realise its assets for the benefit of creditors without the necessity of liquidation. It is ultimately inspired by Chapter 11 protection accorded debtor companies under the US Bankruptcy Code.

Securities Regulation

As in Australia, many of the regulatory provisions concerning capital market activity of companies are found in the Companies Act in Singapore. Provisions regarding prospectuses are found in Part IV together with new provisions dealing with a book-entry system for the transfer of listed securities through a central depository. In addition, ss 213 and s 214, together with the non-statutory Singapore Code on Take-Overs and Mergers (based on the UK City Code), govern take-overs of public companies (whether listed or not).

Part IV of the Companies Act contains detailed exemptions from prospectus requirements in a variety of circumstances, many of which are drawn from North American securities legislation. Special discretionary exemptive powers are also
granted to both the Registrar under the Act and the Minister responsible for it. In particular, “international securities” to be listed in Singapore (ie, shares or debentures denominated in a currency other than Singapore dollars and issued by a foreign incorporated entity, government or international organisation (s 46(2B)), may benefit from an order permitting them to deviate from the form or content prescribed by the prospectus provisions. An exemption from a particular requirement is available only if compliance with the requirement is considered to be “unnecessary for the protection of persons who may normally be expected to buy or deal in those securities, being persons who are sufficiently expert to understand the risks involved” (s 46(2A)).

Division 7A of Part IV introduces a book-entry or scripless transfer system through a central depository for listed securities. Woon and Hicks describe the background to the introduction of Division 7A:

The Companies Act is predicated on a fundamental assumption: that the persons registered in the register of members are the members of the company, and anyone not so registered does not have any rights. Unfortunately technology has a nasty habit of not standing still and the advent of computers and computerised trading of shares has rendered that basic assumption obsolete.

Singapore has had scripless trading of securities since 1987, when the Stock Exchange of Singapore Dealing and Automated Quotation (SESDAQ) market was established. All companies listed on SESDAQ are traded on a scripless basis . . . Unfortunately, scripless trading was conducted under a statutory framework that was predicated on the existence of physical scrip. Not surprisingly, a number of legal problems arose. The Companies (Amendment) Act 1993 was passed in order to regularise the position (Hicks and Woon, supra at IV 844).

The amendments have endeavoured to rectify certain technical anomalies to ensure that holders of scripless securities are not, in effect, disenfranchised by virtue of the form in which their securities are held.

Finally, s 213 and following of the Companies Act introduces statutory requirements with respect to take-overs in addition to the non-statutory take-over code. As in other jurisdictions, the provisions attempt “to ensure that sufficient information is provided to shareholders and that the take-over is conducted fairly and in accordance with the proper standard of conduct to be expected in such situations” (ibid at VII 50–80). Of interest is the manner in which the non-statutory code has in effect been incorporated into the statutory regime:

S. 213(18)(a) The Minister . . . has specified that a non-statutory code known as the Singapore Code on Take-Overs and Mergers (referred to in this section as the Code) shall have effect in relation to take-over and merger transactions and the Code shall be administered and enforced by a body known as the Securities Industry Council.

Also of note is the scope of the take-over provisions, which could lead to wide extraterritorial application:

S. 213(1) This section, section 214 and the Tenth Schedule apply to and in relation to all natural persons, whether resident in Singapore or not and whether citizens of Singapore or not, and to all bodies corporate or unincorporate, whether incorporated or carrying on business in Singapore or not, and extend to acts done or omitted to be done outside Singapore . . .
Related to the above amendments was the introduction of the Securities Industry Act 1986 which was a direct response to the stock exchange crisis precipitated by the failure of Pan Electric Industries Limited, a publicly-listed company. The regulatory scheme existing at the time of the crisis relied upon the philosophy of self-regulation in the industry. In December 1985, the Pan-El crisis exposed the regulatory gaps and weaknesses of the then-existing regulatory frame-work. In the scramble for business, workers had indulged in margin financing and credit extension practices which went well beyond normal limits of prudence. As Pan-El was threatened with insolvency and likely to default on their contractual obligations, the Stock Exchange suspended all trading from December 2 to 4, 1985.

The resulting legislation enhanced the Government’s reserve powers, powers of direct regulation, and powers to require information and investigate. Under section 20, the Monetary Authority, a securities exchange or an aggrieved person may apply for a court order to compel observance of rules or listing rules of a securities exchange. Market intermediaries such as dealers and investment advisers must observe further requirements of “business prudence and fair trading practices”. Also introduced were capital maintenance rules for dealers. (See generally T C Choong, “Readjusting the Balance in Market Self-Regulation and Government Prudential Control — Securities Industry Act 1986” (1987) 29 Malayan Law Review 89).

*Foreign Companies*

As noted above, certain of the provisions of the Singapore Companies Act are so broadly drafted as to have an extra-territorial application. In addition, accommodations for foreign corporations participating in the Singapore capital markets are made. Part XI, Division 2, “Foreign Companies”, deals specifically with foreign companies which are required to register under the Act in order to carry on business or establish a place of business in Singapore. Much of Division 2 is fairly innocuous, dealing with the power to own land, registered offices, agents for service of process, etc.

There is however a very broad public interest power to refuse registration:

S. 369(1) . . . the Registrar shall refuse to register a company under this Division if he is satisfied that the foreign company is being used or is likely to be used for an unlawful purpose or for purposes prejudicial to public peace, welfare or good order in Singapore or is acting or is likely to act against the national security or interest.

In addition, although there are numerous grounds upon which the requirement may be waived or modified, a registered foreign company which is not required by the law of its place of incorporation to hold an annual general meeting or prepare audited accounts is obligated to make such filings in Singapore.

*General Observations*

The Singapore Companies Act has retained the general structure of UK-inspired companies legislation. Accordingly, in the same legislation archaic vestiges such as wide “powers” clauses co-exist alongside very new indigenous approaches to local
issues. Very obvious attempts have been made to rapidly adapt the legislation to changing times. The latest legislative developments in the United Kingdom and Australia are mirrored in various parts of the statute. In addition, particularly in the area of securities and shareholder protection, very marked North American influences are discernible.

The reliance on Australian and UK companies law developments has been declining in recent years in Singapore. "The Act has been amended ten times since it came into force. The more recent amendments tend to be 'home-grown'" (Woon and Hicks, supra at I4). This independent-mindedness of the Singapore legislature actually dates back to the early days of the legislation. Singapore enacted in 1974 many of the suggestions of the 1962 UK Jenkins Committee which did not survive bill form in 1973 in the United Kingdom.

There are also indications in the statute that certain of these "home-grown" provisions may in fact be the result of the adaptation of North American approaches to local circumstances. For example, the statutory requirement introduced in 1989, making it mandatory for a listed company to have an audit committee, is a listing requirement of major stock exchanges in the United States and a statutory requirement for many public corporations in Canada. The statutory derivative action which appeared in the Singapore Act in 1993 is taken from the Canada Business Corporations Act.

The use of prescriptive legal rules, statutory requirements, rather than non-legal regulation based on the formulation of broad principles (the London City Code on Takeovers and Mergers being a prime example), is also indicative of a shift away from UK-based models to North American approaches. Critics might point to this trend as one towards over-regulation. Particularly in the areas where there is an overlap with securities regulation, such as the regulation of takeover bids, this movement is evident in Australia as well (see H A J Ford, R P Austin and I M Ramsay, Ford’s Principles of Corporations Law, 8th ed (Sydney: Butterworths, 1997) at 940 et seq.)

The Singapore Companies Act, like the Hong Kong Companies Ordinance, "has been amended a dozen times on an ad hoc basis with no underlying philosophy evident. Most of these amendments are ‘issue-driven’, ie, in response to some problem or potential problem" (Letter of Professor W Woon to C Jordan 7 July 1995). A review of the Singapore Companies Act began in July 1995 “with a view to (I hope) rationalisation and refinement” (ibid). Although Australian law, a traditional source of Singapore law, will be taken into account in the review, it was not anticipated that Singapore would look to the Australian simplification efforts as “the Australians expanded their original 1960 uniform legislation into a monster, something that we have not done” (ibid).

People’s Republic of China

Introduction

On July 1, 1994 the Company Law of the People’s Republic of China (PRC) came into effect. Although there are no reliable statistics available, it has been estimated that
since its implementation there have been approximately 12,000 “joint stock limited liability companies” (comparable to public companies) and 10,000 “limited liability companies” (comparable to private companies) formed under the legislation.

The introduction of company law in the PRC has been said to constitute a “‘quiet revolution’ in Chinese society” (A Qian, “Riding Two Horses: Corporatizing Enterprises and the Emerging Securities Regulatory Regime in China” (1993) 12 Pacific Basin Law Journal 62 at 64). It was not so very long ago that “the Chinese government forbade any discussion concerning the establishment of shareholding companies, issuance of stocks to the public, or opening of stock exchanges” (ibid at 62).

The development of a company law in the PRC, for political, ideological and legal reasons, has been controversial. It has followed a long, slow and winding path which begins with the economic reforms initiated in 1978. At that time, “there was no need for such legislation because almost all industrial entities were state-owned and were covered by legislation on state enterprises” (P M Torbert, “China’s Evolving Company Legislation: A Status Report” (1993) 14 Northwestern Journal of International Law and Business 1 at 1). The journey is not over.

The Company Law grew out of and to a large measure now supersedes a variety of local laws relating to the organisation and ongoing administration of companies and other enterprises in the PRC. Special laws applicable to various forms of enterprises with foreign participation remain in place and supplement the Company Law (art18).

As in other countries with a civil law tradition, the concept of “legal person” which forms part of the new Civil Code (introduced in the PRC in 1986) predates and interacts with Company Law. Article 36 and following of the Civil Code define a legal person as an “organization that possesses capacity to acquire civil rights and competence to perform civil acts, and that, according to the law, may independently assume civil rights and bear civil liability” (see H R Zheng, China’s Civil and Commercial Law (Singapore: Butterworths, 1988) at 311).

The concept of legal personality is well developed in the civil law tradition, applying to a broad range of associations, including but not limited to, business corporations. The significance of the concept resides in the fact that it endows the entity to which it attaches with legal capacity; for example, the ability to contract and to sue and be sued. Legal personality does not necessarily imply limited liability. In the civil law, partnerships may be endowed with legal personality, for example, but that does not automatically protect the individual partners from civil liability.

So despite the fact that the Company Law, as such, did not appear until 1994, the concept of legal person already existed in the PRC, nurtured by Chinese jurists by reference to civil law jurisprudence even before the promulgation of the Civil Code (see Zheng, supra at 310–311). State-owned and collective enterprises are legal persons under the Civil Code.

Despite the somewhat misleading nomenclature which appears in some English translations, it is important when considering the Company Law to keep in mind the fact that its ultimate source and inspiration is primarily the civil law tradition of continental Europe (Germany in particular), as well as the civilian tradition which has manifested
itself in Asia (Japan and Taiwan). The civil law tradition is evident in both the form and
the substance of the Company Law. The drafting style is that of the great civil code
traditions, with its emphasis on simplicity, clarity and the statement of general principle.
In structure and concept the two forms of company created by the PRC Company Law
show the influences of the German AG and GmbH and, more indirectly, the French SA
and SARL described above.

Historical Background

Pre-1949 China

Historically, the first company law in China appeared in 1904; it was in fact the
“first modern law drafted by the Imperial Codification Commission, whose work was
part of the Qing government’s reformist ‘new policies’ in the wake of the recent
humiliations at the hands of Japan and the Western powers. In giving the highest priority
to enacting a law governing the organisation of commercial companies, the Qing
government had several interlocking objectives” (W Kirby, “China Unincorporated:
of Asian Studies 43). A primary objective was the desire to promote and control modern
telegraph company. The company form which this created was a hybrid of Japanese (which itself
had borrowed liberally from German sources) and English laws in an abridged form
(ibid at 47). The 1904 law was replaced in 1914 by a new ordinance which borrowed
much more directly from German commercial law which included a “true corporation”
(ibid at 49). After 1949, the “entire Republican legal system, including Company Law,
was abolished” (ibid at 56).

Factors Precipitating the Introduction of PRC Company Law

1. Political/economic

Without the tremendous economic changes that resulted from the change in
political leadership in the late 1970s, there would be now no Company Law in the PRC.
In December 1978, the Third Plenary Session of the 11th Central Committee of the
Communist Party of China simultaneously launched a policy of economic reform and
opened the PRC to increased contacts with the outside world.

Since then, the PRC has been reforming, inter alia, its highly centralised and unitary
banking and financial structure. Economic reform created an urgent need to build up the
PRCs financial markets. The economy grew rapidly, as did the corresponding capital
requirements of the country’s various localities and enterprises. However, capital
requirements could not be met due to the state’s limited financial resources. The PRC,
thus, began to explore setting up financial markets (Qian, supra at 65–66). The creation
of capital markets, however, forced the issue of creating a shareholding system.

A fierce debate raged over many years about the creation of a shareholding system,
the system of enterprise ownership and property rights being the two most difficult
issues to resolve.
Early in 1979, right after the Third Plenary Session of the CPC, the Central Committee called for the implementation of Deng Xiaoping's economic reform and open-door policies, only a few scholars challenged or questioned the existing socialist all-people's ownership. At that time, almost nobody talked about establishing a shareholding system or issuing and trading stocks (ibid at 73).

At the outset of the debate, two poles emerged. One suggested the establishment of a shareholding system uniquely adapted to the PRC (ibid at 76), the other arguing that as “the product of capitalist social production, that socialist enterprises issuing shares will change the nature of socialism, and that stock speculation will occur in the stock market so that a minority of people may become a new rich class that makes a good living through stock speculation” (ibid).

In the later stages of the debate, theoretical difficulties with respect to the concept of property rights and ownership were addressed and, in large measure due to the difficulties presented by the low-productivity and desperate need for capital of state-owned enterprises, a consensus developed that reform of the “mechanisms of operation and management in the enterprises” was necessary.

Thus, the driving force behind the Company Law is the restructuring or transformation of state-owned enterprises into a shareholding system with the state remaining the majority shareholder.

The ongoing process may be better characterized as corporatization, where a former state-owned enterprise is restructured into a corporation that has some division of ownership and management, more in line with international corporate management norms. Thus, there may be less emphasis on the social welfare of enterprise employees and more stress on the profit interests of its owners, mainly its shareholders (ibid at 92).

This is the quiet revolution that Qian refers to as creating a “hybrid composition of public, collective, and private ownership in one single shareholding enterprise entity” (ibid at 63). Thus the goal is to separate the ownership and management of state-owned enterprises, making them independent entities responsible for their own profit and loss in the market. The 10-year trial period carried out in selected state-owned enterprises manifested tremendous vitality in the market economy and accelerated the pace for establishing a modern enterprise system. Market reforms, a modern enterprise system, corporatisation and the creation of stock markets all interacted to create interesting economic synergies for the PRC.

2. The open door swings both ways

Just as domestic economic reform contributed to the need for the corporate vehicle, so did the open-door policy which coincided with the economic reforms. In their search for capital, Chinese companies are seeking to list and trade their securities outside the PRC. Although governments and state-owned enterprises of many countries have been raising money outside their domestic markets for decades, the pressures of the international markets has driven inexorably towards a standardisation of vehicle and product.
It would be a safe assumption that the desire to participate in the international capital markets was a spur to the transformation of large numbers of state-owned enterprises into "companies" more as we know them. The creation of a consistent standard and more internationally recognisable form of enterprise makes enterprises created or continued under the Company Law more acceptable to foreign regulators (such as stock exchanges) and investors alike.

Equally, the interest of foreign enterprises to enter the Chinese marketplace via the "incubators" of the Special Economic Zones led to the development of corporate vehicles to facilitate foreign investment in the PRC. The Guangdong Corporation Law, for example, applied only to Sino-foreign stock corporations established in the three Special Economic Zones in Guangdong Province. This was the first comprehensive corporation law in the PRC, and an experiment. Like other measures, it was viewed as essentially transitional in nature, serving to explore "a feasible legislative approach" (Zheng, supra at 365).

In keeping with the incremental approach of the PRC government to change, the Company Law of 1994 has built primarily, among other measures, on the Guangdong Corporation Law. The provisions relating to the creation, as well as the organisation and management of the Sino-foreign stock corporation, have been incorporated into the new Company Law. "It will increase opportunities for active foreign investment, and provide a legal framework for it that more closely resembles what investors find in other jurisdictions around the world" (P M Torbert, "China's New Company Law: Foreign Investment Issues" (15 August 1994) East Asian Executive Reports 7 at 7).

In searching to develop internationally accepted norms for their Companies Law, the PRC translated and referenced for drafting the companies legislation of Britain, the United States, Germany, Japan, France, etc. Jurists who had studied in these jurisdictions joined together in the drafting and review of the legislation. Given the large choice of models and options presented, those considered the most suitable for conditions in the PRC were adopted. Much heavier reliance was placed on Japanese and continental European models than on any other single source in terms of the structure and orientation of the resulting legislation.

**Significant Characteristics of the Company Law of the People's Republic of China**

There are two kinds of entities created by the Company Law, the joint stock limited company (also translated as company limited by shares) and the limited liability company. (It should be noted at the outset that the author of this book has been working with three different English translations of the legislation, all of which differ in detail.) Both entities are legal persons and thus subject to the provisions of the Civil Code. The main significance of this is that they are endowed with legal capacity as discussed above, and their relations with third parties will be governed by the Civil Code. Both entities are liable for their debts to the extent of their assets; and they are to operate independently and be responsible for their own profits and losses.

The limited liability company corresponds roughly to the private company, the
GmbH or SARL. It must have at least two but no more than 50 members. It must have a minimum registered capital, which in certain circumstances varies with the activity of the company. The capital must be paid up (and verified) at the time of subscription. The provisions dealing with paid-up capital are unusually detailed and demonstrate the great concern of the PRC with respect to the protection of creditors. Continental European corporate legislation tends to be more creditor protective than the common law and it is thus not surprising that its influences are apparent here.

The limited liability company does not issue shares but rather capital contribution certificates. There are restrictions on the withdrawal of capital and the transfer of capital contributions. Flexibility is provided to the extent that annual general meetings of shareholders and, for small companies, a board of directors, may be dispensed with. A great many matters may be dealt with in the articles of association.

The shareholders' meeting has much broader powers than that usual in the Anglo-American tradition. It can, among other things: decide on the business policy and investment plan of the company; elect and recall directors and decide on their remuneration; elect and recall supervisors representing shareholders on the supervisory board (discussed below); examine and approve the budget; adopt resolutions on the issuance of company bonds; and exercise many more direct powers of management. The extensive powers granted to shareholders are consistent with a regime where the line between ownership and management is not yet a clear one. This is a transitional phase where state appointed managers share the same interests as the state shareholder.

It is in the management structure of the limited liability company that the adaptation of the German model to PRC circumstances is most apparent. Day-to-day operations continue to be delegated to a "manager" (as in the pre-company law days) by a board of directors which oversees operations. In smaller companies, the board of directors may be replaced by an executive director who may also assume the role of the manager. Where there is significant state ownership, the board of directors must include representatives of the staff and workers of the company. Relatively larger enterprises must, in addition, have a supervisory board (the well-known German dual board structure) representing shareholders, staff and workers. Shareholder representatives maintain the balance of power on the supervisory board. Unlike the continental European supervisory board, the supervisory board in the PRC is dominated by the shareholders. In the tradition of the French labour council (see Part V above), in certain matters of direct interest to them, workers and staff, as well as trade unions, must be consulted in advance and their opinions solicited.

There are prohibitions on acting as a director, supervisor or manager of a company, some of which echo recent developments in other jurisdictions. Persons convicted of certain kinds of crimes, those responsible for bankruptcy liquidation of a company within 3 years, etc. are disqualified. There are strict prohibitions on self-dealing and conflicts of interest for directors and managers. These prohibitions are very much inspired by the severe fiduciary-like duties imposed in Anglo-American law and jurisprudence on directors (rather than the laxer European standard associated with the legal concept of mandate).
In fact, the statutory standard imposed in the PRC is arguably much stricter than that prevailing in most of the common law world. In addition to explicit prohibitions (for example, against taking bribes), there is a more generalised statutory duty imposed on directors, supervisors and the manager to "comply with the articles of association of the company, faithfully perform their duties and maintain the interests of the company and...not take advantage of their position, functions and powers in the company to seek personal gains" (art 59). Finally, wholly state-owned enterprises may be organised as limited liability companies, with certain adaptations. They do not have shareholders meetings, but do have a board and manager.

The joint stock limited company in structure more closely resembles the public company, the AG or SA of continental law, with the capital raised by either "sponsorship" or offer to the public. Different rules apply to each method. Where there is an offer to the public, prospectus and other investor protection rules apply. In order to promote the stability of an enterprise, promoters are required to hold not less than 35 per cent of the total shares issued by the company.

There is a one-vote, one-share rule, provisions for proxies, and super-majority voting requirements for amendment to the articles of association. There are provisions incorporated by reference or similar to those applicable to the limited liability company with respect to powers of the board of directors, the appointment and powers of a general manager, consultations with the labour council and directors' duties and disqualification. The supervisory board is mandatory for joint stock limited companies and provisions for its duties and disqualification of its members are incorporated by reference from those applicable to limited liability companies.

In addition, separate parts of the Company Law deal with: the issue and transfer of shares and bonds; merger and division; bankruptcy, dissolution and liquidation; branches of foreign companies; and legal liability (including the creation of criminal offences).

**General Observations**

The Company Law is viewed as a first step. In certain respects it is simply not as comprehensive or as detailed as the Japanese or German models upon which it draws heavily. There are few statutory protections offered to minority shareholders and the merger and acquisitions provisions are rudimentary at best. However, given the still dominant role of the state as shareholder, this lack of protection is understandable. The potential for conflict arising from the dual role of the state as administrator and enterprise owner is expected to diminish over time as the two roles diverge. Most commentators expect that the difficulties that have arisen in this transitional period will be overcome.

The Company Law shows an astute adaptation of company law principles from around the world. In style and in much of its substance, it is in keeping with the PRC's civil law tradition. Measures promoting the protection of creditors, the dual board structure, labour councils and co-determination have been easily adapted to suit the
‚socialist market economy‘ (art 1) which is being developed. In other areas, such as
strict fiduciary-like duties for directors, managers and supervisors, ideas borrowed from
the Anglo-American tradition, the PRC has gone beyond their original sources and
raised these standards of conduct. Although some archaic principles are retained, such
as par value shares and a minimum of two shareholders for private companies, in most
respects (for example, the possibility for uncertificated securities) the Company Law
has picked up on some very modern notions.
Part 7

Bermuda
Part 7

Bermuda

Introduction

Bermuda has been included in this Survey for one reason. Over 40 per cent of companies currently listed on the Stock Exchange of Hong Kong are incorporated in Bermuda. The reasons for this astonishingly high figure and its implications for Hong Kong will be examined in greater detail later in this Review.

Bermuda, like Delaware, has created a local industry catering to incorporations for off-shore business. A UK-style statute, the Companies Act 1981 (BCA), has been tailored to some very specific uses. In fact, the familiar terrain of the UK memorandum of association company is deceptive. On the one hand, North American influences strongly mark the legislation; on the other, the legislation has been developed in close cooperation with industry and demonstrates a pragmatic and particularised approach.

Bermuda is a popular center for international business. Despite its small size (population approximately 60,000), it has parlayed its natural beauty and political stability into the basis of a healthy economy oriented toward tourism and international business. The attractions of the first may explain Bermuda's attractiveness for the second; customs duties account for a surprising 40 per cent of government income; while the remainder is filled out by company and vehicle licensing fees, stamp duties, and some taxes (on land and the tourist industry for the most part). The Bermudian government has a payroll tax payable by all employers in varying percentages with certain optional arrangements made available to exempted company employers. There is also a Corporate Services tax payable by those who render services to international business currently assessed at 4 per cent of the gross income derived (again with a myriad of exceptions and variations) but otherwise income, profits, and capital gains are not taxed. When the tax situation is combined with relative ease of incorporation, air links to Europe and North America (Bermuda is approximately 90 minutes flight time from New York City), excellent communications infrastructure, minimal regulatory burden, and Government policy that actively fosters foreign investment in exempted undertakings (see infra), the Colony's popularity as a jurisdiction for incorporation becomes clear.

The Bermuda Companies Act 1981 provides for three main types of company. These are:

- Local Companies: these are incorporated in Bermuda, and have the power to do business in the Colony and abroad. Non-Bermudian ownership is limited to 40 per cent.
- Exempted Companies: these are incorporated in Bermuda, for the purpose of carrying on business outside the Colony; they are generally prohibited from doing business in
Bermuda with entities other than exempted companies. They are also prohibited from acquiring or holding land in Bermuda other than that leased to meet business requirements (the leases in question must be for a maximum of 21 years). Furthermore, without the prior consent of the Minister of Finance (which is readily forthcoming), they may not acquire or hold mortgages in Bermudian land over BDS$50,000, debentures or bonds securing Bermudian land (save those issued by public utilities), or shares or interests in Bermudian companies or other entities (other than exempted undertakings). There are requirements for minimum capital, and a quorum of directors (usually two) must be resident in Bermuda.

- Permit Companies: these are companies incorporated outside Bermuda that do business outside Bermuda from a place of business within Bermuda. These are less frequent, although the required licence is readily granted where it can be shown that the use of a Bermudian company would be inappropriate, for example shipping companies incorporated in Liberia or Panama. The Bermuda government does however favour the use of the exempted undertaking for these purposes.

The tax situation for exempted companies deserves a brief mention of its own: the Exempted Undertakings Tax Protection Act 1966 provides that exempted undertakings can obtain exemption from any future Bermudian tax on profits, income, or capital gain, assets, or appreciation up until March 28, 2016. This exemption is normally applied for on incorporation. Exempted companies are also subject to the requirement that they file on an annual basis with the registrar a declaration stating the company’s principal business and the company’s capital situation.

As a place of incorporation, Bermuda demonstrates some very particular characteristics. First of all, since the early 1920s when company legislation was introduced, incorporation in Bermuda has been a privilege, subject to the discretion of the Bermuda Monetary Authority (BMA). Bermuda takes care to promote a “squeaky-clean” image with respect to its incorporation business in part to foster its offshore reinsurance industry which requires a reputable foreign jurisdiction of incorporation. In addition, the use of Bermuda as a place of incorporation for off-shore business does not permit the enterprise to carry on business in Bermuda although it does entail, in some respects, a significant (and expensive) Bermudian presence.

Secondly, controls on foreign investment in Bermuda-based businesses are very strict. “Local” Bermudian companies (that may do business both in Bermuda and abroad) must be 60 per cent owned by Bermudians. Given the small population and the exclusivity of Bermudian residence requirements, this puts Bermudian business under very tight local control.

For purposes of this Survey, the distinction between “exempted”, “permit” and “non-exempted” companies is of the greatest interest. Briefly, exempted companies are the principal form of company incorporated in Bermuda for the purpose of doing business outside Bermuda. Because of the significant costs involved and the fairly onerous requirements associated with incorporation, for Hong Kong — based businesses Bermuda has been primarily a jurisdiction of choice for only major public enterprises. For small or closely-held businesses, the British Virgin Islands have
provided an alternative. There is a considerable competition for the offshore incorporation business among various jurisdictions.

**Significant Provisions of the Bermuda Companies Act 1981**

*Corporate Form and Constitution*

The Bermudian government is concerned with ensuring that companies incorporated in its jurisdiction meet certain basic standards; the BMA is its principal agent of corporate quality control. The approval of the BMA is required for the incorporation of any company. This approval is discretionary; furthermore, on certain limited grounds set forth in the statute, the Registrar may refuse to register a company, although this refusal may be appealed to the Minister. Before granting approval for the incorporation of an exempted undertaking, the BMA requires bank references relating to the “ultimate beneficiaries” of the exempted company. The requirements are quite extensive; for individuals, they include names, addresses, nationality, and occupation, plus statement of financial standing and any other available information concerning the individual’s integrity, from a bank with which the individual has dealt for a minimum of three years. For corporations, a banking reference, most recent financial statements, and a complete and detailed list of shareholders are required.

Unsurprisingly given Bermuda’s British colonial status, the BCA is a memorandum of association statute. Thus, its theoretical model of the corporation is contractarian, rather than a North American statutory division of powers model. The contents of the memorandum may affect the governance of the company to a somewhat larger degree than does the corporate constitution of a company in a jurisdiction with a North American-model statute.

Rather at odds with the contractarian model, but indicative of both the pragmatic approach and the desire to meet international expectations, the minimum number of subscribers to the memorandum is one. A copy is kept on file with the Registrar of Companies; it is a public document, and is available for viewing by the general public. The memorandum must state the following requirements, which are set forth at BCA s 6:

- the name of the company (including the usual requirement that limited companies include the word “Limited” as the last word of the name),
- its objects,
- the names, addresses, and nationalities of the subscribers,
- the exempted or non-exempted status of the company,
- the land holding powers of the company,
- the period of the company’s duration or dissolution-triggering events, if any,
- proposed share capital, amount of minimum subscription, and division thereof into shares, and
- undertakings by the subscribers to take up their share allotments and to satisfy any calls made in respect of those shares.
The BCA does not distinguish between publicly traded companies and private or close companies in terms of governance or other requirements, aside from a prospectus requirement for public issuers at BCA s 26.

The First Schedule to the BCA sets out powers available to companies incorporated under it; these are possessed by all companies unless excluded in their memoranda. These powers may be exercised outside the frontiers of Bermuda to the extent that other jurisdictions permit. As well, companies are empowered to do anything else that is "... incidental or conducive to the attainment of the objects and the exercise of the powers of the company". The Second Schedule sets out certain objects available to companies limited by shares or possessing a share capital; these must be included by reference in their memoranda. Among these objects are:

- insurance,
- packaging,
- buying, selling, and dealing in goods,
- design and manufacturing,
- mining, prospecting, processing, transportation and the like of mineral resources and petroleum products,
- research and development,
- land, sea, and air carriage of passengers or goods, the construction, operation, management, ownership, and the like of ships and aircraft, and related undertakings,
- engineering,
- consultation,
- agriculture and the processing of agricultural products,
- acquisition and investment in patents, trademarks, and the like,
- trading in conveyances,
- operating personnel agencies,
- trading in real or personal property,
- acting as guarantor or surety, with or without consideration.

It must be noted that BCA ss 129, 129A and 144 place restrictions on the powers of exempted companies. Unless provided otherwise by Act or memorandum an exempted company generally may not do business or hold interests in real property in Bermuda, with a few exceptions. Exempted undertakings may not:

- hold land in Bermuda save land required for its business, by lease not to exceed twenty-one years,
- hold mortgages in Bermuda with a value of greater than BD$50,000, save with permission of the Minister,
- hold any Bermudian bonds and debentures save those issued by the Government or another public authority,
- acquire any shares or interest in a Bermudian business or undertaking with the exception of exempted undertakings,
- enter into contracts or exercise other corporate powers in Bermuda save that which is necessary for the conduct of its extra-Bermudian business (BCA s 129).

Other exceptions include reinsurance for Bermudian companies, acting as manager,
agent, or consultant for another exempted undertaking, and conveyance by ships, subject to the restrictions set out at BCA s 129. BCA s 129 provides that breach of these restrictions can lead to escheat of the property involved under the Escheats Act 1871.

The declaration of dividends or distribution out of contributed surplus is conditional on two alternative tests, set out in BCA s 54(1). The dividend declaration or surplus distribution may not be made unless the company will remain able to pay its liabilities as they come due, or that the realizable value of the company’s assets will not become less than the aggregate of its liabilities and its issued share capital and share premium accounts. BCA s 13(3)(ix), (xvii) provides that the bylaws may also set additional restrictions on dividends and distributions.

BCA s 77 provides a non-mandatory presumption that one share carries one vote at general meetings of companies limited by shares. This may be varied by the memorandum or bylaws. Votes may be given in person or by proxy. Where the shareholder is a corporation, BCA s 78 permits it to authorise another person to act at its representative at general or class meetings. As well, provisions for special voting rights in the event of amalgamations are set out at BCA s 106(3); any share carries the right to vote on such transactions.

The BCA does not provide for North American style unanimous shareholder agreements. It does, however, provide at s 74 that holders of a minimum 10 per cent interest may require the directors to call a special general meeting; the request must state the purpose of the meeting. Should the directors refuse or fail to call the meeting, the requisitioning shareholders may call the meeting themselves, and will be entitled to reimbursement for any reasonable expenses incurred. As well, any director or member of the company, where it is impracticable to call a meeting in the required manner, may apply to the Court under BCA s 76 to have it order a meeting.

Mergers and mandatory share exchanges are covered by Part VII, Arrangements, Reconstructions, and Amalgamations, of the BCA. Consent of the Minister is required for any amalgamation, under the provisions of BCA s 104 and there must be a statutory declaration as to the solvency of the amalgamated company. Companies proposing to amalgamate must enter into an agreement detailing the terms of the proposed merger.

The amalgamation agreement must then be submitted to the shareholders of each amalgamating company, which is to take place at a general meeting of each company. The requirements concerning such meetings are set out at BCA s 106. The notice of the meeting is to include a copy of the agreement, and state the fair value of the shares as determined by the company and the fact that dissenting shareholders are entitled to be paid such fair value. BCA s 106 also carries a special voting provision; all shares carry the right to vote on amalgamations whether or not they carry other voting rights, and classes are entitled to a class vote if the amalgamation agreement will vary the rights of that class. There is a suppletive supermajority requirement of 75 per cent of votes in order to approve the transaction, but the bylaws may modify this.

An appraisal remedy is available for dissenting shareholders: provided that the shareholder did not vote in favour of the amalgamation, an application may be made to the Court for an appraisal. The Court’s decision in such an action may not be appealed.
Upon judgment in favour of the shareholder, the company has the following options:
- to pay the dissenting shareholder the fair value of his shares as determined by the Court, or,
- where the amalgamation agreement so provides, to terminate the amalgamation, or,
- where the amalgamation has already taken place and the shareholder has received some consideration, to pay the shareholder the difference between this and the Court’s appraisal.

BCA s 107 provides a short form amalgamation procedure for amalgamations involving wholly-owned subsidiaries.

The BCA also provides for mandatory share exchanges in s 102. These provisions operate in the context of a share transfer plan or contract entered into with another company. There is a requirement that the holders of 90 per cent of the value and 75 per cent of the shares involved approve of the transaction, and dissenting shareholders may apply to the Court for relief; no specific remedies are detailed.

The BCA contains no provisions on takeovers nor any special provisions concerning sales of all or substantially all assets, although the memorandum may include such provisions. Thus, a company is suppletively presumed to be able to dispose of all or substantially all of its assets in the normal course of business, subject to any relevant provisions in the memorandum or bylaws.

Part XIII of the BCA provides for the winding-up of Bermudian companies. It is by far the largest Part of the BCA, spanning ss 157–264. Section 157 provides that winding-up may be either voluntary or by the Court.

BCA s 161 covers the eventualities in which a judicial winding-up may take place. These are:
- the company has resolved that it be judicially wound up, or
- there is failure to comply with the requirement that financial statements and auditor’s reports be presented to the annual general meeting, unless the company follows the waiving procedure set out in s 88, or
- the company does not begin its business within a year of incorporation or suspends its business for a year, or
- the company is unable to pay its debts, or
- material misstatement was used to obtain ministerial consent, or
- the Court finds that it would be just and equitable to wind up the company.

BCA s 163 provides that an application for judicial winding-up shall be made by petition by any combination of creditors or contributories, present, contingent, or otherwise, subject to the following requirements:
- if the petitioner is a contributory, he must have held his shares in some way for a minimum of 6 months or inherited them, or,
- if the petition is on the ground of default to hold the statutory meeting, the petitioner must be a member, and the petitioner must allow the company a two-week grace period after the last possible day on which the meeting could be held before applying to the court.

BCA s 201 provides for the voluntary winding-up of companies. Companies may be
wound up either when the duration provided for in its memorandum or incorporating act occurs, or by resolution in general meeting. The winding-up takes effect at the time of the resolution or triggering event; from this moment, termed "commencement of winding-up", the company must cease doing any business save that necessary for the winding-up. In the event of a voluntary winding up, the company must publish notice of the winding-up in an appointed newspaper.

In the event of a voluntary winding-up, each director must make and deliver under BCA s 206 to the registrar a statutory declaration within the five weeks preceding the resolution or triggering event to the effect that it is his opinion that the company is solvent. If such a declaration is filed, the winding-up is termed a "members’ voluntary winding-up"; if not, it is termed a "creditors’ voluntary winding-up". BCA ss 207–214 and ss 215–223 contain provisions governing each of these, respectively.

Shareholder Rights and Remedies

In flavour, the provisions of the BCA dealing with shareholders rights are very North American. The BCA does not contain any specific provisions on shareholder preemptive rights on new share issues, although there is nothing to prevent incorporators from providing for such in the memorandum or bylaws. Neither does the BCA contain any special provisions for cumulative voting. Voting to elect directors, as for any other matters that may come up, is presumed by BCA s 77(2) to be by simple majority, unless the bylaws provide otherwise. BCA s 70 requires that the first general meeting of the company be held to elect directors; this meeting follows the same procedure as a regular general meeting. Once the first board is elected, failure to hold an election or general meeting does not disqualify them; BCA s 73 states that it is lawful for them to continue in office in the event that an annual general election or election does not occur. BCA s 91 provides for specifics as to the election of directors; the only mandatory requirement is that the board be constituted of at least two persons who must be individuals. The bylaws may provide for any other such details as election or appointment requirements, term of office, and the like.

There is no provision in the BCA for statutory derivative actions; the common-law derivative action is all that is available. The BCA does, however, provide at s 111 for an oppression remedy and the Court is broadly empowered to make "... such order as it sees fit..." (s 111(2)) in order to remedy the situation.

Although there is no specific section on appraisal remedies in the BCA, appraisal remedies are provided in the relevant sections for amalgamations, mandatory share transfers, and to a certain extent, alterations to the memorandum. The oppression remedy at BCA s 111 may of course be an option in cases where an appraisal remedy is unavailable.

Directors’ Duties and Liabilities

The board of directors must consist of at least two individuals who must be elected at the first general meeting, and each subsequent annual general meeting, or elected or appointed in the manner and for the term provided for in the bylaws. Alternate directors
may be appointed, and any vacancies on the board may be filled by the remaining directors, provided that quorum exists and that the bylaws do not provide otherwise. In addition to a secretary (s 92), under the BCA all companies must have the following officers:

- a president or chairman
- a vice-president or deputy chairman,
- any other officers as may be provided for (s 91).

The president, vice-president or chairman, and deputy chairman must be directors; there is no such requirement for any other directors.

Exempted undertakings are subject to the requirement that a quorum of non-alternate directors be ordinarily resident in Bermuda. Exempted companies which are listed on certain stock exchanges may in lieu of the resident director requirement appoint an ordinarily resident individual as their resident representative, whose duties include the maintenance of all corporate records, the making of all filings, and keeping proof of the company’s being listed on an approved exchange. Failure by the company to comply with these requirements grants the right to the Minister to revoke the exemption; failure by the representative to comply is an offence under BCA s 130(4) punishable by a maximum fine of BDS$5,000.

The BCA does not contain any specific provisions codifying the duty of care applicable to directors. It does, however, contain a statement of the duty of care applicable to officers of the company (s 97) which includes directors. This section provides that officers shall in the discharge of their duties and exercise of their powers, always act honestly and in good faith with a view to the best interests of the company, and exercise the care, diligence, and skill that a reasonable person would exercise in the same circumstances.

Certain actions are deemed to be breaches of this duty:

- failure to disclose upon request by the auditors the full details of any benefit the officer has or is to receive from the company or any of its subsidiaries, or
- failure to disclose upon request by the auditors the full details of any loan the officer is to receive from the company or any of its subsidiaries, or
- failure to disclose at the first opportunity, either in writing or at a meeting, the officer’s interest in any material contract, material or proposed, with the company or any of its subsidiaries, or
- failure to disclose the officer’s material interest (10 per cent or greater) in any entity to such a contract (s 97(4)).

The BCA’s codification of the conflict of interest rules can be found at s 97(4) which only applies to officers and takes the form of a deemed breach of the duty of care.

Again, the BCA does not contain any specific provisions concerning the insurance by the company of its directors. However, companies may, either in bylaws or by contract, exempt an officer from or indemnify the officer for any loss or liability stemming from any "... negligence, default, breach of duty or breach of trust ..." committed with regard to the company or any of its subsidiaries. This does not extend to "... wilful negligence, wilful default, fraud, or dishonesty". Any clause purporting to
exempt or indemnify the officer for such a breach of duty is voided by BCA s 98(2). Notwithstanding this, s 92(2)(b) nevertheless permits the company to indemnify the officer for any proceedings in which judgment is given in the officer’s favour, or in which the Court grants the officer relief under BCA s 281.

**General Observations**

The Bermuda companies legislation has been successful in accomplishing its aims. It is rather like Darwin’s finches, an example of highly specialised evolution to suit a niche environment. Its success may be attributed to its focused approach to the goals which it wishes to attain and a high degree of responsiveness to and consultation with its end users.
Part 8

Conclusion
Part 8

Conclusion

A Period of Transition for UK-Style Companies Legislation

Company law in the United Kingdom has been undergoing a difficult period of transition and instability over the last 15 years. Nearly a dozen major statutory initiatives associated with companies law have been introduced or attempted in the United Kingdom, and in some instances, introduced, attempted and withdrawn. The prime motor for this high level of legislative activity has been the imposition of European Commission Directives which have their source in the civil law tradition. The difficulties that have ensued go beyond those involved in simply adapting civil law concepts to the very different legal tradition in the United Kingdom; there are profound divergences of political and social views, particularly with respect to the relationship between management and labour.

As Professor Gower sadly notes, UK companies legislation is no longer in a state to serve as a model to other jurisdictions. Commonwealth and other jurisdictions which have traditionally relied heavily on the UK as the source of their company law have deliberately broken away or been orphaned. Canada made the break over twenty years ago; the resulting federal legislation used the US Model Business Corporations Act as its starting point. Onto this American stalk was grafted the then most highly desirable aspects of UK companies law. Although showing its age somewhat and currently the subject of a comprehensive review (primarily as a result of the shifting boundaries between companies law and securities regulation), the Canada Business Corporations Act is still a highly regarded corporate law regime.

New Zealand, in implementing the Companies Act 1993, has openly turned to North American models, much as Canada did before it. The New Zealand legislation has suffered more compromises during the legislative process and has had a more difficult birth. Given the already well-established separation in New Zealand of securities law from company law in 1978, there is little doubt however of the future direction of New Zealand companies law. The use of North American judicial decisions to interpret the statute may be eased by the recent decision to consider eliminating appeals to the Privy Council from New Zealand courts.

Australia, for many reasons, began a major company law reform initiative in 1993 which has been proceeding rapidly apace. Form has determined substance in Australia; simplification of the form of the legislation has turned to consideration of the introduction of new concepts and substantive approaches. In terms of the future direction of Australian corporate law, the jurisdictions considered to be of most direct relevance now are, first, Canada and second, the United States.
Jurisdictions as different as Singapore, South Africa and the PRC have turned to solutions and approaches developed in other jurisdictions. South Africa, as a mixed civil law/common law jurisdiction, is an interesting case in point. The North American influences on the South African Close Corporations Act of 1984 are quite obvious; the European civil law influences may be more subtle. In looking to Malaysia and Australia as its traditional sources of companies law, Singapore was in fact indirectly modelling its legislation on that of the UK. Over time however Singapore did not hesitate to look elsewhere for solutions to problem areas, in doing so, adapting them to local circumstances. The result has been a rather eclectic and fairly indigenous mix, but with more pronounced North American overtones of late. The PRC has looked everywhere (including the UK), but, in keeping with the European civil law roots of its Western legal tradition, primarily to civil law jurisdictions.

**Diversity of Company Law Regimes**

In companies and corporate law, there is certainly an embarrassment of riches in terms of approach, even within the common law tradition. North America alone has over 60 different corporate law regimes, some of which are highly distinctive and quite idiosyncratic although most show a good deal of similarity in structure and fundamentals.

As the North American and the European experience has shown, the existence of a multiplicity of corporate law regimes in the same business community, region or country (usually the result of a particular political imperative) is not necessarily a bad thing. Much has been written in the United States about competition among state jurisdictions for incorporations but the dire predictions about a “race to the bottom” have, in reality, not materialised. Although there are notable exceptions (Delaware and the many small off-shore incorporation jurisdictions), usually companies law serves primarily local interests. It has a local face. There are not the same pressures towards uniform international standards which have manifested themselves, for example, in banking or capital markets regulation.

This situation, a diversity of existing legal regimes and the absence of strong international pressures towards harmonisation, permits great latitude in crafting a companies law regime. Singapore and the PRC, for example, have shown fairly eclectic taste in fashioning their companies law. Bermuda’s very specialised forms of incorporation have been highly tailored to suit local circumstances and foster the local economy. Despite a Memorandum of Understanding between Australia and New Zealand concerning harmonisation of commercial law, New Zealand did not feel overly compelled to coordinate its new approach to companies law with that in Australia.

However, some care should be taken in the degree to which a jurisdiction mixes and matches. Generally speaking, a great divide still exists in the common law world between the UK approach to companies law and that in North America. An even greater gulf stretches between the continental approach and that of the common law world. It is certainly possible to draw, successfully, on different legal traditions in creating a
statutory framework in any particular area; jurisdictions such as South Africa and Canada, which share in common both the civil law and common law traditions, have done so. The UK is having a more difficult time of it, with the forced imposition of alien concepts on a somewhat reluctant legal profession and business community.

The danger, of course, is producing an elephant designed by a committee. Even the generally successful Canadian experience of using a US structure to give support to certain UK concepts, has shown signs of the stresses produced. As the statute aged, some of the most heavily criticised provisions, those concerning the financial assistance and the oppression remedy, have proved to be of UK origin.

**Meeting International Expectations**

Although there are not compelling reasons leading to homogeneity in companies law throughout the world, nonetheless, there are identifiable trends creating international expectations, if not international standards. Companies law regimes no longer operate in domestic isolation but are constantly the subject of comparison in international business transactions.

Law reform bodies are looking to other jurisdictions in making their proposals; the Australian Simplification Task Force has several people assigned watching briefs as to developments in overseas jurisdictions. The PRC and Singapore have been opportunistic in seizing on and adapting foreign concepts. Commonwealth jurisdictions have for many years looked to each other for legislative approaches. Jurisdictions specialising in off-shore incorporation are niche players carefully assessing market demand and tailoring their legislation to meet it. Introduction of one foreign legal concept may subsequently pull in whole legislative regimes with repercussions extending beyond the original horizons.
Appendices

Appendix I  European Commission Directives implemented by UK Legislation — the Company and its Incorporation
Appendix II  Essentials of Alice Springs Agreement
Appendix III  Cross-Sectional Survey of (Revised) Model Business Corporations Act
Appendix I

The Company and its Incorporation

Table of European Commission directives which have been implemented by UK legislation

<table>
<thead>
<tr>
<th>Number</th>
<th>Subject</th>
<th>Enacted By</th>
<th>Current Reference</th>
</tr>
</thead>
<tbody>
<tr>
<td>First</td>
<td>Corporate powers and representation</td>
<td>European Communities Act 1972, s 9, CA 1980</td>
<td>CA 1985, ss 35–35B, 36C, 42</td>
</tr>
<tr>
<td>Second</td>
<td>Capital requirements</td>
<td>CA 1980</td>
<td>CA 1985, passim</td>
</tr>
<tr>
<td>Third</td>
<td>Mergers</td>
<td>SI 1987/1991</td>
<td>CA 1985, Sch 15</td>
</tr>
<tr>
<td>Fourth</td>
<td>Accounts</td>
<td>CA 1981</td>
<td>CA 1985, Pt VII, Schs 4, 5</td>
</tr>
<tr>
<td>Sixth</td>
<td>Demergers</td>
<td>SI 1987/1991</td>
<td>CA 1985, Sch 15</td>
</tr>
<tr>
<td>—</td>
<td>Admission to listing</td>
<td>SI 1984/716</td>
<td>FSA 1986, Pt IV</td>
</tr>
<tr>
<td>—</td>
<td>Listing particulars</td>
<td>SI 1984/716</td>
<td>FSA 1986, Pt IV</td>
</tr>
<tr>
<td>—</td>
<td>Continuing disclosure</td>
<td>SI 1984/716</td>
<td>FSA 1986, Pt IV</td>
</tr>
<tr>
<td>UCITS</td>
<td>Collective investment schemes</td>
<td>FSA 1986</td>
<td>FSA 1986, s 86</td>
</tr>
<tr>
<td>Seventh</td>
<td>Consolidated accounts</td>
<td>CA 1989</td>
<td>CA 1985, Pt VII, Sch 4A</td>
</tr>
<tr>
<td>Eighth</td>
<td>Qualification of auditors</td>
<td>CA 1989</td>
<td>CA 1989, Pt II, Schs 11–14</td>
</tr>
<tr>
<td>—</td>
<td>Mutual recognition of listing particulars</td>
<td>FSA 1986 amendments</td>
<td>FSA 1986 and the “Yellow Book”</td>
</tr>
<tr>
<td>Appendix</td>
<td>Mutual recognition of prospectuses</td>
<td>Amendments to Yellow Book</td>
<td>Yellow Book</td>
</tr>
<tr>
<td>---</td>
<td>---</td>
<td>---</td>
<td>---</td>
</tr>
<tr>
<td>90/211</td>
<td>Major acquisitions and dispositions</td>
<td>SI 1993/819</td>
<td>CA 1985, Pt VI</td>
</tr>
<tr>
<td>88/677</td>
<td>Prospectuses</td>
<td>SI 1995/1537</td>
<td>SI 1995/1537</td>
</tr>
<tr>
<td>89/592</td>
<td>Branches</td>
<td>SI 1992/3179</td>
<td>CA 1985, s 690A and Sch 21A</td>
</tr>
<tr>
<td>Eleventh 89/666</td>
<td>Single-member companies</td>
<td>SI 1992/1699</td>
<td>CA 1985, s 1(3A), etc.</td>
</tr>
</tbody>
</table>
Appendix II

Essentials of Alice Springs Agreement

- The Corporations Act and the Australian Securities Commission Act were to be amended by the Commonwealth so as to become laws for the Australian Capital Territory.
- Each State would enact application legislation adopting by reference the ACT law as amended from time to time.
- The applied law would have the characteristics and status for all practical purposes of Commonwealth rather than State law.
- The ASC would replace the NCSC and State Corporate Affairs Commissioners as the sole administrative authority in this area, and the Commonwealth would compensate the States for the loss of revenues resulting from this assumption of authority.
- The ASC would become formally accountable to the Commonwealth Attorney General and the Commonwealth Parliament.
- The ASC and Commonwealth criminal-law enforcement authorities (ie the Federal Police and Commonwealth Director of Public Prosecutions) would replace the State authorities in this area.
- The Ministerial Council, renamed the Ministerial Council for Corporations, would be reconstituted with the Commonwealth Attorney General as permanent chairperson and continue its supervisory role over the ASC. Furthermore, the Commonwealth would have four votes and a casting vote, while the States and the Northern Territory received one vote each.
- The Ministerial Council would be consulted on amendments to companies and securities law, but its approval would not be required for legislative proposals for the national markets (ie with regard to takeovers, securities, public fundraising, and futures).
- Building societies, friendly societies, cooperatives, credit unions, State statutory corporations and incorporated associations would not come under the purview of the new legislative scheme but would remain subject to State authority.
Appendix III


A. Corporate Form and Constitution

Issue 1: Reservation of Power by State

The RMBCA provides that the state reserves the “power to amend or repeal all or part of this Act at any time and all domestic and foreign corporations subject to this Act are governed by the amendment or repeal” (RMBCA 1.02). This provision has its origin in American constitutional law. Article I section 10 of the American Constitution states that “no state shall . . . pass any law impairing the obligation of contracts”. Pursuant to the Supreme Court decision in Trustees of Dartmouth College v Woodward (1819) 4 Wheat 518, a state may avoid possible arguments that a corporation has contractual or vested rights in statutory provisions which are later amended by including such a provision in its corporate statute.

Both Delaware and New York have substantially the same provision as the RMBCA (8 Del C 394 (1991); NY Const art X, 1 (McKinney, 1994)).

Issue 2: Articles of Incorporation

The RMBCA sets out both minimum mandatory requirements for all articles of incorporation (name of corporation; number of authorized shares; address of corporation’s initial registered office and agent; name and address of each incorporator) and enabling ones (including purposes and powers of corporation; par value for authorized shares or classes of shares; imposition of personal liability on shareholders for the debts of the corporation to a specified extent and upon specified conditions) (RMBCA 2.02(a) (mandatory provisions); 2.02(b) (enabling provisions)).

An important new provision in this section was added in 1990 in response partly to a notorious decision of the Delaware Supreme Court, Smith v Van Gorkom 488 A 2d 858 (Del SC 1985), and partly to the concurrent insurance crisis for directors’ and officers’ liability in the United States (RMBCA 2.02(b)(4)). This provision, inspired by a similar provision enacted in 1986 by the Delaware legislature, enables a corporation to limit the liability of its directors to the corporation for money damages arising from negligent conduct. As has been pointed out by many critics, states which adopt this kind of provision pave the way for a significant weakening of directors’ duty of care (cf D Branson, “Recent Changes to the Model Business Corporation Act: Death Knells for Main Street Corporation Law” (1993) 72 Nebraska Law Review 259 at 270 ff
[hereinafter 2 Branson]. But see, contra, Note, "Limiting Corporate Directors’ Liability: Delaware’s Section 102(b)(7) and the Erosion of the Directors’ Duty of Care" (1987) 136 University of Pennsylvania Law Review 239 which suggests that such provisions may have very limited effects, in that they do not protect actions of directors acting *qua* officers and in that plaintiffs will tend now to recast their claims in terms of a breach of a director’s duty of loyalty. However, for discussion of the concurrent weakening of directors’ duty of loyalty in contemporary American corporate law statutes, see (1) Branson *supra* as referred to in Part 4 of this survey, as well as (2) Branson, *supra* at 268 ff.

Both Delaware (*cf* previous paragraph) and New York have provisions substantially the same as those of the RMBCA with regard to articles of incorporation, including the provision limiting directors’ liability to the corporation for negligence (8 Del C ss 101–102 (1991); NY Bus Corp Law ss 401–402 (McKinney, 1994)).

**Issue 3: Purposes**

The RMBCA provides that every corporation has the purpose of engaging in any lawful business unless the corporations’ articles expressly state otherwise (RMBCA 3.01(a)).

Legislation containing provisions that permit the formation of corporations for any lawful purpose have a very long history in the United States, reaching back to legislation passed by the state of Connecticut in 1837.

If the shareholders of the corporation chose to limit corporate purposes, it should be noted that the RMBCA limits the operation of the doctrine of *ultra vires* to corporate insiders and the doctrine does not affect third parties acting in good faith with a restricted purpose corporation (RMBCA 3.04). Both Delaware and New York have substantially the same provisions (8 Del C ss 101, 121–123 (1991); NY Bus Corp Law ss 201–202 (McKinney, 1994)).

**Issue 4 Authorization and Issuance of Shares**

The RMBCA states that the articles of incorporation must prescribe the classes of shares and the number of shares of each class that the corporation is authorized to issue. If more than one class of shares is authorized, the articles of incorporation must prescribe a distinguishing designation for each.

In addition, the articles of incorporation must authorize one or more classes of shares that together have unlimited voting rights, as well as one or more classes that together are entitled to receive the net assets of the corporation upon dissolution.

The section dealing with authorized shares in the RMBCA also provides an option to authorize one or more classes of shares in the articles of incorporation that:
- have limited, conditional or no voting rights;
- are redeemable or convertible with or without reference to an extrinsic event;
- entitle the holders to non-cumulative, partially cumulative, or cumulative dividends;
or

• have preferences over other classes of shares with regard to distributions.

Both Delaware and New York law is similar, although they retain the somewhat awkward concept of legal capital (8 Del C s 151 (1991); NY Bus Corp Law ss 501, 502, 512, 519 (McKinney, 1994)). In 1975, California led the way in dropping the requirement that corporations include in their articles of incorporation references to the par value of shares (See B Manning, Legal Capital (Westbury: Foundation Press, 1981) at 164). The RMBCA soon followed suit in 1980.

**Issue 5: Limited Liability of Shareholders**

The RMBCA states that a purchaser of shares from a corporation is liable only for payment of the consideration for which the shares were authorized to be issued or that specified in the subscription agreement. The same section provides however that a shareholder may be personally liable “by reason of his own acts or conduct”, thereby keeping the door open for an application by the courts of the common law doctrine of “piercing the corporate veil” (RMBCA 6.22(b)).

The earliest American statutes dealing with limited liability of shareholders capped liability at an amount equal to (yet over and above) the consideration originally paid for them by the shareholder (in effect a “double liability”). These statutes were repealed during the early part of the twentieth century.

Delaware law is substantially the same as the RMBCA (8 Del C s 162 (1991)). New York law, on the other hand, creates an exception such that the top ten shareholders of a corporation are potentially liable for wages owed to employees of the corporation (implicit in NY Bus Corp Law ss 628–630 (McKinney, 1994)).

**Issue 6: Restrictions on Share Transfers**

The RMBCA provisions allow restrictions on the transfer of shares to be imposed either in a corporation’s articles of incorporation, its bylaws, by means of an agreement between shareholders, or between shareholders and the corporation. It may:

• be imposed for any reasonable purpose;
• obligate the transferor to first offer the corporation an opportunity to acquire the restricted shares;
• obligate the corporation to acquire the shares;
• require the corporation to approve the transfer of the restricted shares; or
• prohibit the transfer of restricted shares to designated persons or classes of persons.

These last two stipulations will only be possible where manifestly reasonable.

Such restrictions are enforceable against third parties only where they are noted conspicuously on the share certificate (RMBCA 6.27(a)–(d)).

Delaware law has substantially the same provision (8 Del C s 202 (1991)). New York law has no equivalent provision.
Issue 7: Distributions to Shareholders

The RMBCA enables a corporation to make distributions to its shareholders at the discretion of its board of directors. However, their exercise of discretion is subject to a determination to be made of the corporation's financial state by means of both an equity insolvency test and a balance sheet test (RMBCA 6.40(c)(2)).

The insolvency test is formulated such that no distribution may take place if the corporation would not be able to pay its debts as they become due in the usual course of business. The balance sheet test is formulated such that no distribution may be made if the corporation's total assets would be less than the sum of its total liabilities plus (and what follows is a mere presumption only) the amount that would be needed, if the corporation were to be dissolved at the time of the distribution, to satisfy the preferential rights upon dissolution of shareholders with preferred shares.

The RMBCA provisions in this section apply equally to the acquisition by the corporation of its own shares, with the exception of a specific rule regarding the time for measuring the effect of a distribution (RMBCA 6.40(c)(2)).

A corporation's indebtedness to a shareholder incurred by reason of a legal distribution will rank at parity with the corporation's indebtedness to its unsecured creditors (RMBCA 6.40(f)).

As noted under the rubric of Issue 4, the 1980 revisions of the MBCA did away with distinctions such as "stated capital" and "capital surplus" along with requirements for statements of share par values. Both Delaware and New York retain legal capital regimes. Under both states' laws, dividends and repurchases of stock are treated separately: the power to distribute dividends is pegged to capital surplus or net profits; and the power to repurchase stock is pegged to capital impairment. In New York, an insolvency test also figures as an element of the formula allowing for valid distributions and stock repurchases (8 Del C ss 154, 160(a)–(b), 170–173, 243, 244 (1991); NY Bus Corp Law ss 510, 511, 513, 515–517 (McKinney, 1994)).

New York also has a special provision making a corporation liable to its shareholders for failure to make disclosures and give notices pursuant to its dividend and distribution provisions (NY Bus Corp Law s 520 (McKinney, 1994)).

Issue 8: Voting Entitlement

The RMBCA creates a non-mandatory presumption of the principle of one share one vote at shareholders' meetings, and imposes the mandatory principle that only shareholders are allowed to vote (RMBCA 7.21(a)).

This section also prohibits the voting of shares held by a domestic or foreign corporation that is a majority-owned subsidiary of the corporation whose voting shares are in question (RMBCA 7.21(b)). This practice is also called "circular voting". Such a provision is aimed at preventing management from using a corporate investment to perpetuate its own control over the parent corporation. Shares held by the corporation in a fiduciary capacity are however exempted from the rule prohibiting circular voting (RMBCA 7.21(c)).
Appendix

Delaware and New York have different provisions from the RMBCA. While the principle of shareholders-voting is the suppletive norm, voting rights can be given in the corporation’s articles of incorporation to bondholders (8 Del C ss 160(c)-(d), 212(a), 221 (1991); NY Bus Corp Law ss 501, 518(c), 612, 613 (McKinney, 1994)).

Issue 9: Unanimous Shareholder Agreements

The RMBCA section dealing with unanimous shareholder agreements is one of its newest provisions, having made its first appearance in 1992 (RMBCA 7.32). This section validates for non-public corporations various types of agreements among shareholders even when such agreements are inconsistent with many of the mandatory requirements of the RMBCA (RMBCA 7.32(d)). In this way it provides a corporation interested in running its affairs as a close corporation with the alternative of incorporating under the provisions of an “integrated” close corporation Act.

The American Bar Association has in fact provided its own version of such an integrated Act in the form of the Model Statutory Close Corporation Supplement (Reprinted in Vol 4 Revised Model Business Corporation Act Annotated (1993) at 1803–1880) [hereinafter MSCCS]. This piece of model legislation, unlike the unanimous shareholder agreement section of the RMBCA, limits the size of a corporation to 50 shareholders as a prerequisite for opting into its provisions (MSCCS 3(b)).

In an article examining the comparative advantages and disadvantages of enacting integrated close corporation Acts, Siedel concludes that there is no overwhelming need for the integrated approach (G Siedel, “Close Corporation Law: Michigan, Delaware and the Model Act” (1987) 11 Delaware Journal of Corporate Law 383 at 432). Close corporations in jurisdictions without integrated Acts can use the provisions of general corporation Acts equally effectively to maximize flexibility, minimize legal formality, and avoid shareholder oppression. Nor are integrated Acts, despite appearances, any less cumbersome to use than general Acts. In fact, Siedel finds that in practice the contrary is more likely the case.

The RMBCA section on shareholder agreements allows corporations, once such agreements are unanimously approved by its shareholders, to set forth in their articles of incorporation or bylaws provisions which, for example: eliminate the board of directors or restrict the discretion or powers of the board of directors; govern the authorization or making of distributions, even those that are not in proportion to share ownership (subject to limitations on distributions by making them post-requisite to both an insolvency and a balance-sheet test); establish who shall be directors or officers of the corporation, their terms of office or manner of selection or removal; govern the division of voting power between the shareholders and directors as well as amongst themselves; establish the terms and conditions of any agreement for the transfer or use of property or the provision of services between the corporation and any shareholder, director, officer or employee of the corporation; transfer to one or more shareholders or other persons the authority to exercise the corporate powers (ie the directors’ functions) or to manage the affairs of the corporation; require dissolution of the corporation at the request of one
or more of the shareholders or upon the occurrence of a contingency (RMBCA 7.32(a)(1)–(7)).

Another provision reaffirms the principle of limited liability for shareholders. This shields shareholders from personal liability from the debts and acts of the corporation, even if the unanimous shareholder agreement in effect creates an organizational structure analogous in other ways to a partnership (RMBCA 7.32(f)).

Delaware uses an integrated approach to close corporations which is substantially the same as the MSCCS (8 Del C ss 341-356 (1991)). The New York Act on the other hand contains a provision substantially the same as section 7.32 of the RMBCA, although the enabling parts of it containing the permissible substantive content of such agreements are less detailed (NY Bus Corp Law ss 620(b)–(g) (McKinney, 1994)).

**Issue 10: Amendment of Articles of Incorporation and Bylaws**

The RMBCA enables a corporation to amend its articles of incorporation at any time. No vested proprietary interests accrue to shareholders as a result of any provisions contained in the articles (RMBCA 10.01(a)–(b)).

Unless the articles of corporation provide otherwise, the board of directors can without shareholder approval amend the articles with respect to matters which are merely routine or housekeeping in nature, such as deleting names and addresses of the initial directors, or extending the duration of the corporation if it was incorporated at a time when limited duration was required by law (RMBCA 10.02)

In all other cases, amendments to the articles of incorporation are to be initiated by the board of directors and approved:
- by a majority of all shareholders;
- by a majority of the holders of shares of any voting group that would give rise to dissenters rights if the amendment were adopted;
- by groups affected by the amendment in the manner described at section 10.04 and in accordance with a procedure set out elsewhere in the RMBCA concerning voting groups, whether or not the articles of incorporation in fact provided that the affected shares are voting shares; or
- by any requisite supermajority vote as mandated by the RMBCA, the articles of incorporation or the board action initiating the amendment.

Under the RMBCA provisions, a corporation’s board of directors and shareholders have shared jurisdiction to amend or repeal its bylaws. This suppletive rule can be altered by the articles of incorporation or by the shareholder action initiating the bylaw amendment in order to reserve this power in favour of the shareholders alone. The directors on the other hand can never effect a like reservation of power (RMBCA 10).

Both Delaware and New York law are substantially the same as the RMBCA provisions, with a few exceptions. First, Delaware, unlike both the Model Act and New York, does not provide for unilateral amendment by the corporation’s board of directors with respect to non substantive matters. Second, both jurisdictions reverse the presumption of shared power of the board of directors and shareholders to amend
corporate bylaws, vesting this power instead in the shareholders alone, subject to an opting-out provision in the articles of incorporation (Delaware) (8 Del C s 109 (1991) or in either the articles of incorporation or the bylaws (New York) (NY Bus Corp Law s 601 (McKinney, 1994)).

Issue 11: Mergers and Mandatory Share Exchanges

Under the provisions of the Model Act, a corporation may enter into a merger or a mandatory share exchange with another corporation. Mergers and share exchanges are initiated by the board of directors of a corporation in the form of a plan. The plans are then submitted to shareholders for approval.

The plan must set forth the name of each corporation merging and the name of the surviving corporation, or the name of the corporation whose shares will be acquired and the name of the acquiring corporation; the terms and conditions of the merger or exchange; and the manner and basis of converting or exchanging the shares of each corporation into shares, obligations, cash or property.

As described above in connection with our discussion of amendment procedure under Issue 10, such action is subject to any relevant voting group structure or any supermajority vote requirement imposed by the RMBCA, by its articles of incorporation, or by the board's plan of action (See RMBCA II).

Delaware law concerning mergers is substantially the same as the RMBCA, but has no provisions concerning mandatory share exchanges (8 Del C s 251 (1991)).

New York has substantially the same type of enabling provisions for both mergers and share exchanges, but differs with respect to its procedure for shareholder approval: two-thirds, not a mere majority, of all of the voting shares and a majority of each class of voting shares is required. There is no provision allowing a corporation to opt out of the two-thirds requirement (NY Bus Corp Law ss 901–903, 913 (McKinney, 1994)).

Issue 12: Sale of Assets

Under the RMBCA, a corporation is presumed, unless otherwise provided, to be able to dispose of all or substantially all of its assets in the normal course of business. It may mortgage its assets, or it may transfer its assets to a wholly-owned subsidiary without shareholder approval. If disposal of all or substantially all of its assets is sought by the board of directors of a corporation, it must be submitted to the shareholders for approval by a vote of the holders of a majority of its voting shares, subject always to any relevant voting group structure or any supermajority vote requirement imposed by the RMBCA, by its articles of incorporation, or by the board's proposal (RMBCA 12.02).

Delaware law contains substantially the same provisions concerning sales of assets. New York's law is also substantially the same, except for the procedural requirement of a mandatory two-thirds shareholder vote for approval of the sale (8 Del C ss 27–272 (1991); NY Bus Corp Law ss 909, 911 (McKinney, 1994)).
Issue 13: Takeovers

The RMBCA contains no special provisions dealing with takeovers of publicly held corporations. The ABA, jointly with the North American Securities Administrators Association, has on the other hand drawn up model provisions concerning this issue, namely the Model Control Share Statute (Reprinted in Selected Corporation and Partnership Statutes, Rules and Forms (St Paul: West Publications, 1993) at 460).

Delaware law contains an anti-takeover provision which prohibits a business combination between a publicly held corporation and a holder of fifteen percent or more of its voting shares for a period of three years after a holder acquires such a percentage (8 Del C s 203 (1991)).

New York law contains an anti-takeover section which is much broader in scope than Delaware’s. It prohibits business combinations between a publicly held corporation and a holder of twenty percent or more of the corporation’s voting shares for five years, unless pre-acquisition approval by the target’s board of directors has occurred.

In addition, New York law requires that such a transaction be approved by a majority vote of the disinterested shareholders and that the consideration given to shareholders meet certain minimum price requirements, based on the price originally paid for his shares by the acquiring shareholder and on market prices.

Finally, New York law specifically allows a corporation to adopt “poison pills” and establishes detailed mandatory disclosure requirements with respect to takeover transactions (NY Bus Corp Law s 505 (McKinney, 1994)).

Issue 14: Dissolution

The RMBCA treats voluntary dissolution of a corporation in the same way it treats other fundamental corporate changes, such as amendments to articles of incorporation, mergers, mandatory share exchanges and sales of assets, all of which are discussed in the above text.

Voluntary dissolution is initiated by a proposal of the board of directors. This proposal must be submitted to the shareholders for approval by a majority thereof, subject to any relevant voting group structure or to any super majority vote requirements imposed by the articles of corporation or contained in the board’s proposal itself.

The Model Act also allows for both administrative dissolution and judicial dissolution. Administrative dissolution is initiated by the secretary of state if the corporation fails, for example, to pay franchise taxes or penalties within 60 days after they are due; fails to deliver its annual report within 60 days after it is due; is without a registered agent or office for 60 days or more; or if its period of duration as stated in its articles of incorporation expires.

Judicial dissolution is initiated by any of four parties: by the attorney general, on ground of fraud or abuse; by a shareholder, on grounds of a director or shareholder deadlock, of illegal, oppressive or fraudulent conduct by the directors, or of waste of corporate assets; and by a creditor, in the event of corporate insolvency; or by the
corporation itself, if judicial supervision of voluntary dissolution is desired.

The RMBCA also addresses the situation of a request for judicial dissolution initiated by a shareholder of a close corporation. A dissolution so initiated can be avoided by the other shareholders if they follow the special procedures allowing them to buy out the disgruntled shareholder (RMBCA 14.20).

Delaware law concerning voluntary dissolution is similar to the Model Act, except that it enables the shareholders, acting unanimously, to initiate a dissolution of this kind without any involvement of the board of directors. Nor does New York’s law require approval by the board of directors; a two-thirds majority vote by the shareholders will suffice (8 Del C s 275 (1991); NY Bus Corp Law s 1001 (McKinney, 1994)).

Both Delaware and New York law differ from the grounds available for administrative dissolution under the MBCA in that this may will only be possible where a corporation fails to pay taxes (8 Del C s 510 (1991); NY Tax Law s 203(a) (McKinney, 1994)).

Delaware law concerning judicial dissolution confers power on the state attorney general to seek dissolution on grounds of abuse, misuse or non-use. It does not however provide for opting out of a shareholder initiated judicial dissolution by means of a buyout.

New York law provides its own definition of parties who can initiate judicial dissolution and its own criteria. New York law differs from the RMBCA and the Delaware Act on a number of points, including: initiation by a majority of shareholders or a majority of directors, on grounds of insufficient assets or benefit to the shareholders; and initiation by holders of twenty percent of shares of a closed corporation, on grounds of illegal, oppressive or fraudulent conduct or waste of corporate assets (8 Del C ss 283-285 (1991); NY Bus Corp. Law ss 1008, 1101–1104 (a) (McKinney, 1994)).

B. Shareholder Rights and Remedies

Issue 15: Shareholders’ Preemptive Rights

The RMBCA creates an enabling presumption that shareholders do not have preemptive rights. It does, however, set out an optional provision defining what the granting of preemptive rights for shareholders entails where such rights are provided for in the corporation’s articles of incorporation (RMBCA 6.30).

Delaware law is substantially the same as the Model Act. New York reverses the suppletive presumption of the two Acts cited above: shareholders have preemptive rights, unless otherwise provided for in the articles of incorporation (8 Del C s 102(b)(3) (1991); NY Bus Corp Law s 622 (McKinney, 1994)).

Issue 16: Voting for Directors and Cumulative Voting

The RMBCA states that individuals with the largest number of votes are elected as directors up to the maximum number of directors to be chosen at the election (“by a
plurality of the votes cast"), unless the articles of incorporation or bylaws provide otherwise. The Model Act then sets out an optional definition of what an election of cumulative voting rights in the articles of a corporation entails, subject to opt-out variations (RMBCA 7.28(a),(c)).

Delaware and New York law are substantially the same as the RMBCA provisions, except that both states provide for the appointment of inspectors at shareholders’ meetings to monitor voting procedures. Delaware also has special provisions mandating judicial resolution of disputes arising out of contested elections for directors and other matters at shareholders’ meetings (8 Del C ss 214, 216, 231, 225, 227 (1991); NY Bus Corp Law ss 610, 611, 614, 618 (McKinney, 1994)).

**Issue 17: Derivative Actions**

Subchapter D of the RMBCA codifies the rules and procedures governing derivative actions. These rules have in most states, Delaware and New York included, traditionally been a matter of court rule and case law (D Drexl er et al, Delaware Corporation Law and Practice (New York: Matthew Bender, 1992 supp) at 42-1 cf the seminal case of Hawes v Oakland, 104 US 450 (1881)).

Derivative actions are suits brought by a stockholder for the benefit of a corporation in which he or she owns stock. Under the RMBCA the definition of shareholder includes a beneficial owner.

The RMBCA states that the plaintiff in a derivative suit must first demand leave of the board of directors of a corporation at least 90 days before the commencement of a suit in a court of law. In a subsequent section, it states that upon receiving the demand, the corporation can dismiss the shareholder’s demand if it determines in good faith, after conducting a reasonable inquiry, that the maintenance of the derivative proceeding is not in the best interests of the corporation.

The recommendations for dismissal must be made by a committee of two or more independent directors, a so called “special litigation committee”, or by court appointed panels of independent persons (RMBCA 7.40, 7.42, 7.44).

As Branson points out (supra at 275), the RMBCA in so formulating its procedural requirements for dismissal of a demand for derivative action, effectively declines to follow the common law test followed by most states which incorporated the so-called “Zapata second step”. This “second step” means that even though the corporation follows the proper procedural requirements for setting up a special litigation committee, the courts may go on to review the merits of the plaintiff’s allegations and the committee’s analysis of them, and then, in select cases, may overrule the decision of the committee on the basis of public policy or other considerations (Zapata Corp v Maldonado, 430 A2d 779 (Del 1981)).

Neither Delaware nor New York has codified corporate law on the derivative action in a way comparable to the RMBCA, although the derivative action is addressed briefly by the Acts of both states. Whereas New York law, like the RMBCA, expressly permits suits to be maintained by beneficial holders of shares, Delaware law is silent on this issue (8 Del C s 327 (1991); NY Bus Corp Law ss 626, 627 (McKinney, 1994)).
Appendix

Issue 18: Removal of Directors by Shareholders

Shareholders have the power to remove directors, with or without cause, at a shareholders’ meeting held with proper notice under the RMBCA. This power is however subject to relevant voting group structures provided for in the corporation’s articles of incorporation (this power can be limited to that of removal with cause only if the corporation’s articles of incorporation so provide, RMBCA 8.08).

Delaware law has a provision substantially the same as the RMBCA. New York however reverses the presumption of removal without cause, stating that such is only allowable where the articles of incorporation or bylaws so specify expressly. It also allows for the removal of a director with cause by the other directors if the articles of incorporation or bylaws of the corporation so permit (8 Del C s 141(k) (1991); NY Bus Corp Law s 706 (McKinney, 1994)).

Issue 19: Dissenting Shareholders’ Rights

The RMBCA dissenters’ rights chapter allows shareholders to dissent from certain fundamental corporate changes and to receive fair market value for their shares when such changes are approved by the majority. The fundamental changes in question under the Model Act are mergers, mandatory share exchanges, sales of assets other than in the normal course of business, certain amendments of a corporation’s articles, and any other corporate action which the articles of incorporation, bylaws or a resolution by the board of directors provide for.

Shareholders wishing to avail themselves of their right to dissent must notify the corporation before the shareholders’ vote and may not themselves vote on such an action. If the shareholders’ vote is favourable, the dissenters will be notified and will be required to deposit their share certificates, in exchange for which they will receive payment from the corporation at a price estimated by the latter to be fair in light of the current market. If the shareholders are not satisfied by the price determined by the corporation, they may notify the corporation. The corporation will then be obliged to take the matter before the courts within 60 days if no agreement is reached. The courts will then determine and order the payment of the fair market value. If the corporation does not take the matter before the courts as is required by the Act, it must pay the amount asked by the dissenters by default (RMBCA Chapter 13, RMBCA 13.28, 13.30, 13.31).

Under Delaware law, the only major corporate action that leads to the creation of mandatory dissenters’ rights is a merger. Shareholders of publicly held corporations and those who receive a combination of shares and cash may not avail themselves of this right. A corporation may however provide suppletively for dissenters’ rights as triggered by an amendment of the articles of incorporation or a sale of assets (8 Del C s 262 (1991)).

New York law provides that the corporation need only pay 80 percent of its estimated fair market value of the shares. It also states that a corporation need not itself initiate a court proceeding at the time it decides not to pay a dissenter or disagrees with
the latter with regard to the fair value of the shares. It will then be up to the dissenter to bring the matter before the courts (NY Bus Corp Law ss 605(a), 623, 806(b)(6), 910 (McKinney, 1994)).

C. Directors’ Duties and Liabilities

Issue 20: Duties of Board of Directors

The RMBCA states that each corporation must have a board of directors unless this requirement is avoided by a shareholders’ agreement. It further states that all corporate powers shall be exercised by, and the business and affairs of the corporation managed under the directions of, its board of directors (RMBCA 7.32, 8.01).

Delaware and New York law are substantially the same as the RMBCA on this issue (8 Del C s 141(a) (1991); NY Bus Corp Law s 701 (McKinney, 1994)).

Issue 21: Directors’ and Officers’ Duty of Care

The RMBCA codification of the duty of care provides that directors and officers shall discharge their duties in good faith, with the care an ordinarily prudent person in a like position would exercise under similar circumstances, and in a manner they reasonably believe to be in the best interests of the corporation.

Under the Model Act, they are entitled to rely, within the bounds of reasonableness, on certain documents and persons, such as financial statements prepared by employees of the corporation, legal counsel, and accountants.

If directors and officers meet these standards, they will not be held personally liable for their acts or omissions. Moreover, in the RMBCA, as discussed supra in Issue 2, the articles of incorporation may serve to lower the standard of care even further by exempting directors, but not officers, from liability for monetary damages due to their negligence (RMBCA ss 2.02, 8.30, 8.42).

New York Law is somewhat similar to the RMBCA, with the important difference that its standard of conduct does not require directors or officers to act with a reasonable belief that what they are doing is in the best interests of the corporation. The New York law also includes a provision enabling director liability to be limited (NY Bus Corp Law ss 401, 402, 715(h), 717, 720 (McKinney, 1994)).

Delaware law contrasts markedly from the RMBCA on this crucial issue. No standard of conduct is provided for directors or officers. Rather, the Delaware Act provides affirmatively that directors will not be personally liable where they rely in good faith on the enumerated class of documents and persons. The articles of incorporation may further limit directors’ personal liability for monetary damages due to negligence (8 Del C ss 102, 141 (1991)).

Issue 22: Liability for Unlawful Distributions

Under the provisions of the RMBCA, a director, who votes for, or assents to, a distribution made in violation of the standard of care required of a director in the Act
(see supra Issue 21), is personally liable to the corporation for the amount of the distribution that exceeds what could have been distributed lawfully (RMBCA 8.33(a)).

Delaware and New York laws are substantially the same as the RMBCA on this issue, except that in Delaware, no reference is made to the director's standard of care as a result of the absence from that Act of any such standard (8 Del C ss 172, 174 (1991); NY Bus Corp Law ss 719, 720 (McKinney, 1994)).

**Issue 23: Conflict of Interest Transactions**

The relatively recent re-codification of the duty of loyalty by the ABA as presented in subchapter F of the RMBCA represents, for Branson, a regrettable further weakening of traditional notions of directors' fiduciary duties (1) Branson, supra at 59; (2) Branson, supra at 268. Subchapter F was first published in 1988).

The Model Act narrowly defines an interested directors' transaction as one which involves both a corporation and either a director of such corporation, a related person, or an entity in which the director or a related person has a stake (RMBCA 8.60).

The test set out in the RMBCA for allowing a shareholder, in a direct or derivative action, to set aside, enjoin or receive damages for an interested directors' transaction, effectively modifies what was at common law a conjunctive, partly procedural, partly substantive test (cf Remillard Brick Co v Remillard-Dandini Co, 109 Cal App 2d 405, 241 P2d 66 (1952)). The Model Act's test states that a director's transaction cannot be impugned if either the requisite disclosure and disinterested shareholder ratification procedures have been followed, or the transaction is judged by the court to have been "fair" to the corporation (RMBCA 8.61(b)).

Delaware law departs from the RMBCA only in that it does not require shareholder approval of the transaction to be given solely by disinterested shareholders (8 Del C s 144 (1991)).

New York law is also similar to the RMBCA. It is even more explicit in providing that fairness need be proved only if the full disclosure and shareholder approval "safe-harbours" have not been reached. In addition, it states that additional constraints can be put on conflict of interest transactions in the articles of incorporation (NY Bus Corp Law s 713 (McKinney, 1994)).

**Issue 24: Indemnification**

The RMBCA enables a director or officer to be indemnified for any liability incurred in those capacities. Moreover they are entitled to be advanced expenses during a proceeding threatening liability on the condition that they acted in good faith and reasonably believed that their conduct was in the best interests of the corporation.

Subject to any provision in the articles of incorporation providing otherwise, the RMBCA presumes that a director who is successful in his or her proceeding is entitled to mandatory indemnification. With regards to advances or expenses, these can be made only if the director or officer affirms in writing that the standards referred to above have
been met and provides a written undertaking to repay the advances if the said standards have in fact not been met.

Officers who are not directors are entitled to broader indemnification under the Model Act than directors. The Act does not limit indemnification for officers to reasonable expenses incurred in connection with the proceedings. Instead, it states that they might be indemnified "to the extent, consistent with public policy" as provided for by a corporation's articles of incorporation, bylaws, action of the board of directors, or contract.

While the Model Act will not allow the corporation to augment the availability of indemnification or make advances for expenses beyond the scope specifically provided for in the Act, it will allow a corporation to obtain insurance for its directors acting in that capacity to cover liabilities, regardless of whether such liabilities are indemnifiable (RMBCA 8.51–8.53, 8.57 (directors); 8.56 (officers)).

Delaware and New York law are very similar to the RMBCA except that neither jurisdiction makes the RMBCA's distinction between directors and officers in determining their respective scopes of indemnification.

**Issue 25: Stakeholder Considerations**

Neither the RMBCA nor Delaware law provide for enabling rules describing the consideration and interests which may be taken into consideration by the directors and officers of a corporation as they discharge their duties.

New York law on the other hand specifically authorizes the directors and officers of a corporation to take into account both the long-term and short-term effects of their decisions, and significantly adds creditors to the list of the decision-makers' potential constituents (NY Bus Corp Law s 717(b) (McKinney, 1994)).
Selected Bibliography of Secondary Sources

I. Reports


Australia, Corporations Law Simplification Program Task Force, Plan of Action — Stage 2 (Canberra: Attorney-General’s Department, 1994).


Toronto Stock Exchange, Committee on Corporate Governance in Canada, *Where were the Directors?*: Guidelines for Improved Corporate Governance in Canada (Toronto, 1994) (The Dey Report).


II. Books and Articles


Hahlo, H, South African Company Law through the Cases (Cape Town: Juts, 1984).


