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### **What Do You Do With a High Court Decision You Don't Like? Legislative, Judicial and Academic Responses to Gambotto v WCP LTD**

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# WHAT DO YOU DO WITH A HIGH COURT DECISION YOU DON'T LIKE? LEGISLATIVE, JUDICIAL AND ACADEMIC RESPONSES TO *GAMBOTTO V WCP LTD*

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The decision of the High Court of Australia in *Gambotto v WCP Ltd* was both controversial and widely debated. Some saw the decision as radically altering the balance of power in corporate law by granting minority shareholders extensive new powers to prevent the compulsory acquisition of their shares and thereby impeding commercial transactions that would benefit companies. There was also concern that the principles developed by the High Court for compulsory acquisition of shares undertaken by way of amendment of the corporate constitution would apply to other forms of compulsory acquisition, and corporate law more generally, again impeding many types of corporate transactions. We analyse the responses to the High Court decision. The decision had the potential to have a significant influence on Australian corporate law and the way corporate transactions involving compulsory share acquisitions are conducted. In particular, *Gambotto* was considered in more than 50 subsequent judgments giving many judges the opportunity to extend the *Gambotto* principles into new areas. We show that the responses to *Gambotto* were largely negative. Initial commentary in the media and subsequent academic commentary was mostly critical. Almost uniformly, courts decided that the principles should not be extended. Parliament responded by enacting new provisions in the corporations legislation facilitating the compulsory acquisition of shares and limiting the application of *Gambotto*. We document how courts and Parliament responded to a decision they did not like – a decision that had the potential to have major implications for corporate law and commercial transactions. We also analyse *Gambotto* by placing it in the broader political context of the role of the High Court at the time of the decision. *Gambotto* was decided when the High Court was in a period of unprecedented judicial activism. Subsequently the High Court retreated from this judicial activism and we observe similarities in how other courts restricted the application of *Gambotto*.

## I INTRODUCTION

*Gambotto v WCP Ltd*<sup>1</sup> was one of the most controversial corporate law judgments in Australian legal history. In *Gambotto*, the High Court of Australia struck down an amendment to a company's constitution<sup>2</sup> which enabled the majority shareholders to compulsorily acquire, or expropriate, the shares of the minority.

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<sup>1</sup> *Gambotto v WCP Ltd* (1995) 182 CLR 432; 127 ALR 417; 16 ACSR 1; 13 ACLC 342 (“*Gambotto*”).

<sup>2</sup> For convenience, the terms memorandum and articles of association are often referred to in this article as constitution.

The *Australian Financial Review*, in a front page story on 9 March 1995 (the day following the decision), referred to the High Court decision as one that had “radically altered the balance of power within corporate Australia”. In the same edition, a columnist stated that the decision “appears, at first glance, to have turned Australia into a greenmailer’s paradise”.

The High Court held that for an amendment to the corporate constitution which allows for the expropriation of shares to be valid, the amendment must be for a proper purpose and must not be oppressive. The court defined what a proper purpose is very narrowly to mean that the amendment to the constitution would only be valid if the purpose of the expropriation was to prevent harm or detriment to the company. It is not sufficient for the expropriation to advance the interests of the company (for example, for the company to receive taxation or administrative benefits). This was in the context of the price paid to those whose shares were expropriated being fair.

Many concerns were expressed after the High Court handed down its decision. The decision was seen by some as radically altering the balance of power in corporate law, elevating minority rights and giving minority shareholders additional power to engage in greenmailing. In particular, it was feared that the strict test laid down by the High Court would infect the other forms of compulsory acquisition, and corporate law more generally, impeding many types of corporate transactions. The decision led to the restructuring of one of the most significant corporate transactions underway at the time the High Court handed down its judgment – the demutualisation of the NRMA – which had at the time 1.8 million members and over \$4 billion in assets.

The decision of the High Court reflected several core tensions in corporate law such as the balance between the powers given to majority and minority shareholders; the extent to which corporate transactions which benefit the company should be facilitated even where this involves the expropriation of the shares of some shareholders against their will but at a fair price; and the rights that should attach to shares and when these rights should be able to be defeated or taken away.

Sixteen years after the High Court’s decision, we are in a position to evaluate the responses to *Gambotto*. As we document in this article, the responses were largely negative. However, what is unusual about this decision of the High Court is how widespread the responses were. They began with media commentary and then moved to a debate among corporate law commentators including academics. Courts also responded as they considered arguments in subsequent cases about whether the principles in *Gambotto* should be extended. Parliament responded by enacting new provisions in the corporations legislation facilitating the compulsory acquisition of shares.

The responses of the courts are important. In subsequent judgments, courts have, almost uniformly, refused to extend the principles in *Gambotto* to other situations with the result that the principles have largely been confined to the factual situation that was before the High Court in *Gambotto*. The potential for *Gambotto* to have wider application than the circumstances before the High Court is reflected in the fact that it has been considered in more than 50 subsequent judgments.

Parliament's response was to enact a new method of compulsory acquisition that means that if the circumstances in *Gambotto* occur again, majority shareholders have an alternative option for compulsory acquisition available to them. As we document in this article, the response of Parliament was influenced by the debate generated by the High Court's decision in *Gambotto*.

In summary, our research indicates how courts and Parliament respond to a High Court decision they do not like. The result is that what initially appeared to be a decision that had broad implications for corporate law and corporate transactions has been so restricted that its influence in other parts of the law is now very limited. At the same time, our research indicates the potential influence of decisions of the High Court. The decision generated considerable controversy and was followed by a range of important responses.

The structure of the article is as follows. First, the decision in *Gambotto* is discussed and the major elements of the High Court's decision are highlighted. Second, academic and practitioner commentary is then reviewed to determine the major areas of criticism. Third, we place the decision in *Gambotto* in the broader political context of the role of the High Court at the time of the decision. Fourth, subsequent judicial interpretation of the meaning and scope of *Gambotto* is examined to review the effect of *Gambotto* on corporate law and the other methods of compulsory acquisition. Finally, the legislative response is discussed.

## II THE DECISION IN *GAMBOTTO*

This section provides an outline of the decisions of the Supreme Court of New South Wales and the High Court in *Gambotto*.

### A The Facts

The *Gambotto* litigation concerned the majority's attempt to obtain 100% ownership in WCP Limited ("WCP"). The majority shareholders, wholly owned subsidiaries of Industrial Equity Ltd (collectively referred to as "IEL"), held approximately 99.7% of the issued share capital of WCP. The appellants, Giancarlo Gambotto and Eliandri Sandri, held approximately 0.094% of the issued share capital.

IEL desired to obtain 100% control of WCP to enable it to obtain significant taxation and administrative benefits, including income tax savings in excess of \$4 million and accounting fee savings of approximately \$3,000 per year. IEL was not able to acquire the appellants' shares under alternative compulsory acquisition mechanisms.<sup>3</sup>

IEL therefore sought to insert a provision into the company's constitution enabling any member who held 90% or more of the issued shares to compulsorily acquire, before 30 June 1992, all the issued shares in WCP at a price of \$1.80 per share. WCP sent a notice to its shareholders that a meeting was to be held on 11 May 1992 to consider an

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<sup>3</sup> Sections 414 and 701 of the *Corporations Law*. The *Corporations Law* is now the *Corporations Act 2001* (Cth).

amendment to this effect. An expert had valued the shares at \$1.365 per share, which the appellants conceded was a fair valuation.

The appellants did not want to sell their shares, and instituted proceedings prior to the meeting, seeking to prevent the resolution being passed. The meeting subsequently took place, although WCP undertook not to acquire any shares under the new article until the conclusion of the court proceedings. The amendment was passed at the meeting and IEL did not vote its shares at the meeting.

### **B The Decision at First Instance**

In the Supreme Court of New South Wales, McLelland J noted that although s 176(1) of the *Corporations Law* gave broad scope to a company to amend its constitution, the exercise of that power was constrained by equitable principles.<sup>4</sup> He held that:

The immediate purpose and effect of the amendment was to permit the shares of the minority shareholders to be expropriated by the majority shareholders. In my opinion such an amendment amounts to unjust oppression of those minority shareholders who object.<sup>5</sup>

His Honour noted that if it was permissible to allow expropriations of minority shareholders by majority shareholders holding 75% of the shares (the minimum percentage needed to amend the corporate constitution), the procedures for compulsory acquisition set out in the *Corporations Law* such as ss 414 and 701 would be unnecessary.<sup>6</sup>

### **C New South Wales Court of Appeal Decision**

The New South Wales Court of Appeal unanimously overturned McLelland J's decision.<sup>7</sup> The leading judgment was delivered by Meagher JA.<sup>8</sup> His Honour noted that the ability of a company to alter its constitution was wide, but subject to equitable limitations.

His Honour stated that McLelland J's view was only consistent with the notion that an expropriation of shares is a *malum in se*.<sup>9</sup> As the *Corporations Law* contained provisions expressly permitting expropriation, an expropriation was not contrary to legislative policy, and those provisions did not constitute an exclusive code governing expropriation.<sup>10</sup> Meagher JA held that considerable benefits would accrue from the expropriation and it had not been asserted that the amount to be paid for the shares was inadequate. Accordingly, there was no reason for the court to intervene.<sup>11</sup>

Priestly JA, agreeing with the orders proposed by Meagher JA, noted that a person, upon becoming a member of a company, agrees to be bound by duly passed resolutions of the

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<sup>4</sup> *Gambotto v WCP Ltd* (1992) 8 ACSR 141 at 143.

<sup>5</sup> *Ibid* at 144.

<sup>6</sup> *Ibid* at 145.

<sup>7</sup> *WCP v Gambotto* (1993) 30 NSWLR 385.

<sup>8</sup> Cripps and Priestly JJA agreeing.

<sup>9</sup> Above n 7.

<sup>10</sup> *Ibid*.

<sup>11</sup> *Ibid*.

company, and so an expropriation effected by means of an amendment to the company's constitution "is, in a real sense, not a divestment against the shareholder's will".<sup>12</sup>

The Court of Appeal's decision thus appeared to stand for the proposition that as long as adequate compensation was provided, the majority is able to expropriate the minority's shares.<sup>13</sup>

### **D High Court Decision: The Majority**

The High Court overturned the Court of Appeal decision, holding that the amendment was invalid as it was not made for a proper purpose.<sup>14</sup> The majority (consisting of Mason CJ, Brennan, Deane and Dawson JJ) commenced their analysis by framing the fundamental question as "whether, and if so in what circumstances, the taking of a power by majority shareholders by amendment to the articles to acquire compulsorily the shares of the minority shareholders will be held invalid on the basis that it is oppressive".<sup>15</sup>

In the much cited judgment *Allen v Gold Reefs of West Africa Ltd*,<sup>16</sup> Lindley MR had stated that the power to amend the corporate constitution by special resolution "must be exercised, not only in the manner required by law, but also bona fide for the benefit of the company as a whole, and it must not be exceeded".

Following *Peters' American Delicacy Co Ltd v Heath*,<sup>17</sup> the majority of the High Court in *Gambotto* rejected the "bona fide for the benefit of the company as a whole" test laid down by Lindley MR in *Allen* as inappropriate in the context of competing rights and interests of shareholders.<sup>18</sup> The court drew a distinction between two different types of constitutional alterations. For alterations not involving "expropriation of shares or of valuable proprietary rights attaching to shares" it is sufficient if the special resolution is passed regularly, is not ultra vires, not beyond any purpose contemplated by the constitution nor oppressive.<sup>19</sup>

With respect to alterations that do involve expropriation of shares, or valuable proprietary rights attached to shares, different considerations apply. The majority laid down a two-pronged test, holding that amendments to the constitution permitting expropriation are only permissible if:

- the power is exercisable for a proper purpose; and
- its exercise will not operate oppressively in relation to minority shareholders.<sup>20</sup>

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<sup>12</sup> Ibid at 386. Contra this reasoning see Brett W King, "Use of Supermajority Voting Rules in Corporate America: Majority Rule, Corporate Legitimacy, and Minority Shareholder Protection" (1996) 21 *Delaware Journal of Corporate Law* 895 at 907.

<sup>13</sup> Vanessa Mitchell, "*Gambotto* and the Rights of Minority Shareholders" (1994) 6 *Bond Law Review* 92 at 102.

<sup>14</sup> *Gambotto v WCP Ltd* (1995) 182 CLR 432 at 448. For a more detailed discussion of the High Court decision, see H A J Ford, R P Austin and I M Ramsay, *Ford's Principles of Corporations Law* (Looseleaf, LexisNexis Butterworths), Ch 11.

<sup>15</sup> *Gambotto* at 439.

<sup>16</sup> [1900] 1 Ch 656 at 671 (Romer J agreeing at 678).

<sup>17</sup> (1939) 61 CLR 457 at 481 (Latham CJ), 512 (Dixon J).

<sup>18</sup> *Gambotto* at 444.

<sup>19</sup> Ibid.

<sup>20</sup> Ibid at 445.

The first limb of this test, the proper purpose requirement, meant that expropriation was only justified “where it is reasonably apprehended that the continued shareholding of the minority is detrimental to the company, its undertaking or the conduct of its affairs ... and expropriation is a reasonable means of eliminating or mitigating that detriment”.<sup>21</sup>

The majority considered that it would not be sufficient justification that an expropriation would advance the interests of the company, or secure some commercial advantage.<sup>22</sup> An expropriation will only be for a valid purpose if it secures the company from detriment or harm. The majority gave two examples of a proper purpose: where a shareholder is competing with the company, or if it is necessary to ensure that the company can comply with a regulatory regime, such as shareholder residency requirements.<sup>23</sup>

The second limb of the test, the requirement that the expropriation must be fair and not oppressive, was held to include procedural and substantive aspects. The process by which the expropriation is undertaken must be fair, requiring the majority to disclose all relevant information and have the shares valued by an independent expert. Substantive fairness is concerned with the price to be paid for the shares. The majority noted that market value may not be a sufficient indicator of the fair value of the shares, but that all relevant factors should be taken into account, including, in addition to market value, the assets of the company, dividends, and the nature of the company and its likely future.<sup>24</sup>

Fairness was not challenged by the appellants but it could not be established that the expropriation was for a proper purpose. Notably, the majority also held that the onus should be upon the party intending to expropriate to prove that the power is validly exercised.

### **E High Court Decision: McHugh J**

McHugh J held that a company may alter its constitution to enable a shareholder to acquire the shares of another “only when the acquisition is necessary to protect or promote the interests of the company and when the alteration will not be oppressive to those shareholders”.<sup>25</sup> This is supported by the fact that shares are private property and a general statutory power such as s 176 of the *Corporations Law* permitting a company to amend its constitution should not be construed so as to enable such rights to be taken away.<sup>26</sup>

His Honour rejected the distinction between the avoidance of a detriment and the securing of a benefit as in both cases it can be said that the expropriation is commercially necessary to protect the company’s assets. His Honour instead distinguished between benefits which are external to the company and those which are internal.<sup>27</sup> McHugh J

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<sup>21</sup> Ibid.

<sup>22</sup> Ibid at 446.

<sup>23</sup> Ibid at 445-6.

<sup>24</sup> Ibid at 446-7.

<sup>25</sup> Ibid at 453.

<sup>26</sup> Ibid.

<sup>27</sup> Ibid at 455.

held there are two elements relevant to the question of oppression, fair dealing and fair price, mirroring the majority's procedural and substantive fairness requirements.<sup>28</sup>

On the facts, McHugh J held that the purpose of amending the constitution of WCP was to enable an expropriation of shares that would promote the interests of the company and this was a legitimate business objective. However, IEL had not established that the expropriation was not oppressive. The onus is on the would-be expropriator to establish the fairness of the expropriation, and the majority shareholder and the company made almost no attempt to properly disclose all relevant information.

## F Key Aspects of the Decision

Some important aspects of the majority decision in *Gambotto* can be noted. Other aspects will be discussed in detail below. First, by defining what is a proper purpose narrowly, the test laid down by the High Court is therefore a stringent test for would-be expropriators to satisfy,<sup>29</sup> and is an objective test, which does not limit the inquiry to the subjective good faith of the majority.<sup>30</sup> It is likely that the court deliberately framed the test this way to make it unattractive for majority shareholders to seek to avoid the protections contained in the statutory expropriation mechanisms. The "proper purpose" test laid down by the High Court has no equivalent in the statutory mechanisms for expropriation.<sup>31</sup>

Second, the majority placed an important emphasis on the concept of shares as property, with the holder having proprietary rights in that property:

we do not consider that, in the case of an alteration to the articles authorising the expropriation of shares, it is a sufficient justification of an expropriation that the expropriation, being fair, will advance the interests of the company as a legal and commercial entity. ... This approach does not attach sufficient weight to the proprietary nature of a share.<sup>32</sup>

Third, the principles in *Gambotto* apply only to amendments to the constitution and do not apply to the constitution upon incorporation. Later judgments have confirmed that expropriatory provisions are valid if they are present from incorporation.<sup>33</sup>

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<sup>28</sup> Ibid at 459.

<sup>29</sup> *Re Australian Co-operative Foods Ltd* (2001) 186 ALR 21; (2001) 162 FLR 360; (2001) 38 ACSR 71; (2001) 19 ACLC 1120; [2001] NSWSC 382 at [76] (Santow J).

<sup>30</sup> Paul L Davies, *Gower and Davies Principles of Modern Company Law* (Sweet & Maxwell, 8<sup>th</sup> ed, 2008, 657).

<sup>31</sup> As Santow J said in *Re Australian Co-operative Foods Ltd*, "Fairness, however, does not in the scheme [of arrangement] context have the stringent narrowness of the non-statutory *Gambotto* test of only permitting a scheme which avoids detriment to the company": *Re Australian Co-operative Foods Ltd* (2001) 186 ALR 21; (2001) 162 FLR 360; (2001) 38 ACSR 71; (2001) 19 ACLC 1120; [2001] NSWSC 382 at [76].

<sup>32</sup> *Gambotto v WCP Ltd* (1995) 182 CLR 432 at 446.

<sup>33</sup> *Accurate Financial Consultants Pty Ltd v Koko Black Pty Ltd* [2007] VSC 40 at [106], referring to *Gambotto v WCP Ltd* (1995) 182 CLR 432 at 445; *Associated World Investments Pty Ltd v Aristocrat Leisure Ltd* (1997) 25 ACSR 783; (1998) 16 ACLC 455.



### III MEDIA, ACADEMIC AND PRACTITIONER RESPONSES TO *GAMBOTTO*

Unusually for a High Court decision, *Gambotto* generated widespread media attention, most of it hostile. Legal practitioners were generally critical of the decision, seeing it as an obstacle to corporate reorganisations and other transactions. Academics were divided, with some seeing the decision as a welcome one, but most were opposed.

#### A General Assessments and Media Commentary

*Gambotto* evoked passionate responses from media commentators and the legal community. Chulov believed that *Gambotto* was “the most radical power-swing in the history of corporate Australia”, which “chilled corporate Australia and catapulted the rights of the small investor to the forefront of decision making”.<sup>34</sup>

The decision was widely seen as a significant victory for minority shareholders,<sup>35</sup> as the High Court “dramatically turned the tide of power in favour of minority shareholders”.<sup>36</sup> *Gambotto* “ushered in a new era of minority shareholder protections”,<sup>37</sup> and was said to elevate the rights of minority shareholders above those of majorities.<sup>38</sup>

Some saw this as a welcome reversal of the traditional approach which favoured the majority<sup>39</sup> and gave priority to market efficiency over shareholder protection.<sup>40</sup> The Court of Appeal decision<sup>41</sup> had been seen by some as shifting the balance too far in favour of the majority.<sup>42</sup> An editorial in the *Australian Financial Review* stated that the “spirit of Giancarlo *Gambotto*’s historic victory deserves to remain part of Australian company law”.<sup>43</sup>

Overwhelmingly, however, the response to *Gambotto* was negative.<sup>44</sup> The day after the decision was handed down, the *Australian Financial Review* published an article which argued that the decision would “turn Australia into a greenmailer’s paradise”.<sup>45</sup> Fridman argued that *Gambotto* potentially created an environment where minority dictatorship

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<sup>34</sup> Martin Chulov, “Little Battler Beats Giant Corporations”, *Sun Herald*, 7 May 1995, 51.

<sup>35</sup> Jeanne Cilliers, “Is the Tide Turning Against Green-Mailers?” (2001) 39(9) *Law Society Journal* 59; Verge Blunden, “Court Rules For Minority Shareholders”, *Sydney Morning Herald*, 9 March 1995, 39.

<sup>36</sup> Stephen Kevans, “Oppression of Majority Shareholders by a Minority? *Gambotto v WCP Ltd*” (1996) 18 *Sydney Law Review* 110 at 110.

<sup>37</sup> Michael Yew Seong Chin, “Being in the Minority: The Compulsory Acquisition of Shares” (1997) 8 *Auckland University Law Review* 413 at 413.

<sup>38</sup> Stephen Bartholomeusz, “NRMA Defeat Emphasises Obstacles Mutuals Face”, *The Age*, 30 May 1995, 39.

<sup>39</sup> Glenn Hughes, “Compulsory Acquisition of Minority Shareholders’ Interests – Still a Tyranny of the Majority?” (2000) 18 *Company and Securities Law Journal* 197.

<sup>40</sup> Peta Spender, “Compulsory Acquisition of Minority Shareholdings” (1993) 11 *Company and Securities Law Journal* 83 at 88, 101.

<sup>41</sup> *WCP Ltd v Gambotto* (1993) 10 ACSR 468.

<sup>42</sup> Karen Yeung, “*WCP Ltd v Gambotto*” (1993) 11 *Company and Securities Law Journal* 323 at 325.

<sup>43</sup> Editorial, “Balancing Corporate Power”, *Australian Financial Review*, 10 March 1995, 28.

<sup>44</sup> Peta Spender, “Guns and Greenmail: Fear and Loathing After *Gambotto*” (1998) 22 *Melbourne University Law Review* 96 at 102.

<sup>45</sup> Ivor Ries, Chanticleer Column, *Australian Financial Review*, 9 March 1995, 60

may prevail,<sup>46</sup> and Kevans agreed that greenmailing would be a significant problem arising from *Gambotto* as it placed shareholders in a “supreme position”.<sup>47</sup> Other commentators believed that *Gambotto* represented a failure to strike an appropriate balance between majority and minority shareholders.<sup>48</sup>

Fridman criticised the “seriously flawed” logic of the High Court, in particular by failing to provide a definitive statement as to the balance between majority and minority shareholders.<sup>49</sup> Wishart criticised the High Court for wasting an important opportunity to lay down appropriate guidance for corporate law management.<sup>50</sup>

There was also widespread uncertainty as to its implications, with most seeing the decision as having far-reaching effects on corporate law.<sup>51</sup> It was reported that legal advisors began to quickly consider its potential implications.<sup>52</sup> Chulov and Potts asserted that *Gambotto* “prohibits large corporations from scooping up small investors’ shares in subsidiary companies against their will”.<sup>53</sup> Others said that “*Gambotto* basically stops companies compulsorily acquiring minority holders unless its rules specifically confer that right.”<sup>54</sup>

The consensus of the business community was that the decision “might impede value-adding corporate restructures and empower greenmailers”, although others doubted that *Gambotto* would have such widespread ramifications.<sup>55</sup> Bartholomeusz stated that *Gambotto* was being interpreted such that:

unless the company’s business was threatened by their behaviour or expropriation was required for compliance with a regulatory regime, it is almost impossible to expropriate a minority’s interest.<sup>56</sup>

In assessments of *Gambotto*, one of the aspects that appeared to exacerbate criticisms the most was the particular facts of the case. The proposed acquisition price was a 31.9% premium to the value of \$1.365 per share which had been determined by an independent expert. Priestly JA had stated that it was “undisputedly the case” that this represented fair

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<sup>46</sup> Saul Fridman, “When Should Compulsory Acquisition of Shares be Permitted, and if so, What Ought the Rules be?” in Ian M Ramsay (ed), *Gambotto v WCP Ltd: Its Implications for Corporate Regulation* (Centre for Corporate Law and Securities Regulation, University of Melbourne, 1996) at 135.

<sup>47</sup> Kevans, above n 36 at 114.

<sup>48</sup> Jeanne Cilliers and Stephanie Luiz, “Comments on the Test Determining the Validity of an Alteration of Articles of Association” (1999) 11 *Australian Journal of Corporate Law* 89 at 109, 112.

<sup>49</sup> Saul Fridman, “No Definitive Statement on Issue”, *Australian Financial Review*, 13 March 1995, 19.

<sup>50</sup> David Wishart, “Does the High Court Understand Corporations Law?” (1996) 6 *Australian Journal of Corporate Law* 424 at 430.

<sup>51</sup> Chris Merritt, “High Court Verdict Spells Trouble Ahead”, *Australian Financial Review*, 10 March 1995, 33.

<sup>52</sup> Stephen Bartholomeusz, “Banks Are Not in the Social Equity Business”, *The Age*, 1 April 1995, 27; Martin Chulov, “Small Investor Bites Watchdog”, *Sun Herald*, 21 May 1995, 47.

<sup>53</sup> Martin Chulov and David Potts, “Insurers Polish Float Plans”, *Sun Herald*, 4 June 1995, 61.

<sup>54</sup> Glenn Burge, “Plenty of Potholes Ahead For NRMA”, *Sydney Morning Herald*, 6 April 1995, 39.

<sup>55</sup> Saul Fridman, “NRMA Float and the Ghost of the *Gambotto* Judgment”, *Australian Financial Review*, 21 May 1999, 28.

<sup>56</sup> Stephen Bartholomeusz, “NRMA Defeat Emphasises Obstacles Mutuals Face”, *The Age*, 30 May 1995, 39.

compensation.<sup>57</sup> Further, significant tax savings would have accrued to the company.<sup>58</sup> Given these facts, many commentators appeared to accept that this was not a case where expropriation should have been refused. If compulsory acquisition was not permissible under these circumstances, when would it be permissible? The decision fuelled concerns that *Gambotto* would have broader application in company law.<sup>59</sup>

## B The Demutualisation of NRMA

*Gambotto* was to prove very significant for the demutualisation of the NRMA group of companies and its legal advisors. The NRMA group consisted of a number of companies operating under the collective name of NRMA (previously the National Roads and Motorists Association). The group was based in New South Wales and had operated since 1920, providing insurance and financial services to its members. By 1994 the group had over 1,800,000 members, with assets of over \$4 billion under its management.<sup>60</sup>

In 1992 the NRMA group decided to “demutualise” into a listed profit making company that would pay dividends to shareholders. The demutualisation was initially proposed to be undertaken by means of amending the relevant companies’ articles of association, which the NRMA’s legal counsel had advised was a valid means of effecting the demutualisation.

The proposal was to incorporate a new company limited by shares to become a member of the relevant NRMA companies (Association and Insurance). General meetings of those companies would be held to pass resolutions with the effect that all members of Association and Insurance other than the new company would cease to be members, and would at their election either become shareholders in the new holding company or receive a cash payment. The new company would be listed on the Australian Stock Exchange. As a result, the NRMA companies would become wholly-owned subsidiaries of the new company, which would be a listed holding company.<sup>61</sup>

While this proposal was being implemented, *Gambotto* was handed down. The decision was widely seen as preventing the demutualisation from proceeding as initially proposed.<sup>62</sup> Digby noted at the time that “the apparent consensus of authority ... [is] that

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<sup>57</sup> *WCP v Gambotto* (1993) 30 NSWLR 385 at 386.

<sup>58</sup> Michael J Whincop, “An Economic Analysis of *Gambotto*” in Ian M Ramsay (ed), *Gambotto v WCP Ltd: Its Implications for Corporate Regulation* (Centre for Corporate Law and Securities Regulation, University of Melbourne, 1996) at 110-11.

<sup>59</sup> See Yeung, above n 42 at 325-6, discussing the decision of the Court of Appeal.

<sup>60</sup> For more detail see *Heydon v NRMA Ltd* (2000) 51 NSWLR 1; (2000) 36 ACSR 462; (2001) 19 ACLC 1 at [5]ff (Malcolm A-JA).

<sup>61</sup> This summary is taken from *Heydon v NRMA Ltd* (2000) 51 NSWLR 1; (2000) 36 ACSR 462; (2001) 19 ACLC 1 at [15] (Malcolm A-JA).

<sup>62</sup> Stephen Bartholomeusz, “NM’s Small Loss Can Only Assist Its AXA Deal”, *The Age*, 2 June 1995, 21; Stephen Bartholomeusz, “NRMA Defeat Emphasises Obstacles Mutuals Face”, *The Age*, 30 May 1995, 39; Glenn Burge, “NRMA \$2bn Float Buried”, *Sydney Morning Herald*, 29 May 1995, 21; Glenn Burge, “Crunch Time for the NRMA Board”, *Sydney Morning Herald*, 26 May 1995, 21; Glenn Burge, “Plenty of Potholes Ahead For NRMA”, *Sydney Morning Herald*, 6 April 1995, 39. But see “The NRMA Backs Off”, *Sydney Morning Herald*, 1 June 1995, 14, in which it is argued that citing *Gambotto* as the reason for abandoning the articles-amendment route “is mere face-saving”.

the *Gambotto* decision rules out any possibility of effecting a demutualisation by means of an alteration to the Articles”.<sup>63</sup>

Entirely as a consequence of *Gambotto*, therefore, the original approach was abandoned, and the demutualisation proceeded by way of a scheme of arrangement.<sup>64</sup> NRMA then sued its legal advisers in negligence for failing to anticipate the potential effect of the *Gambotto* decision on the demutualisation, seeking recovery of its wasted costs and expenses.<sup>65</sup> NRMA won at first instance and was awarded approximately \$32 million.<sup>66</sup> However, the judgment was overturned on appeal.<sup>67</sup> The reorganisation eventually proceeded by means of a scheme of arrangement, which was approved in 2000.<sup>68</sup>

The NSW Court of Appeal decision in *Heydon v NRMA Ltd* subjected the decision in *Gambotto* to intense scrutiny. The two critical questions in that case were, first, whether the NRMA’s demutualisation proposal constituted an expropriation of members’ rights, and whether the *Gambotto* principles were applicable. Second, whether the decision in *Gambotto* was consistent with previous judicial authority or whether it was a departure from previous law. These issues are discussed below.

*Gambotto* therefore had an immediate effect on the approach adopted by legal practitioners, including significantly altering a large corporate reconstruction, as well as forcing the reconsideration of other corporate actions.

### **C *Gambotto* as a Radical Change in Company Law**

Many commentators saw *Gambotto* as representing a radical change from previous decisions. Whincop described the decision in *Gambotto* as “judicial legislation that ignores precedent”.<sup>69</sup> In an article in the *Australian Financial Review*, Chris Merritt wrote that the ruling “has radically altered the balance of power within corporate Australia”.<sup>70</sup> Whincop and Keyes stated that the High Court “changed the substantive law in this area”.<sup>71</sup>

Kevans saw the decision, and the fairness test in particular, as remarkable because it represented an interventionist approach which differed markedly from the previous tradition of non-interference.<sup>72</sup> Boros noted that the decision was a departure from the

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<sup>63</sup> Quentin Digby, “The Implications of *Gambotto* for Non-Takeover Aspects of Compulsory Acquisitions: A Comment” in Ian M Ramsay (ed), *Gambotto v WCP Ltd: Its Implications for Corporate Regulation* (Centre for Corporate Law and Securities Regulation, University of Melbourne, 1996) at 73.

<sup>64</sup> Approval to convene the required meetings of members was granted in *Re NRMA Ltd (No 1)* (2000) 156 FLR 349; (2000) 33 ACSR 595.

<sup>65</sup> Kathryn Bice, “Failed NRMA Float Sinks Lawyers”, *Australian Financial Review*, 14 May 1999, 1.

<sup>66</sup> *NRMA Ltd v Morgan* (1999) 31 ACSR 435; (1999) 17 ACLC 1029 (Giles J).

<sup>67</sup> *Heydon v NRMA Ltd* (2000) 51 NSWLR 1; (2000) 36 ACSR 462; (2001) 19 ACLC 1; (2001) Aust Torts Reports 81-588 (Malcolm A-JA, McPherson A-JA and Ormiston A-JA).

<sup>68</sup> *Re NRMA Ltd (No 2)* (2000) 156 FLR 412; (2000) 34 ACSR 261; (2000) 18 ACLC 533.

<sup>69</sup> Whincop, above n 58 at 112.

<sup>70</sup> Chris Merritt, “*Gambotto*: A Roar Deal for Corporate Mice,” *Australian Financial Review*, 9 March 1995, 1.

<sup>71</sup> Michael J Whincop and Mary E Keyes, “Corporation, Contract, Community: An Analysis of Governance in the Privatisation of Public Enterprise and the Publicisation of Private Corporate Law” (1997) 25 *Federal Law Review* 51 at 82.

<sup>72</sup> Kevans, above n 36 at 110, 116.

essentially subjective test of the English authorities and diverged from those authorities by placing the onus on those effecting the expropriation to show its validity.<sup>73</sup>

This question was one of the crucial issues in *Heydon v NRMA Ltd*, in which all three judges held that *Gambotto* was a departure from the previous law. Malcolm A-JA stated that *Gambotto* “substantially altered the settled law”,<sup>74</sup> and Ormiston A-JA held that *Gambotto* “went far beyond anything which could fairly have been forecast by considering existing authority and the relevant text writers”.<sup>75</sup> Malcolm A-JA stated that *Gambotto* substantially altered the settled law by stipulating a very narrow range of permitted purposes for expropriation; reversing the onus of proof; drawing a sharp distinction between expropriatory constitutional provisions introduced when a company is incorporated and after it is incorporated; and introducing new fairness requirements.<sup>76</sup>

Two other commentators saw the decision as consistent with previous cases. Mitchell said that *Gambotto* largely reinstated the British authorities on expropriation of minority shares.<sup>77</sup> Her view of the older cases was that in the absence of a specific statutory power, it was not permissible for the majority to alter the constitution in order to acquire the shares of a minority shareholder.<sup>78</sup> Responding to the claims of Chris Merritt (noted above), Spender argued that the ratio of *Gambotto* was in fact “narrow and moderate” and consistent with previous authority.<sup>79</sup>

Evaluating the consistency of *Gambotto* with previous authority is complicated by the inconsistencies in those earlier cases, including the fact that the High Court in *Peters* had rejected the “bona fide in the benefit of the company as a whole” test, but laid down no definitive test in its place.<sup>80</sup> It can be argued that there was no authoritative test prior to *Gambotto*.

The High Court’s reversal of the traditional onus of proof<sup>81</sup> represents a clear departure from the previous position. However, some aspects of the *Gambotto* judgment are consistent with previous authority. Many decisions stood for the proposition that the voting power of majority shareholders was to be exercised subject to equitable principles

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<sup>73</sup> Elizabeth Boros, *Minority Shareholders’ Remedies* (Clarendon Press, 1995), 209.

<sup>74</sup> *Heydon v NRMA Ltd* (2000) 51 NSWLR 1 at [229].

<sup>75</sup> *Ibid* at [600] (Ormiston A-JA). See also at [571], [586] (Ormiston A-JA) and [394]-[405] (McPherson A-JA). McPherson A-JA at [400] stated: “Judging by the number of opinions, journal articles and comments it generated, the decision of the High Court in *Gambotto* came as a surprise to most if not all of those in the profession who specialise in company law”.

<sup>76</sup> *Ibid* at [229].

<sup>77</sup> Referring to *Brown v British Abrasive Wheel Co Ltd* [1919] 1 Ch 290; *Dafen Tinsplate Co Ltd v Llanelly Steel Co* (1907) *Ltd* [1920] 2 Ch 124 and *Sidebottom v Kershaw, Leese and Co Ltd* [1920] 1 Ch 154; Vanessa Mitchell, “The High Court and Minority Shareholders” (1995) 7 *Bond Law Review* 58.

<sup>78</sup> Vanessa Mitchell, “Protecting Minorities – *Gambotto*’s case and the Bona Fide Doctrine” (1997) 49(11) *Australian Company Secretary* 468.

<sup>79</sup> Spender, above n 44 at 103, referring to *Gambotto v WCP Ltd* (1995) 182 CLR 432 at 439-42, which in turn referred to *Re Bugle Press Ltd* [1961] Ch 270.

<sup>80</sup> *Peters’ American Delicacy Co Ltd v Heath* (1939) 61 CLR 457 at 481 (Latham CJ, McTiernan JJ agreeing), 495 (Rich J) and 512 (Dixon J).

<sup>81</sup> *Ibid* at 482 (Latham CJ).

of fraud on a power.<sup>82</sup> *Gambotto* is an example of such limitations.<sup>83</sup> Fraud on the minority was a well-established principle of company law and would have been applicable to the *Gambotto* situation.<sup>84</sup>

The former cases had shown hostility to constitutional amendments introducing expropriation provisions,<sup>85</sup> but although they were generally invalid, they were not necessarily so.<sup>86</sup> Where an expropriation merely amounted to the aggrandisement of the majority at the expense of the minority, the amendment would be impermissible.<sup>87</sup> However, where there was a valid reason for the expropriation, and it was accompanied by fair compensation, then the amendment would likely be acceptable. A valid reason included protecting the company from detriment,<sup>88</sup> removing a competing shareholder<sup>89</sup> or a shareholder who was acting in a manner which was damaging to the company's interests.<sup>90</sup>

These cases made it clear that the mere wish of the majority was not sufficient to justify an expropriation. There had to be a valid reason.<sup>91</sup> This is similar to a proper purpose requirement,<sup>92</sup> although the precise scope of what constituted a proper purpose was not clear. The no oppression requirement has some similarity with the cases which had placed importance on oppression or unfairness as an element of the test for determining the validity of alterations to the articles.<sup>93</sup>

*Gambotto* thus picks up a number of threads scattered throughout the previous decisions. However, *Gambotto* laid down a test which goes beyond those cases, and reversed the onus of proof. *Gambotto* differs from prior authority not by the fact that it places obstacles in the way of would-be expropriators, but in the restrictive nature of the test that it laid down.

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<sup>82</sup> Stefan Lo, "The Continuing Role of Equity in Restraining Majority Shareholder Power" (2004) 16 *Australian Journal of Corporate Law* 96 at 97; see generally Yuri Grbich, "Fraud on a Power: Judicial Control of Appointments by Discretionary Trustees" (1977) 3 *Monash University Law Review* 210.

<sup>83</sup> Digby, above n 63 at 73.

<sup>84</sup> Cf B H McPherson, "Limits of Fraud on the Minority" (1960) 77 *South African Law Journal* 297 at 298.

<sup>85</sup> Robert R Pennington, *Company Law* (6th ed, Butterworths, 1990) at 81.

<sup>86</sup> H A J Ford and R P Austin, *Ford's Principles of Corporations Law* (Butterworths, 6<sup>th</sup> ed, 1992) at [1704].

<sup>87</sup> *Peters' American Delicacy Co Ltd v Heath* (1939) 61 CLR 457.

<sup>88</sup> Pennington, above n 85 at 81.

<sup>89</sup> *Sidebottom v Kershaw, Leese and Co Ltd* [1920] 1 Ch 154.

<sup>90</sup> *Re Bugle Press Ltd* [1961] Ch 270 at 287.

<sup>91</sup> *Brown v British Abrasive Wheel Co Ltd* [1919] 1 Ch 290; *Dafen Tinplate Co Ltd v Llanelly Steel Co (1907) Ltd* [1920] 2 Ch 124; *Sidebottom v Kershaw, Leese and Co Ltd* [1920] 1 Ch 154.

<sup>92</sup> See also *Shuttleworth v Cox Brothers and Co (Maidenhead) Ltd* [1927] 2 KB 9 at 18: "the alteration of a company's articles shall not stand if it is such that no reasonable men could consider it for the benefit of the company".

<sup>93</sup> *Allen v Gold Reefs of West Africa Ltd* [1900] 1 Ch 656 at 676 (Vaughan Williams LJ); *Brown v British Abrasive Wheel Co Ltd* [1919] 1 Ch 290 at 294; *Dafen Tinplate Co Ltd v Llanelly Steel Co (1907) Ltd* [1920] 2 Ch 124 at 137; *Peters' American Delicacy Co Ltd v Heath* (1939) 61 CLR 457 at 486, 491 (Latham CJ), 513 (Dixon J); F G Rixon, "Competing Interests and Conflicting Principles: An Examination of the Power of Alteration of Articles of Association" (1986) 49 *Modern Law Review* 446 at 462; Pennington, above n 85 at 81.

## D Differing Interpretations of *Gambotto* and its Broader Implications

This section considers where *Gambotto* fits within broader trends in corporate law and the philosophical approach of the courts, together with its implications more generally for corporate law. As with most aspects of the decision, opinion is divided.

Many commentators saw *Gambotto* as representing a definite shift in the High Court's basic policy regarding minority shareholders and compulsory acquisition.<sup>94</sup> Writing shortly after the decision, it was said that "the High Court has placed new emphasis on the rights of minority shareholders and has carved out an important role for itself as a custodian of those rights".<sup>95</sup> Renard questioned whether the court's "basic philosophical approach to compulsory acquisition may diverge from that previously taken by Australian and English courts".<sup>96</sup> Chin stated that *Gambotto* represented "a considerable shift in philosophy with a new balance struck in the favour of the minority shareholder".<sup>97</sup>

One writer went so far as to say that "the High Court was prepared to countenance an expropriation of shares in the narrowest of circumstances, the rights of shareholders being prima facie absolute".<sup>98</sup> Fridman stated that the essence of the majority's decision in *Gambotto* was the focus on property rights as pivotal, and that this leads to a conclusion that compulsory acquisitions are in principle impermissible.<sup>99</sup> Ormiston A-JA expressed a similar view in *Heydon v NRMA Ltd*.<sup>100</sup>

Spender saw the decision as placing a primary emphasis upon the right of minority shareholders to hold their shares, with shareholders having a legitimate expectation to hold their shares until they wish to sell or the company is wound up.<sup>101</sup> Hughes wrote that the law has traditionally proceeded on the basis of economic justifications, effectively ignoring the proprietary nature of the minority shareholder's interest, and that *Gambotto* represents a departure from this trend.<sup>102</sup>

This perceived change in the attitude of the courts potentially had far reaching effects, with a number of commentators expressing concern that the *Gambotto* principles may "infect" other areas of law.<sup>103</sup> Whincop and Keyes noted that the rule only applied to

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<sup>94</sup> Note in this context the discussion regarding the nature of shares as property, which is discussed below.

<sup>95</sup> Ian M Ramsay, "Key Aspects of the Decision of the High Court in *Gambotto v WCP Limited*" in Ian M Ramsay (ed), *Gambotto v WCP Ltd: Its Implications for Corporate Regulation* (Centre for Corporate Law and Securities Regulation, University of Melbourne, 1996) at 7.

<sup>96</sup> Ian Renard, "The Implications of *Gambotto* for Takeovers: A Comment" in Ian M Ramsay (ed), *Gambotto v WCP Ltd: Its Implications for Corporate Regulation* (Centre for Corporate Law and Securities Regulation, University of Melbourne, 1996) at 77-8.

<sup>97</sup> Chin, above n 37 at 443.

<sup>98</sup> Roger Walton, "*Gambotto v WCP Ltd*: A Justified Reassertion of Minority Shareholder Rights or Unwelcome Step Back In Time" (2000) 12 *Australian Journal of Corporate Law* 20 at 28.

<sup>99</sup> Fridman, above n 46 at 118. See also *WCP v Gambotto* (1993) 30 NSWLR 385 at 389 (Meagher JA).

<sup>100</sup> (2000) 51 NSWLR 1; (2000) 36 ACSR 462; (2001) 19 ACLC 1 at [481].

<sup>101</sup> Spender, above n 44 at 104.

<sup>102</sup> Hughes, above n 39 at 204.

<sup>103</sup> George Durbridge, "A Decade of Compulsory Acquisition" (paper presented at the Centre for Corporate Law and Securities Regulation seminar, Compulsory Acquisition: Key Issues and Developments, Melbourne, 6 June 2002), 22-5. Our thanks to Mr Durbridge for his efforts in locating this paper.

alterations to the constitution which conferred expropriation power, but said that it was not difficult to envisage the principles spreading more broadly to other situations.<sup>104</sup>

Robson predicted that “a superior court will eventually apply *Gambotto* to all methods of expropriating the minority in a takeover”.<sup>105</sup> Mitchell opined that the decision would have serious implications for other areas such as takeovers and reconstructions.<sup>106</sup> Bird suggested that *Gambotto* put in doubt expropriation by the non-orthodox expropriation schemes.<sup>107</sup> Renard and Santamaria believed that the High Court in *Gambotto* gave “a strong hint” that greater disclosure would be required for compulsory acquisitions under s 414.<sup>108</sup>

Other commentators saw the High Court’s decision as having a narrower reach in seeking to protect minority shareholders by preventing majority shareholders from circumventing the statutory safeguards. One writer noted that *Gambotto* was solely concerned with expropriations effected by an amendment to the constitution.<sup>109</sup> Digby stated that it was clear “that the High Court was motivated by a concern that if the Court permitted a *Gambotto* style “expropriation” it would render superfluous the various statutory methods of compulsory acquisition”.<sup>110</sup>

Renard wrote that the High Court “justified the tough stance it took on the validity of an expropriation article because the *Corporations Law* provides express procedures in ss 414 and 701 for compulsory acquisition”.<sup>111</sup> Contrary to Ormiston A-JA’s view noted above, McPherson A-JA in *Heydon v NRMA Ltd* stated that “[i]t is essential to bear in mind that it is not the fact of expropriation that constitutes oppression. It is the action of amending the articles that was singled out by the High Court in *Gambotto* as impermissible”.<sup>112</sup>

Other commentators saw *Gambotto* as consistent with trends in corporate law.<sup>113</sup> MacIntosh traced several developments in corporate law, arguing that these evidence a revitalisation of the rule in *Allen’s* case, which has led to greater protections for minorities against discriminatory treatment, together with a winding back of the traditional deference paid to the majority.<sup>114</sup> Boros argued in a similar vein that *Gambotto*

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<sup>104</sup> Whincop and Keyes, above n 71 at 86.

<sup>105</sup> Ken Robson, “Expropriating the Minority” (1997) 71 *Australian Law Journal* 679 at 680.

<sup>106</sup> Vanessa Mitchell, “Victory for Minority Shareholders” (1995) 16(7) *Company Lawyer* 219.

<sup>107</sup> Helen Bird, “A Critique of the Proprietary Nature of Share Rights in Australian Publicly Listed Corporations” (1998) 22 *Melbourne University Law Review* 131 at 145.

<sup>108</sup> I Renard and J G Santamaria, *Takeovers and Reconstructions in Australia* (Looseleaf, Butterworths) at [1222].

<sup>109</sup> Chin, above n 37 at 414.

<sup>110</sup> Digby, above n 63 at 71.

<sup>111</sup> Renard, above n 96 at 76.

<sup>112</sup> (2000) 51 NSWLR 1; (2000) 36 ACSR 462; (2001) 19 ACLC 1 at [393].

<sup>113</sup> In the American context, see Anupam Chander, “Minorities, Shareholder and Otherwise” (2003-2004) 113 *Yale Law Journal* 119.

<sup>114</sup> Jeffrey G MacIntosh, “Minority Shareholder Rights in Canada and England: 1860-1987” (1989) *Osgoode Hall Law Journal* 561. Cf also M J Trebilcock, “A New Concern for the Minority Shareholder” (1973) 19 *McGill Law Journal* 106.



follows recent trends towards “a more sympathetic hearing of minority shareholder complaints”.<sup>115</sup>

In contrast, Kent and Vary argued that developments up to 1991 relating to compulsory acquisition led to the conclusion that parliament and the courts exhibited a tendency to privilege the interests of commercial efficiency over the rights of minority shareholders.<sup>116</sup>

Outside the corporate law context, Paul Finn argued that *Gambotto* fits within a broader trend of regulating the exercise of power. *Gambotto* is an example of the common law controlling the exercise of power in situations where the power has been exercised in a manner that is disproportionate or unfair,<sup>117</sup> and is consistent with the approaches in other cases.<sup>118</sup>

In a series of articles Whincop saw a number of trends reflected in *Gambotto*. The decision was seen as following a broader trend of the increasing “publicisation” of private corporate law, where “the black box of corporate discretions and procedures is increasingly being opened to judicial review”.<sup>119</sup> The High Court effectively elevated a company’s articles into something resembling “the constitution of a polity”,<sup>120</sup> such that public institutions define the scope of legitimate corporate behaviour.<sup>121</sup> Pentony expressed a similar view, arguing that *Gambotto* “displays a willingness on the part of the court to play a more interventionist role in a corporation’s affairs”.<sup>122</sup>

Various commentators have considered the philosophy embodied in the majority’s decision. Whincop declared that the decision was not conservative as the High Court set forth new law on the subject.<sup>123</sup> Spender saw the normative approach of *Gambotto* as an “associative model”, where the corporation is conceived as “more connected and based on responsibility”. She also argued that much of the commentary on *Gambotto* criticised the decision from a liberal-utilitarian paradigm.<sup>124</sup>

Bird considered that *Gambotto*’s majority judges’ conception of property resembled John Locke’s labour theory of property, while McHugh J favoured a utilitarian account of

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<sup>115</sup> Elizabeth Boros, “Altering the Articles of Association to Acquire Minority Shareholdings” in Barry A K Rider (ed), *The Realm of Company Law* (Kluwer, 1998).

<sup>116</sup> Wayne Kent and Leonard Vary, “Compulsory Acquisition of Shares” (1991) 9 *Company and Securities Law Journal* 261 at 262.

<sup>117</sup> Paul Finn, “Controlling the Exercise of Power” (1996) 7 *Public Law Review* 86.

<sup>118</sup> Among others, *Stern v McArthur* (1988) 165 CLR 489; *Nationwide News Pty Ltd v Wills* (1992) 177 CLR 1; and *Australian Capital Television Pty Ltd v Commonwealth (No 2)* (1992) 177 CLR 106 were cited as examples.

<sup>119</sup> Whincop and Keyes, above n 71 at 84-5.

<sup>120</sup> Michael J Whincop, “Liberalism, Conservatism, and Economic Efficiency: Tradition and Change in the Values of Corporate Law” (2000) 23 *University of New South Wales Law Journal* 111 at 139.

<sup>121</sup> Michael J Whincop, “The Institutional Politics of Corporate Law in Australia: From *Gambotto* to *DB Management*” (2000) 11 *Australian Journal of Corporate Law* 247.

<sup>122</sup> Brendan Pentony, “Majority Interests v Minority Interests: Achieving a Balance” (1995) 5 *Australian Journal of Corporate Law* 117 at 119.

<sup>123</sup> Whincop, above n 120 at 139.

<sup>124</sup> Spender, above n 44 at 126.

property.<sup>125</sup> One of the most strident critics of the decision was Saul Fridman, who saw the decision as strongly asserting property rights, and establishing a “property rule”, one which privileges the concept of property and a property owner’s right to hold that property.<sup>126</sup> DeMott agreed that *Gambotto* applies a property rule: “each shareholder has an absolute veto over the sale of his shares, unless the majority establishes his continuing ownership itself to be detrimental”.<sup>127</sup>

Mitchell argued that the crucial factor in *Gambotto* was not the assertion of the proprietary nature of shares.<sup>128</sup> The High Court was instead concerned to ensure fairness between the parties, based on an “individualist” jurisprudential approach<sup>129</sup> which highlights the significance and rights of the individual,<sup>130</sup> and follows the High Court’s approach in cases such as *Mabo*<sup>131</sup> and *Theophanous*.<sup>132</sup> That is, there must be some justifiable purpose for an expropriation above the mere wish of the majority.<sup>133</sup>

These different views of commentators indicate the difficulty of identifying the philosophy underpinning the decision in *Gambotto*.

### E Criticisms of the Test

We noted above that the High Court rejected the “bona fide in the interests of the company” test when there are competing interests of shareholders. In its place the High Court laid down the two-pronged proper purpose and no oppression test.

Given the inadequacies of the former position, the High Court’s rejection of the bona fide test was welcomed by commentators. Fridman applauded the High Court’s rejection of the *Allen* test.<sup>134</sup> Chin stated that the bona fide test was more applicable to directors who owe fiduciary duties to the company,<sup>135</sup> and Prentice said that “[t]here is much to commend the approach: the problem is what to put in its place”.<sup>136</sup>

However, the test that the High Court did put in its place was widely criticised by commentators. Whincop saw the *Gambotto* test as the reintroduction of the discredited tests applied in earlier English judgments, which imposed a positive requirement that the

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<sup>125</sup> Bird, above n 107 at 147.

<sup>126</sup> Fridman, above n 46 at 131.

<sup>127</sup> Deborah DeMott, “Proprietary Norms in Corporate Law: An Essay on Reading *Gambotto* in the United States” in Ian M Ramsay (ed), *Gambotto v WCP Ltd: Its Implications for Corporate Regulation* (Centre for Corporate Law and Securities Regulation, University of Melbourne, 1996) at 97.

<sup>128</sup> Mitchell, above n 77. See also Whincop, above n 121.

<sup>129</sup> Ibid.

<sup>130</sup> Ibid at 62.

<sup>131</sup> *Mabo v Queensland (No 2)* (1992) 175 CLR 1.

<sup>132</sup> *Theophanous v Herald and Weekly Times Ltd* (1994) 182 CLR 104.

<sup>133</sup> Vanessa Mitchell, “The US Approach Towards the Acquisition of Minority Shares: Have we Anything to Learn?” (1996) 14 *Company and Securities Law Journal* 283 at 304.

<sup>134</sup> Fridman, above n 46 at 119.

<sup>135</sup> Chin, above n 37 at 421.

<sup>136</sup> D D Prentice, “Alteration of Articles of Association - Expropriation of Shares” (1996) 112 *Law Quarterly Review* 194 at 196.

alteration be in good faith and in the interests of the company as assessed by the court, and which had been rejected in the *Shuttleworth* and *Peters* cases.<sup>137</sup>

One commentator argued that the benefit of the company as a whole test should be applied with greater vigour, and rather than giving primacy to shareholder interests, courts should consider a broader range of stakeholders.<sup>138</sup> Cilliers and Luiz criticised *Gambotto* for distinguishing between expropriatory and non-expropriatory alterations, which amounts to “reverse reasoning”.<sup>139</sup> Prentice agreed that the distinction “is unsatisfactory and very difficult to apply”.<sup>140</sup>

Fridman argued that the distinction between transactions which secure a benefit and those which avoid a detriment is meaningless as both ultimately amount to the same thing.<sup>141</sup> Arvanitis stated that the distinction is artificial,<sup>142</sup> and Kevans argued that the distinction was “logically tenuous at best”, preferring instead McHugh J’s test.<sup>143</sup>

Prentice proposed, in place of the majority’s test, that a constitutional alteration which beneficially affects the entitlements of some shareholders and prejudices the entitlements of others should only be valid “if there are commercial reasons justifying the alteration”.<sup>144</sup>

Overwhelmingly, the commentators saw the proper purpose requirement as the most troubling element of the decision. Cilliers and Luiz argued that the proper purpose requirement is unhelpful, perpetuating the same error as the English cases after *Allen*, and should be rejected in favour of a single fairness requirement.<sup>145</sup> Robson argued that the proper purpose test “has no relevance at all” and the courts should confine themselves to considering fairness.<sup>146</sup>

Evaluations by commentators of the tests in *Gambotto* were not all negative. Chin argued that the proper purpose test was preferable to the bona fide test and should be adopted in New Zealand.<sup>147</sup> Chan and Law argued that the fairness requirement laid down by *Gambotto* was appropriate,<sup>148</sup> and the High Court’s reversal of the onus of proof was said

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<sup>137</sup> Whincop, above n 58 at 107, 111, referring to *Shuttleworth v Cox Brothers and Co (Maidenhead) Ltd* [1927] 2 KB 9 and *Peters’ American Delicacy Co Ltd v Heath* (1939) 61 CLR 457. Whincop argued that the test should be: where an alteration “achieves a genuine benefit to the corporation by maximising the value of its assets, the alteration should stand” unless it infringes the test applied by Latham CJ in *Peters*: *ibid* at 115.

<sup>138</sup> Andrea Corfield, “The Stakeholder Theory and Its Future in Australian Corporate Governance: A Preliminary Analysis” (1998) 10 *Bond Law Review* 213 at 226.

<sup>139</sup> Cilliers and Luiz, above n 48 at 102.

<sup>140</sup> Prentice, above n 136 at 197.

<sup>141</sup> Fridman, above n 46 at 121-2. See also Whincop, above n 58 at 111.

<sup>142</sup> K Gary Arvanitis, “Gambotto and Anor v WCP Ltd” (1995) 13 *Company and Securities Law Journal* 326 at 328.

<sup>143</sup> Kevans, above n 36 at 113, 115.

<sup>144</sup> Prentice, above n 136 at 196.

<sup>145</sup> Cilliers and Luiz, above n 48 at 104-6.

<sup>146</sup> Robson, above n 105 at 681.

<sup>147</sup> Chin, above n 37.

<sup>148</sup> Sen Hwei Chan and Larelle Law, “Interests of the Company as a Whole: An Economic Appraisal of Fiduciary Controls” (1999) 20 *University of Queensland Law Journal* 186 at 199.

to be “an undoubted improvement on the position in England” which placed the burden on the objectors.<sup>149</sup>

## F The Conception of Shares as Property

One of the most controversial aspects of the High Court’s decision in *Gambotto* was the court’s conception of shares. The majority said that a share “is more than a “capitalized dividend stream”: it is a form of investment that confers proprietary rights on the investor”.<sup>150</sup> This reflects the belief that shares are items of property which have intrinsic value in addition to their monetary value, and challenges the view that a share is merely a defeasible interest.<sup>151</sup> As a consequence, shares cannot be expropriated in the absence of specific legislative power to do so.<sup>152</sup> This was widely seen as a critical aspect of the decision whereby minority shareholders’ rights were strengthened and expropriations were prima facie unacceptable.<sup>153</sup>

Renard suggested that *Gambotto* represented a fundamental change in the courts’ attitude towards shareholding and compulsory acquisition in general.<sup>154</sup> The consequence would be that the *Gambotto* principles would encroach upon other areas of corporate law, including methods of expropriation.

Many commentators rejected the High Court’s view of the nature of a share and argued instead that shares should be seen as defeasible property. Kevans argued that the property conception of a share was not acceptable for public companies where shareholders are usually passive investors with no expectations of participation other than receiving a return.<sup>155</sup> Walton argued that entitlements attaching to shares are defeasible, rights attaching to shares are conditional, and so shares are property in name only.<sup>156</sup> Elliot argued that there is no basis to view minority interests as sacrosanct; an expropriation should be fair if an independently determined fair price is paid,<sup>157</sup> which is the position now adopted in Part 6A.2 of the *Corporations Act*.<sup>158</sup>

Bird discussed this question in detail, arguing that the power to alter the constitution makes certain share rights defeasible. Numerous provisions of the corporations legislation restrict or override property principles in relation to shares, and so as the core elements of property, namely indefeasibility, exclusivity and voluntary transfer rights, do not exist or are subject to restriction or destruction, with the result that it is difficult to argue that shares are property.<sup>159</sup>

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<sup>149</sup> Prentice, above n 136 at 196.

<sup>150</sup> *Gambotto v WCP Ltd* (1995) 182 CLR 432 at 447. McHugh J held a similar view of the nature of a share: see his comments at 453.

<sup>151</sup> Boros, above n 115 at 124.

<sup>152</sup> Mitchell, above n 133 at 303, Mitchell, above n 13 at 108.

<sup>153</sup> Cf Cilliers and Luiz, above n 48 at 101-2.

<sup>154</sup> Renard, above n 96 at 77-8.

<sup>155</sup> Kevans, above n 36 at 114.

<sup>156</sup> Walton, above n 98.

<sup>157</sup> Andrew Elliott, “WCP Limited v Gambotto & Anor: Expropriation of Minority Shareholding is not a *Malum in se*” (1994) 19 *Melbourne University Law Review* 776 at 780.

<sup>158</sup> Alberto Colla, “Eliminating Minority Shareholdings - Recent Developments” (2001) 19 *Company and Securities Law Journal* 7 at 25. Part 6A.2 is discussed later in this article.

<sup>159</sup> Bird, above n 107 at 131.

Fridman argued that a share is a chose in action and thus should be seen as analogous to a contract. The right to specific performance of a contract is generally restricted to cases where the property involved is unique. As shares represent nothing more than an investment which can readily be replaced, shareholders should not be able to resist the expropriation of shares.<sup>160</sup> Prentice characterised this capitalised dividend stream conception of a share as “not widely recognised in company law but it is one that has a place albeit solely through legislative reform”.<sup>161</sup>

Other commentators defended the High Court’s reasoning. Hughes argued that a share confers valuable property rights.<sup>162</sup> Arvanitis argued that the Court of Appeal judgment did not give sufficient weight to the proprietary nature of a share, and that only in extreme circumstances should shares be permitted to be taken away.<sup>163</sup> Chin argued that shares are property, and as a consequence the power of expropriation is extraordinary as it involves the compulsorily taking away of property.<sup>164</sup>

McConvill argued that the fact that the assets of the company are separate from those of the shareholder does not preclude shares being characterised as property, for the proprietary rights attach to the shares themselves. Shares carry the traditional indicia of ownership, being the right to use, exclude and alienate in relation to the shares, and shareholders are the ultimate owners of the company, even if they do not exercise day-to-day control over the affairs of the company.<sup>165</sup> There is thus no reason to doubt the long held doctrine that shares are:

a species of intangible movable property which comprise a collection of rights and obligations relating to an interest in a company of an economic and proprietary character, but not constituting a debt.<sup>166</sup>

Spender, in a detailed analysis responding to the claims of Bird, Whincop and others, analysed the characteristics of shares,<sup>167</sup> concluding that “shares overwhelmingly have the character of property” and that defeasible interests may still be property interests.<sup>168</sup> The proper characterisation of a share is as a chose in action, and the contractual and proprietary aspects of a share cannot be separated. According to Spender, proprietary rights are essential to the nature of a share and property should only be taken where there is a public benefit involved, but this was not the case in *Gambotto*.

It is evident from this review that *Gambotto* elicited vigorous and divergent responses with respect to the High Court’s interpretation of shares as a form of property.

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<sup>160</sup> Saul Fridman, “*WCP Ltd v Gambotto*: An Opportunity for the High Court to set Some Corporate Law Norms” (1994) 22 *Federal Law Review* 205 at 211.

<sup>161</sup> Prentice, above n 136 at 197.

<sup>162</sup> Hughes, above n 39 at 198.

<sup>163</sup> Arvanitis, above n 142 at 328.

<sup>164</sup> Chin, above n 37 at 415.

<sup>165</sup> James McConvill, “Do Shares Constitute Property? Reconsidering a Fundamental, yet Unresolved, Question” (2005) 79 *Australian Law Journal* 251.

<sup>166</sup> Robert Pennington, “Can Shares in Companies be Defined?” (1989) 10 *Company Lawyer* 140 at 144.

<sup>167</sup> A M Honoré, “Ownership” in Anthony Guest (ed), *Oxford Essays in Jurisprudence* (1961), 107-147.

<sup>168</sup> Spender, above n 44 at 115.

#### IV *GAMBOTTO* AND THE ROLE OF THE HIGH COURT

One way of interpreting *Gambotto* is to place it in the broader political context of the role of the High Court at the time of the decision. The judges who participated in *Gambotto* were Mason CJ and Brennan, Deane, Dawson and McHugh JJ.

In his book on the High Court under the leadership of Chief Justice Mason, Jason Pierce documents what he refers to as a “transformation” of the High Court that started in the mid-1980s and continued until the mid-1990s<sup>169</sup> (*Gambotto* was decided in 1995 and in that same year Mason CJ retired from the court).

The court “shifted its institutional focus away from simply resolving legal disputes to making policy that addressed some of the country’s most controversial issues”.<sup>170</sup> An emphasis on individual justice underpinned the court’s approach to deciding these issues. The controversial issues included aboriginal land rights,<sup>171</sup> the right of a defendant in criminal proceedings to legal counsel,<sup>172</sup> and an interpretation of the Australian constitution that implied into the constitution certain fundamental rights and freedoms such as an implied freedom of political speech.<sup>173</sup>

This transformation in the role of the High Court involved several aspects.<sup>174</sup> First, there was less emphasis on certainty and more emphasis on fairness and individual justice. Second, litigation before the High Court was viewed not primarily as a process for resolving private disputes but as both a legal and political enterprise. Third, the judges clearly saw themselves as making the law rather than interpreting it. It was a political conception of the judicial role and, as a result, the High Court would occupy “a more visible, powerful, and therefore controversial place in the political system”.<sup>175</sup> Fourth, there was greater acceptance by the judges that their decision-making may require them to draw from community values. Fifth, the court saw itself as less constrained by legal precedent. Sixth, the court saw itself as an active agent for change within the broader political system. Litigation before the court was “conceived as a legal and political enterprise where broad social policy may be established.”<sup>176</sup>

The decision of the High Court in *Gambotto* is not referred to by Pierce in his book. The focus of the book is on constitutional decisions of the Mason court. However, when we interpret *Gambotto*, it is desirable to understand the approach of the High Court to other cases it decided in the previous 10 years. The emphasis on fairness and individual rights that underpinned the court’s constitutional decisions resonates strongly with the decision in *Gambotto*. The court defined very narrowly the purposes for which a company could amend its constitution to expropriate the shares of a minority shareholder, even when the

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<sup>169</sup> Jason L Pierce, *Inside the Mason Court Revolution: The High Court of Australia Transformed* (Carolina Academic Press, 2006).

<sup>170</sup> *Ibid* at 4.

<sup>171</sup> *Mabo v Queensland (No 2)* (1992) 175 CLR 1.

<sup>172</sup> *Deitrich v The Queen* (1992) 177 CLR 292.

<sup>173</sup> *Nationwide News Ltd v Wills* (1992) 177 CLR 1.

<sup>174</sup> The points in this paragraph are summarised from Pierce, above n 169, Chapters 4 and 5.

<sup>175</sup> *Ibid* at 111.

<sup>176</sup> *Ibid* at 5.

price for the shares was fair. It was not sufficient justification according to the court for the expropriation to advance the commercial interests of the company. The court therefore enhanced the rights of minority shareholders. At the same time, the language of the court is rights focussed. For example, McHugh J states:

...to require shareholders to sell their shares against their will is an infringement of their rights as autonomous beings to make their own decisions and to carry out their own actions. In a society and under a legal system that is predicated on its members being free and equal agents any interference with the autonomy of any individual needs to be justified if it is not to be regarded as oppressive.<sup>177</sup>

Given that, according to Pierce, a theme of the High Court under Mason CJ was its emphasis on fairness and individual justice, it is also important to note the underpinning theme of fairness in *Gambotto*. We have already observed how the test adopted by the majority judges required that an amendment of the constitution allowing the majority shareholders to expropriate the shares of the minority must be for a proper purpose and must also be fair – with fairness in this context requiring disclosure by the majority shareholders of all relevant information, valuation of the shares by an independent expert, and a fair price to be paid for the shares to be expropriated.

Other aspects of the transformation of the High Court under Mason CJ identified by Pierce can also be seen in *Gambotto*. For example, many commentators and other courts saw *Gambotto* as a radical change in the law.<sup>178</sup> In this sense, the decision fits with the themes of the court seeing itself as less bound by legal precedent, as an agent of change, and making the law rather than interpreting it.

Another matter can be mentioned. It is the type of legal reasoning adopted by the Mason court in constitutional law matters and how this reasoning relates to that of the court in *Gambotto*. Pierce observes that under Mason CJ, the High Court heard more constitutional law matters and these constitutional matters were individual, rights-oriented disputes.<sup>179</sup> The constitutional disputes heard by the court “dealt more with individuals’ interactions with government...than disputes between the state and national governments”.<sup>180</sup> *Gambotto* involved the validity of a provision in the constitution of WCP Ltd and the court balanced the interests of not only the minority and majority shareholders but also the commercial interests of the company. The type of legal reasoning adopted by the Mason court in the cases interpreting the Australian constitution can be seen to some extent in *Gambotto*. One aspect of the legal reasoning of the Mason court was implying rights into the Australian constitution. In *Gambotto*, the court considered the validity of a new provision of the company’s constitution that empowered any shareholder who was entitled to 90% or more of the issued shares of the company to acquire all the remaining shares in the company at the price of \$1.80 per share. The court introduced significant restrictions on the power to insert such an amendment into a company’s constitution: the purpose for which such an amendment could be introduced was defined narrowly; majority shareholders need to disclose all relevant information

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<sup>177</sup> (1995) 182 CLR 432 at 456.

<sup>178</sup> See nn 69-93 and accompanying text.

<sup>179</sup> Pierce, above n 169 at 139.

<sup>180</sup> *Ibid* at 140.

leading up to the amendment of the constitution; the shares should be valued by an independent expert; the price for the shares must be fair; and the onus lies on those supporting the amendment to show that the power is validly exercised. The court can therefore be seen to imply into the company's constitution certain rights for minority shareholders.

A further aspect of the legal reasoning of the Mason court in constitutional matters was a departure from the orthodox preference for Australian and British legal precedent and a willingness to consider precedent from Anglo-American countries.<sup>181</sup> In *Gambotto*, the court referred to English precedent regarding when the constitution of a company could be amended to introduce a provision that would allow the majority to expropriate the shares of the minority. The court held, as have seen, that it is not sufficient justification that the expropriation would advance the commercial interests of the company. The court stated that this "approach does not attach sufficient weight to the proprietary nature of a share and, to the extent that English authority might appear to support such an approach, we do not agree with it."<sup>182</sup> The court therefore referred to English authority but in the context of not following it. However, the court did refer approvingly to Canadian and US authorities when holding that the majority shareholders must disclose all relevant information leading up to the amendment and the price to be paid for the shares must be fair.<sup>183</sup>

We therefore see how themes that underpin other decisions of the Mason court also underpin the decision in *Gambotto*. In his book, Pierce documents how the High Court subsequently retreated from the judicial activism of the Mason court.<sup>184</sup> This also resonates with the reaction of other courts to *Gambotto*. As we document in the following section, subsequent judgments largely limited *Gambotto* to its facts.

## V COURTS' RESPONSES TO *GAMBOTTO*

Given the potential breadth of the principles articulated by the High Court in *Gambotto*, some plaintiffs have sought to argue the extension of the principles to various types of corporate transactions and to structures and entities other than companies, such as unit trusts. For example, the principles were argued to have application in the context of the Commonwealth and Northern Territory Governments' implementation of policies regarding the Alice Springs aboriginal town camps.<sup>185</sup>

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<sup>181</sup> *Ibid* at 170.

<sup>182</sup> (1995) 182 CLR 432 at 446.

<sup>183</sup> *Ibid* at 446-447.

<sup>184</sup> Pierce, above n 169, Chapter 7.

<sup>185</sup> *Shaw v Minister for Families, Housing, Community Services and Indigenous Affairs* [2009] FCA 1397. The application was unsuccessful and the court distinguished *Gambotto*. The background to the case was that the Commonwealth Government was to invest substantial funds to improve living conditions in the town camps. It was a condition of the availability of these funds that the Commonwealth be granted subleases over the town camp areas for a minimum of 40 years to obtain security for its investment. The Housing Associations (which were the lessees in perpetuity of the town camps) agreed to sign the subleases. The applicants, who were residents of the town camps and members of the Housing Associations, argued, among other things, that the 40 year subleases were contrary to the interests of



This section reviews the responses to, and interpretations of, *Gambotto* in subsequent judicial decisions. Overall, the cases limit and restrict its reach. There are a small number of cases applying *Gambotto*. The vast majority of cases have limited *Gambotto*, holding that it does not apply outside its narrow facts.

### A Judgments Applying *Gambotto*

The authors' research has revealed no case that has extended the principles in *Gambotto* other than a decision that the principles apply to a body corporate formed under the *Strata Schemes Management Act 1996* (NSW).<sup>186</sup> There are several judgments that have applied *Gambotto*.

*Gambotto* was applied in *Gray Eisdell Timms Pty Ltd v Combined Auctions Pty Ltd*.<sup>187</sup> In that case the defendant company was set up as an auction house for pawnbrokers, and in response to the perceived threat of a takeover, the company inserted an article into its constitution which provided that if a member was not actively engaged in pawnbroking the company had the power to sell the member's shares. Young J held that as a result of *Gambotto*, such an expropriatory article was subject to special scrutiny and was only valid if the amendment was undertaken to prevent detriment to the company.

It was held that the amendment was not for a proper purpose and therefore not valid, for two reasons. First, one-third of the shareholders of the company were not currently involved in a pawnbroking business, suggesting that the amendment was not needed to protect the company. Second, the operation of the article was postponed for five years, also suggesting that the company was not facing an immediate threat.

*Gambotto* was also applied in *Bundaberg Sugar Ltd v Isis Central Sugar Mill Co Ltd*.<sup>188</sup> The defendant, Isis Central Sugar Mill, carried on the business of sugar production. It was also a co-operative company for tax purposes, permitting the company to claim deductions for distributions paid to shareholders. Isis had amended its constitution in 1987 in order to comply with the co-operative tax status provisions of the income tax legislation by inserting a number of articles which gave the company power to forfeit and sell the shares of a member who ceased to supply sugar to the company.

The court held that the provisions of the company's constitution came within the principles of *Gambotto* in that the provisions allowed for the expropriation of the shares of the minority by the majority. However, the provisions of the constitution were not invalid as they had been introduced for a proper purpose. The defendant company had for many years enjoyed substantial taxation benefits by reason of it being a co-operative company for the purposes of the income tax laws. The company could lose its co-operative status and its valuable tax deductions if there were continued shareholdings by persons who did not supply sugar to the company.

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members of the Housing Associations. The Associations were incorporated under either the *Associations Act* (NT) or the *Corporations (Aboriginal and Torres Strait Islander) Act 2006* (Cth).

<sup>186</sup> *Young v The Owners Strata Plan No 3529* (2001) 54 NSWLR 60.

<sup>187</sup> (1995) 122 FLR 253; (1995) 17 ACSR 303; (1995) 13 ACLC 965.

<sup>188</sup> [2006] QSC 358; [2007] 2 Qd R 214; (2006) 62 ACSR 502; (2006) 24 ACLC 1550.

There have, therefore, been a small number of cases directly applying *Gambotto*. However, as will be seen in the following sections, the overwhelming majority of cases have distinguished or limited the application of *Gambotto*.

## **B The Meaning of “Expropriation”**

The breadth of the reach of *Gambotto* depends on the meaning of “expropriation”, as the majority in *Gambotto* drew an important distinction between expropriatory and non-expropriatory amendments. Only amendments to the constitution which involve the expropriation of a minority’s shares, or valuable proprietary rights attaching to such shares, are subject to the stringent two-pronged test. Expropriation for the purposes of the principles in *Gambotto* includes not only the compulsory acquisition of the shares of the minority but also the extinction of the rights attached to the shares of the minority.<sup>189</sup> A narrow definition of expropriation would have the effect of limiting the application of *Gambotto*.

The starting point for an examination of this question is *Heydon v NRMA Ltd*.<sup>190</sup> One of the critical questions in that case was whether the demutualisation proposal involved an expropriation, to determine whether *Gambotto* applied to the demutualisation.

The court did not come to a unanimous view. Malcolm A-JA identified three key elements of the transaction which distinguished it from expropriation as that term was used in *Gambotto*. First, an expropriation necessarily involves an attempt by a majority to appropriate the shares of a minority. This was not the case with respect to the NRMA proposal, as there was no identified group of members who sought to take control of the companies.<sup>191</sup>

Second, the proposal was expressly contemplated by NRMA’s articles and the *Corporations Law*.<sup>192</sup> Finally, each member of NRMA had the option to remain a member of the restructured group and thus continue to participate and receive benefits from their status as a member.<sup>193</sup>

Ormiston A-JA held that *Gambotto* did not apply to a proposal where all members are treated equally and are provided with a choice to take up rights or options in exchange for the extinguishment of their membership rights. McPherson A-JA differed from the other judges. In his Honour’s view, the fact that members of NRMA would receive something in return for the extinguishment of their rights did not prevent the proposal from involving an expropriation.

The majority view in *Heydon* was accepted in *Arakella Pty Ltd v Paton*, where Austin J held that *Gambotto* has no application “where the proposed amendment will replace all

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<sup>189</sup> *Young v Owners Strata Plan 3529* (2001) 54 NSWLR 60; [2001] NSWSC 1135; *Bundaberg Sugar Ltd v Isis Central Sugar Mill Co Ltd* [2006] QSC 358; [2007] 2 Qd R 214; (2006) 62 ACSR 502; (2006) 24 ACLC 1550 at [83]; *Lin v Owners of Strata Plan No 50276* [2004] ANZ ConvR 325; (2005) NSW ConvR 56-105; [2004] NSWSC 88 at [84].

<sup>190</sup> See nn 60-68 and 74-76 and accompanying text.

<sup>191</sup> *Heydon v NRMA Ltd* (2000) 51 NSWLR 1 at [177].

<sup>192</sup> *Ibid* at [179].

<sup>193</sup> *Ibid* at [180]-[181].

interests with another species of property in a manner that treats the interest-holders equally, at any rate where (as here) there is no ‘majority’ voting block”.<sup>194</sup>

In *Re Australian Co-operative Foods Ltd*, Santow J doubted the applicability of the *Gambotto* principles to a transaction which does not involve a takeover or aggrandisement, but is merely a restructure.<sup>195</sup> In *Re Arrowfield Group Ltd*, Cohen J distinguished *Gambotto*, including on the ground that there was no act of majority shareholders against a minority, and the action was not unfair.<sup>196</sup> Barrett J in *Re Australand Holdings Ltd* accepted the decisions of Malcolm A-JA and Ormiston A-JA in *Heydon v NRMA Ltd* and that of Austin J in *Arakella*, holding that there must be discrimination for *Gambotto* to apply, where a pre-existing and distinct majority uses its power to “dispense with or dispossess a minority”.<sup>197</sup>

There are further examples of courts limiting the meaning of expropriation in the context of the principles in *Gambotto*. In *Catto v Hampton Australia Ltd (in liq) (No 3)*, Bryson J said that the terms “elimination” and “expropriation” are inappropriate when sought to be applied to the concept of winding up: “where a company is wound up, the necessary result is that all shareholders are eliminated. Nothing is expropriated”.<sup>198</sup>

In *Schrapel v Coopers Brewery Ltd*,<sup>199</sup> Lion Nathan acquired South Australia Brewing Co Ltd which held shares in Coopers. Disputes over various matters arose between Lion Nathan and Coopers, which were resolved by amending the constitution of Coopers. The amendments inserted a pre-emptive rights regime which provided that if a member proposed to transfer any shares, the shares had to be offered first to existing members, secondly to the Australian Mutual Provident Society and finally to Lion Nathan. The amendments also provided that Lion Nathan was deemed not to be a competitor of Coopers for the purposes of Article 143 which restricted competitors from being members in Coopers. These provisions were entrenched in the constitution but the entrenchment ceased if Lion Nathan experienced a change in control, which subsequently occurred.

As a result of the change in control, members of Coopers holding 5% of the voting shares requisitioned a meeting to consider resolutions deleting Lion Nathan’s pre-emptive rights and its exemption from the “no competitor” provision. Finn J said “it is difficult to see that the proposed alteration is anything other than the taking of a step contemplated at the time the Lion Nathan rights were inserted in the Constitution of returning to the tight constraints on membership of the company which existed prior to Lion Nathan being given its rights”.<sup>200</sup> This did not involve “an expropriation of a shareholder in a way discountenanced by *Gambotto*”.<sup>201</sup>

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<sup>194</sup> (2004) 60 NSWLR 334; [2004] NSWSC 13 at [148].

<sup>195</sup> (2001) 186 ALR 21; (2001) 162 FLR 360; (2001) 38 ACSR 71; (2001) 19 ACLC 1120; [2001] NSWSC 382 at [76].

<sup>196</sup> (1995) 17 ACSR 649 at 653-4.

<sup>197</sup> (2005) 219 ALR 728; (2005) 54 ACSR 687; [2005] NSWSC 835 at [12]-[13].

<sup>198</sup> (2004) 89 SASR 234; [2004] SASC 242 at [49].

<sup>199</sup> [2005] FCA 1714.

<sup>200</sup> *Ibid* at [26].

<sup>201</sup> *Ibid* at [28].

## C Expropriation in Accordance with Statutory Procedures

This section sets out the courts' approach to the applicability of *Gambotto* to other corporate reorganisation mechanisms and methods of compulsory acquisition where this is done in accordance with statutory procedures under the *Corporations Act*. The consistency of the courts is striking, holding that *Gambotto* is not relevant to these methods of compulsory acquisition.

### 1 Schemes of Arrangement

In *Re NRMA Ltd (No 1)* Santow J noted that the scheme of arrangement procedure involves an evaluation of the fairness of the proposal by the court as well as members' approval, and as a result *Gambotto* is not applicable.<sup>202</sup>

Subsequent decisions have confirmed that the statutory scheme of arrangement procedure contains adequate safeguards to ensure fairness which leave no room for the *Gambotto* principles to operate.<sup>203</sup> This is the case even where expropriation is involved. In *Re GIO Australia Holdings Ltd*, in response to the question whether a scheme can validly expropriate a member's shares in light of *Gambotto*, Santow J held that "it is clear that the High Court did not intend to preclude such compulsory acquisition as is provided for under schemes of arrangement or other such statutory regimes where fairness is appraised".<sup>204</sup>

### 2 Compulsory Acquisition Following a Takeover

It was held in *Village Roadshow Broadcasting Pty Ltd v Austereo Ltd* that *Gambotto* is not applicable to the compulsory acquisition of shares following a takeover.<sup>205</sup> Similarly, in *Peninsula Gold Pty Ltd v Australian Securities Commission*, it was stated that in Chapter 6 of the corporations legislation, "the legislature has expressly addressed the balance between protecting the interests of minority shareholders ... and promoting a company's ability to compulsorily acquire shares where it is in the best interests of the company to do so".<sup>206</sup>

### 3 Compulsory Acquisition under Chapter 6A

Chapter 6 of the corporations legislation was amended in 1999 to allow the compulsory acquisition of shares independently of a takeover.<sup>207</sup> In *Arakella Pty Ltd v Paton*, Austin J stated that as the majority in *Gambotto* made clear that the *Gambotto* principles did not apply to schemes of arrangement under s 411, or a compulsory acquisition after a

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<sup>202</sup> (2000) 156 FLR 349; (2000) 33 ACSR 595; [2000] NSWSC 82 at [58]-[59].

<sup>203</sup> *Re Australian Co-operative Foods Ltd* (2001) 186 ALR 21; (2001) 162 FLR 360; (2001) 38 ACSR 71; (2001) 19 ACLC 1120; [2001] NSWSC 382 at [72]; *Re Credit Reference Association of Australia Ltd* (1998) 16 ACLC 491 at 494; *Re Archaean Gold NL* (1997) 23 ACSR 143; (1997) 15 ACLC 382.

<sup>204</sup> (1999) 33 ACSR 283; [1999] NSWSC 1276 at [13].

<sup>205</sup> (1997) 24 ACSR 185 at 190; (1997) 15 ACLC 929.

<sup>206</sup> (1996) 19 ACSR 703 at 714; (1996) 23 AAR 1; (1996) 14 ACLC 958 (AAT); affirmed in *Peninsula Gold Pty Ltd v Australian Securities Commission* (1996) 134 FLR 457; (1996) 21 ACSR 246; (1996) 14 ACLC 1435.

<sup>207</sup> See nn 262-278 and accompanying text.

takeover bid, it was clear that the *Gambotto* principles did not apply to Chapter 6A.2 which permits compulsory acquisition independently of a takeover bid.<sup>208</sup>

#### **4 Selective Capital Reductions**

Writing shortly after the High Court delivered its judgment in *Gambotto*, one commentator flagged the possibility that the removal of the requirement to obtain court approval for selective capital reductions<sup>209</sup> would result in *Gambotto* being applicable to selective reductions.<sup>210</sup> The question was answered in subsequent cases which held that the amendments introduced by the *Company Law Review Act 1998* (Cth) have ensured adequate protection for shareholders by requiring disclosure of all material information; that the capital reduction be fair and reasonable to the company's shareholders as a whole; and giving discontented shareholders the option of applying for relief pursuant to s 1324 of the *Corporations Act*. As a result, the *Gambotto* principles are left with no further work to do.<sup>211</sup>

The NSW Court of Appeal in *Winpar Holdings Ltd v Goldfields Kalgoorlie Ltd* held that the selective capital reduction procedure provides a comprehensive procedure to ensure fairness, which is comparable although not identical to the *Gambotto* principles. The provisions impose both procedural and substantive fairness requirements and as the power to reduce capital is specifically provided for by s 256B it does not represent the taking of a power by the majority. Accordingly, "superadded *Gambotto* principles would be conflicting and confusing".<sup>212</sup> A similar approach was adopted in *Re Albert Street Properties Ltd*.<sup>213</sup>

#### **5 Change of Company Type**

*Re NRMA Ltd (No 2)* held that *Gambotto* is not applicable to changes of company type as Part 2B.7 "provides an express statutory regime for expropriation" which "leaves no room for *Gambotto* principles to operate independently".<sup>214</sup>

#### **6 Liquidations**

*Catto v Hampton Australia Ltd (in liq) (No 3)*<sup>215</sup> is authority that *Gambotto* is not applicable to company liquidations, even when these are used as a de facto means of eliminating minority shareholders. *Catto* concerned the validity of a resolution authorising an in specie distribution to the majority shareholder of all of the company's assets other than some cash paid to minority shareholders. Vanstone J held that "where a company is wound up, the necessary result is that all shareholders are eliminated. Nothing is expropriated".<sup>216</sup>

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<sup>208</sup> (2004) 60 NSWLR 334; [2004] NSWSC 13 at [130]. See also *Capricorn Diamonds Investments Pty Ltd v Catto* (2002) 5 VR 61; (2002) 168 FLR 146; (2002) 41 ACSR 376; (2002) 20 ACLC 931; [2002] VSC 105 at [83].

<sup>209</sup> Introduced by the *Company Law Review Act 1998* (Cth).

<sup>210</sup> Digby, above n 63 at 72.

<sup>211</sup> *Winpar Holdings Ltd v Goldfields Kalgoorlie Ltd* (2000) 176 ALR 86; (2000) 157 FLR 59; (2000) 34 ACSR 737; (2000) 18 ACLC 665; [2000] NSWSC 728 at [5], [39].

<sup>212</sup> (2001) 166 FLR 144; (2001) 40 ACSR 221; (2001) 20 ACLC 265 at [95]-[96].

<sup>213</sup> (1997) 23 ACSR 318 at 321-2.

<sup>214</sup> (2000) 156 FLR 412; (2000) 34 ACSR 261; (2000) 18 ACLC 533; [2000] NSWSC 408 at [104].

<sup>215</sup> (2004) 89 SASR 234; [2004] SASC 242.

<sup>216</sup> *Ibid* at [49].

Section 491 of the *Corporations Act* specifically confers a right upon shareholders to move and vote in favour of a resolution to wind the company up.<sup>217</sup> Therefore, voting to wind up a company in accordance with s 491 is not analogous to an expropriation of shares by altering the constitution.<sup>218</sup> Vanstone J stated that the legislation already provided protection for shareholders against unfairness in a liquidation by imposing obligations on liquidators, and so there is no work for the *Gambotto* principles to do.<sup>219</sup>

## 7 Summary

*Gambotto* is not applicable to schemes of arrangement, compulsory acquisitions following a takeover, Chapter 6A.2 acquisitions, selective capital reductions, changes of company type and company liquidations as compulsory acquisition pursuant to these procedures is undertaken as part of a statutory procedure under the *Corporations Act* with protections afforded to those whose shares are to be acquired.

### D Applicability of *Gambotto* to Other Structures and Entities

In addition to considering whether the *Gambotto* principles apply to expropriation by means of a statutory procedure, the courts have also had to consider whether the *Gambotto* principles apply to structures and entities other than companies.

#### 1 Unit Trusts

Hely J in *Cachia v Westpac Financial Services Ltd*<sup>220</sup> stated that the *Gambotto* principles are not applicable to unit trusts. Holding that there is a fundamental difference between a unit in a unit trust and a share in a company, he said that “*Gambotto* was a case concerning company law” and so the “rights and obligations of the trustee, the manager and unitholders” are not to be determined in accordance with company law principles, but by the law of trusts.<sup>221</sup>

In *Arakella Pty Ltd v Paton*,<sup>222</sup> Austin J also considered whether the *Gambotto* principles apply to unit trusts.<sup>223</sup> His Honour appeared to prefer the view that *Gambotto* was capable of wider application given the High Court had expressly formulated the principle<sup>224</sup> in accordance with the equitable fraud on a power doctrine,<sup>225</sup> and had rejected the “company law” formulation of fraud on the minority.<sup>226</sup> However, his Honour did not express a concluded view and in any case *Gambotto* did not apply as s 81 of the *Trustee Act 1925* (NSW) (which allows the court to confer upon the trustee additional powers to deal with trust property) provided a sufficient mechanism for review of the fairness of the proposal.

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<sup>217</sup> *Ibid* at [90].

<sup>218</sup> *Ibid* at [86].

<sup>219</sup> *Ibid* at [96].

<sup>220</sup> (2000) 170 ALR 65; (2000) 33 ACSR 572; (2000) 18 ACLC 293.

<sup>221</sup> *Ibid* at [87].

<sup>222</sup> (2004) 60 NSWLR 334; [2004] NSWSC 13.

<sup>223</sup> *Ibid* at [127].

<sup>224</sup> *Gambotto v WCP Ltd* (1995) 182 CLR 432 at 444.

<sup>225</sup> *Peters' American Delicacy Co Ltd v Heath* (1939) 61 CLR 457 at 511.

<sup>226</sup> *Arakella Pty Ltd v Paton* (2004) 60 NSWLR 334; [2004] NSWSC 13 at [127], referring to *Houghton v Immer (No 155) Pty Ltd* (1997) 44 NSWLR 46 at 53.

In *Re Australand Holdings Pty Ltd*,<sup>227</sup> Barrett J held that sufficient safeguards existed in relation to a merger of a number of managed investment schemes, namely an approach to the court for judicial advice by the relevant schemes involved, which represented “a sufficient analogy with the safeguards in company law to which the majority referred in *Gambotto*”.<sup>228</sup> Accordingly, *Gambotto* did not apply.

Campbell J and Barrett J in the *Re Abacus Funds Management Ltd*<sup>229</sup> decisions also questioned whether the *Gambotto* principles applied to unit trusts, but their Honours did not finally decide that question as there was no discrimination between members and sufficient safeguards existed. Therefore, the *Gambotto* principles did not apply.

Accordingly, although the question has not been conclusively decided, the courts have exhibited a reluctance to apply *Gambotto* to trust structures. This is significant given the growth of the managed funds industry as a vehicle for investment, as many managed investment schemes are structured as unit trusts.<sup>230</sup>

## **2 Other Types of Bodies Corporate**

*Gambotto* involved a company limited by shares. In *Heydon v NRMA Ltd*,<sup>231</sup> the NSW Court of Appeal considered the application of the *Gambotto* principles in the context of a company limited by guarantee. In *Houghton v Immer (No 155) Pty Ltd*,<sup>232</sup> it was held that the *Gambotto* principles apply to strata title bodies corporate, preventing resolutions and actions which are for the personal gain of one member at the expense of another. A special resolution of the body corporate transferring its interest in the common property to one proprietor was held to be a fraud on the minority and voidable in equity. A similar conclusion was reached by Santow J in *Young v Owners S/P 3529*.<sup>233</sup> However, in another case,<sup>234</sup> Simmonds J held that this did not extend to someone who had contracted to purchase a lot in a strata title plan but had not yet taken conveyance of that interest and so was not yet a member.<sup>235</sup>

In *Farrell v Royal King's Park Tennis Club (Inc)*,<sup>236</sup> the plaintiff submitted, relying in part on *Gambotto*, that protection from oppressive conduct was a fundamental principle of the law relating to corporations and should be implied into a contract between a body corporate (in this case, an incorporated association) and its members. Johnson J held that the *Gambotto* principles were not applicable to an incorporated association as *Gambotto*

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<sup>227</sup> (2005) 219 ALR 728; (2005) 54 ACSR 687; [2005] NSWSC 835.

<sup>228</sup> *Ibid* at [15].

<sup>229</sup> *Re Abacus Funds Management Ltd* (2006) 56 ACSR 693; (2006) 24 ACLC 319; [2006] NSWSC 80 (Barrett J) and *Re Abacus Funds Management Ltd* (2006) 24 ACLC 211; [2005] NSWSC 1309 (Campbell J).

<sup>230</sup> See generally Pamela F Hanrahan, *Funds Management in Australia: Officers' Duties and Liabilities* (LexisNexis, 2007) at [1.36], Pamela F Hanrahan, *Managed Investments Law and Practice* (Looseleaf, CCH) at [1-100], [1-200]; Grant Moodie and Ian Ramsay, *Managed Investment Schemes: An Industry Report* (Centre for Corporate Law and Securities Regulation, University of Melbourne, 2003).

<sup>231</sup> (2000) 51 NSWLR 1 at [381].

<sup>232</sup> (1997) 44 NSWLR 46.

<sup>233</sup> (2001) 54 NSWLR 60; (2001) 10 BPR 19,153; [2001] NSWSC 1135.

<sup>234</sup> *Radford v Owners of Miami Apartments, Kings Park Strata Plan 45236* [2007] WASC 250.

<sup>235</sup> *Ibid* at [155].

<sup>236</sup> [2006] WASC 51.

was a case under s 260 of the *Corporations Law* (the oppression remedy).<sup>237</sup> This latter assertion is in fact incorrect, as *Gambotto* was decided under the equitable doctrine of fraud on a power.

In *Shaw v Minister for Families, Housing, Community Services and Indigenous Affairs*,<sup>238</sup> the court considered the application of the principles in *Gambotto* to housing associations incorporated under either the *Associations Act* (NT) or the *Corporations (Aboriginal and Torres Strait Islander) Act 2006* (Cth). The court distinguished *Gambotto*.<sup>239</sup>

### **3 Joint Venture Agreement**

The applicability of *Gambotto* to the passing of resolutions pursuant to a joint venture agreement was considered in *Club of the Clubs Pty Ltd v King Network Group Pty Ltd*.<sup>240</sup> In that case several companies had entered into a joint venture agreement which stated that decisions in relation to certain matters had to be made by participants holding 75% of the total interests in the joint venture. An amendment to the agreement allowed for the expropriation of the interests of shareholders in the joint venture company in certain circumstances.

Bergin J at first instance held that *Gambotto* was not relevant to an assessment of the validity of resolutions passed pursuant to a power conferred by a joint venture agreement, although the doctrine of fraud on a power was relevant.<sup>241</sup> On appeal, the majority (Campbell JA and Young CJ in Eq) held that the principles in *Gambotto* did not apply to the amendment of the joint venture agreement.<sup>242</sup> The majority focused upon the fact that *Gambotto* was concerned with the amendment of a company's constitution. Hodgson JA, in dissent on this point, held that the principles in *Gambotto* did apply to the amendment of the joint venture agreement.

### **4 Summary**

Although *Gambotto* involved a company limited by shares, the principles in that case have been held to apply to companies limited by guarantee and strata title bodies corporate. Generally, however, the courts have restricted *Gambotto* to its facts and declined to give it broader application.

## **VI LEGISLATIVE RESPONSES TO GAMBOTTO**

Soon after *Gambotto* was decided, a number of governmental bodies and committees began considering responses to *Gambotto*,<sup>243</sup> with the federal government ultimately deciding to limit its effect.<sup>244</sup> This section reviews the legislative responses to *Gambotto*.

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<sup>237</sup> Ibid at [93].

<sup>238</sup> [2009] FCA 1397.

<sup>239</sup> See n 185 for further discussion of this judgment.

<sup>240</sup> [2006] NSWSC 1138.

<sup>241</sup> Ibid at [223], [231], referring to Hely J's discussion in *Cachia v Westpac Financial Services Ltd* (2000) 170 ALR 65; (2000) 33 ACSR 572; (2000) 18 ACLC 293 of the applicability of *Gambotto* to unit trusts.

<sup>242</sup> *King Network Group Pty Ltd v Club of the Clubs Pty Ltd* (2008) 69 ACSR 172 at 179.

<sup>243</sup> Chris Merritt, "Gambotto: A Roar Deal for Corporate Mice", *Australian Financial Review*, 9 March 1995, 1 at 12; "AMP Plans Should be in the Open", *The Australian*, 3 July 1997, 12.

<sup>244</sup> "Tighter Takeover Law", *Independent Business Weekly*, 2 February 1996.



## A CASAC Review of Compulsory Acquisitions

In March 1994 the Legal Committee of the Companies and Securities Advisory Committee initiated its review of compulsory acquisitions,<sup>245</sup> and the final report was published in January 1996 following the High Court's decision in *Gambotto*.<sup>246</sup> The report made numerous recommendations for reform of the compulsory acquisition and buy-out procedures contained in the *Corporations Law*.

The CASAC Report noted concerns that *Gambotto* may have more general application and have potentially adverse implications for the compulsory acquisition powers contained in the *Corporations Law*, in particular ss 414 and 701.<sup>247</sup> In response, the Committee recommended that *Gambotto* be confined to expropriations effected by amendments to the company constitution.<sup>248</sup>

The Committee also noted that the decision in *Gambotto* imposed substantial proper purpose, procedural and substantive fairness requirements on expropriations achieved by amendments to the constitution and considered whether these tests should be amended.<sup>249</sup> Significantly, the Committee did not propose that the *Gambotto* tests be added to or replaced insofar as they apply to expropriations effected by alteration of a company's constitution.<sup>250</sup> The Committee did not elaborate on its reasons for this recommendation.

The CASAC Report made various recommendations for amendments to the existing compulsory acquisition procedures. The Committee also recommended the introduction of a new compulsory acquisition power,<sup>251</sup> subsequently to be enacted in substantially the same form as Part 6A.2 of the *Corporations Act*.<sup>252</sup>

The new procedure was recommended to enable controlling entities to achieve full ownership, ensure fair and equal treatment of minorities, and reduce greenmailing opportunities.<sup>253</sup> The new procedure undoubtedly was influenced by *Gambotto*. In particular, the Committee recommended that the *Gambotto* principles not apply to the new procedure and there be no proper purpose requirement.<sup>254</sup> This mechanism was designed to address directly *Gambotto*.

## B The New Compulsory Acquisition Procedure: Part 6A.2

### 1 The Introduction of Part 6A.2

The CLERP Reform Paper No 4 on Takeovers adopted the recommendation of the CASAC Report, proposing the introduction of a new compulsory acquisition power to

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<sup>245</sup> Legal Committee of the Companies and Securities Advisory Committee, *Compulsory Acquisitions Issues Paper* (March 1994).

<sup>246</sup> Legal Committee of the Companies and Securities Advisory Committee, *Compulsory Acquisitions Report* (January 1996) ("CASAC Report").

<sup>247</sup> *Ibid* at 8.

<sup>248</sup> *Ibid*, Recommendation 1.

<sup>249</sup> *Ibid* at 8.

<sup>250</sup> *Ibid* at 61.

<sup>251</sup> *Ibid* at 76-7.

<sup>252</sup> By the *Corporate Law Economic Reform Program Act 1999* (Cth).

<sup>253</sup> CASAC Report at 75.

<sup>254</sup> *Ibid* at 80.

facilitate the acquisition of the outstanding securities in a class by a person who holds 90% of the securities in that class.<sup>255</sup> The CLERP Paper proposed a compulsory acquisition procedure in similar terms to those proposed by CASAC.<sup>256</sup>

When the CLERP Bill was introduced into the Commonwealth Parliament, the compulsory acquisition procedure generated controversy,<sup>257</sup> being “probably the most contentious issue in the Bill”,<sup>258</sup> and with one member of the Opposition stating that the procedure was introduced to “placate vested interests”.<sup>259</sup> Sections 677C(2) and 667AA (requiring the independent expert to be appointed by ASIC), both seeking to increase the safeguards attaching to the acquisition process, were introduced at the request of the Australian Democrats to facilitate the Bill’s passage through the Senate.<sup>260</sup>

While the Bill was under consideration a number of questions were referred to CASAC, which recommended among other things that no proper purpose requirement be introduced as this could give rise to protracted litigation given the decision in *Gambotto*.<sup>261</sup> Part 6A.2 was subsequently introduced into the *Corporations Act* by the *Corporate Law Economic Reform Program Act 1999* (Cth) (CLERP Act).<sup>262</sup>

## **2 Summary of the Operation of Part 6A.2**

Part 6A.2 gives a person who has full beneficial interests in at least 90% of the securities in a class the power to acquire the remaining securities in that class within 6 months after that person becomes a 90% holder.<sup>263</sup> The 90% holder must pay cash consideration for the securities and pay the same amount for each security acquired.<sup>264</sup> The process is initiated by the 90% holder sending a compulsory acquisition notice to the holders of the remaining securities setting out the terms of the acquisition and other required information.<sup>265</sup>

An independent expert’s report must accompany the notice, obtained from an expert nominated by ASIC and stating the expert’s opinion as to whether the terms of the acquisition give fair value for the securities together with the reasons for forming that

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<sup>255</sup> Corporate Law Economic Reform Program Proposals for Reform Paper No 4: *Takeovers* (1997) (“CLERP Paper”).

<sup>256</sup> CASAC Report at 29-30.

<sup>257</sup> *Re Goodyear Australia Ltd; Kelly-Springfield Australia Pty Ltd v Green* (2002) 167 FLR 1; (2002) 20 ACLC 983 at [66].

<sup>258</sup> Parliament of Australia, *Parliamentary Debates*, Senate, 12 October 1999, 9480 (Senator Murray).

<sup>259</sup> Parliament of Australia, *Parliamentary Debates*, Senate, 14 October 1999, 9706 (Senator Conroy).

<sup>260</sup> Parliament of Australia, *Parliamentary Debates*, Senate, 12 October 1999, 9473 (Senator Conroy), 9481 (Senator Murray); 14 October 1999, 9704 (Senator Murray).

<sup>261</sup> Companies and Securities Advisory Committee, *Compulsory Acquisitions and Buy-outs* (March 1999); Companies and Securities Advisory Committee, *Report to the Minister for Financial Services and Regulation on Compulsory Acquisitions* (March 2000).

<sup>262</sup> For a more detailed summary of the amendments see H A J Ford, R P Austin and I M Ramsay, *An Introduction to the CLERP Act 1999* (Butterworths, 2000), Ch 6; Robert Baxt, et al, “CLERP” Explained (CCH, 2000) at [3-410] – [3-530].

<sup>263</sup> Sections 664A, 664AA.

<sup>264</sup> Section 664B.

<sup>265</sup> Section 664C.

view.<sup>266</sup> The method for determining “fair value” for the purposes of Chapter 6A is contained in s 667C.

If securityholders holding at least 10% of the securities covered by the compulsory acquisition notice object to the acquisition, the 90% holder has the option to discontinue the acquisition or apply to the court for approval of the acquisition.<sup>267</sup> The only ground upon which approval may be withheld is an unfair price, for s 664F provides that if the 90% holder establishes to the court that the price is a fair price, the court must approve the acquisition.

### **3 The Purpose of Part 6A.2**

Part 6A.2 was seen by some as an effective reversal of *Gambotto*.<sup>268</sup> However, it is more accurate to view Part 6A.2 as both providing for a new means of compulsory acquisition and limiting any broader application of *Gambotto*. The CLERP Paper stated that Part 6A.2 was introduced:

to ensure, in the interests of economic efficiency, that a person who acquires overwhelming ownership of a class of securities is able to achieve 100 per cent control of that class. This power would also help companies overcome any limitations on acquisitions flowing from the *Gambotto* decision.<sup>269</sup>

The legislative history reveals that it was the primary intention of the new provisions to discourage greenmailing.<sup>270</sup> The CLERP Explanatory Memorandum stated that one of the key reasons for introducing the compulsory acquisition power was to “discourage minority shareholders from demanding a price for their securities that is above a fair value (often referred to as ‘greenmailing’)”.<sup>271</sup>

However, it cannot be said that the introduction of Part 6A.2 was exclusively motivated by *Gambotto*, as the CASAC review of compulsory acquisitions was initiated prior to the High Court’s decision in *Gambotto*, noting defects with the takeover provisions and canvassing reform options.<sup>272</sup> Indeed, its first proposal for a compulsory acquisition power was put forward in November 1994, prior to the decision in *Gambotto*.<sup>273</sup>

Chapter 6A largely removed the impediments for entities seeking full ownership created by former s 701 of the *Corporations Law*, adopting “the utilitarian approach of facilitating the economic desires of the majority”, subject to full disclosure to the

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<sup>266</sup> Sections 667A, 667AA.

<sup>267</sup> Section 664E.

<sup>268</sup> Michael J Duffy, “Shareholder Democracy or Shareholder Plutocracy? Corporate Governance and the Plight of Small Shareholders” (2002) 25 *University of New South Wales Law Journal* 434 at 450; Vanessa Mitchell, “Has the Tyranny of the Majority Become Further Entrenched?” (2002) 20 *Company and Securities Law Journal* 74 at 75; Jolyon Rogers, “Compulsory Acquisition Under Pt 6A.2 and its Implications for Minority Shareholders” (2003) 31 *Australian Business Law Review* 97 at 103.

<sup>269</sup> CLERP Paper, above n 255 at 29.

<sup>270</sup> *Capricorn Diamonds Investments Pty Ltd v Catto* (2002) 5 VR 61; (2002) 168 FLR 146; (2002) 41 ACSR 376; (2002) 20 ACLC 931 at [21]; *Pauls Ltd v Dwyer* (2001) 19 ACLC 856 at [12], [22]; *Australian Securities and Investments Commission v Yandal Gold Pty Ltd* [2003] FCA 77 at [33].

<sup>271</sup> Corporate Law Economic Reform Program Bill, Explanatory Memorandum at [7.31].

<sup>272</sup> CASAC Issues Paper, above n 245.

<sup>273</sup> CASAC Report, above n 246 at 75.

minority holders and to the payment of compensation that has been independently assessed to be fair.<sup>274</sup>

Evaluation of Part 6A.2 has been mixed. Cilliers saw the introduction of Part 6A.2 as an important step “towards restoring the balance between the interests of the majority and those of the minority after *Gambotto*”.<sup>275</sup> Others have seen Part 6A.2 as significantly eroding minority shareholders’ rights,<sup>276</sup> unduly privileging the majority and containing the potential to operate oppressively, with little scope for review.<sup>277</sup> In particular, the requirement to obtain an expert’s report – the primary protection mechanism for the minority – has been seen by some commentators as a weak protection.<sup>278</sup>

### **C The Demutualisation of AMP and Legislation Limiting the Application of *Gambotto***

Subsequent to *Gambotto* and taking place at a similar time to the demutualisation of NRMA, the Australian Mutual Provident Society (AMP) also initiated demutualisation plans, leading ultimately to the demutualised entity listing on the Australian Securities Exchange in June 1998 as AMP Limited. As it was established under a New South Wales statute in 1857, the NSW Parliament considered it was necessary to introduce further legislation enabling the restructure to take place.<sup>279</sup>

The *Australian Mutual Provident Society (Demutualisation and Reconstruction) Act 1997* (NSW) (AMP Act) was consequently enacted, providing that AMP could convert to a company limited by shares provided that members had approved the proposal,<sup>280</sup> as a result of which members would become shareholders in AMP’s holding company.<sup>281</sup> The proposal involved the extinguishment of the rights of AMP’s members, particularly those who did not support the proposal,<sup>282</sup> and thus the spectre of *Gambotto* was raised as a potential threat to the demutualisation.<sup>283</sup>

The Explanatory Note to the AMP Bill stated that “[e]xpropriation occurs by virtue of legislation and a statutory procedure, rather than simply by virtue of the action of members in changing AMP’s constitution” and as a consequence *Gambotto* was not applicable.<sup>284</sup> Although the Explanatory Note stated that the AMP Bill did not remove members’ rights to bring oppression proceedings, any potential challenge to the demutualisation was removed by s 13(3), which stated that once the shareholding had

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<sup>274</sup> Colla, above n 158 at 20, 25.

<sup>275</sup> Cilliers, above n 35 at 60.

<sup>276</sup> Mitchell, above n 268.

<sup>277</sup> Elizabeth Boros, “Compulsory Acquisition of Minority Shareholdings: The Way Forward?” (1998) 16 *Company and Securities Law Journal* 279 at 291, 298.

<sup>278</sup> Hughes, above n 39 at 207; Mitchell, above n 268 at 76; Boros, above n 277 at 291.

<sup>279</sup> “Are AMP’s Barricades Designed to Keep Predators Out or Directors in?”, *National Business Review*, 22 August 1997.

<sup>280</sup> See Part 2, in particular ss 4, 6-9 of the Act.

<sup>281</sup> Section 13.

<sup>282</sup> Explanatory Note, *Australian Mutual Provident Society (Demutualisation and Reconstruction) Bill 1997* (NSW) at [9].

<sup>283</sup> “AMP Plans Should be in the Open”, *The Australian*, 3 July 1997, 12.

<sup>284</sup> Explanatory Note, *Australian Mutual Provident Society (Demutualisation and Reconstruction) Bill 1997* (NSW) at [9].

been restructured, no court or tribunal could make an order reversing the issue of the shares. The legislation therefore was introduced and drafted in a manner that prevented the application of the *Gambotto* principles.

#### **D Company Law Review Act**

The selective reduction of capital provisions were substantially amended by the *Company Law Review Act 1998* (Cth) which inserted Part 2J.1 into the *Corporations Law*. Reductions of capital continue to require shareholder approval,<sup>285</sup> but there is no longer a requirement that the reduction be authorised by the company's constitution, and court approval is no longer required. All material information relevant to the proposal must be disclosed to the shareholders.<sup>286</sup>

Importantly, the Explanatory Memorandum expressly stated that the *Gambotto* principles will not apply: "the principles set out in *Gambotto* ... do not apply to the expropriation of rights under this mechanism".<sup>287</sup>

#### **E Evaluation**

The legislative responses to *Gambotto* all evidence the same desire to confine *Gambotto* to its particular facts and not allow it to have a broader operation. The CASAC Report recommended that it be confined to its facts and Part 6A.2 was introduced partially to avoid potential problems with respect to compulsory acquisitions flowing from *Gambotto*.

### **VII CONCLUSION**

As we have seen, the decision of the High Court in *Gambotto* proved to be very controversial. Some saw the decision as radically altering the balance of power in corporate law by granting minority shareholders extensive new powers to prevent the compulsory acquisition of their shares and thereby impeding commercial transactions that would benefit companies. There was also concern that the principles developed by the High Court for compulsory acquisition of shares undertaken by way of amendment of the corporate constitution would apply to other forms of compulsory acquisition, and corporate law more generally, again impeding many types of corporate transactions.

The High Court decision had the potential to have a significant influence on Australian corporate law and the way corporate transactions involving compulsory share acquisitions are conducted. In particular, *Gambotto* was considered in more than 50 subsequent judgments giving many judges the opportunity to extend the *Gambotto* principles into new areas. These subsequent judgments considered whether the principles in *Gambotto* should extend to compulsory share acquisitions undertaken as part of a scheme of arrangement, selective capital reduction, Chapter 6A acquisition or change of company type. Courts also considered whether the principles in *Gambotto* should extend to structures other than companies such as unit trusts. Almost uniformly, courts decided that the principles should not be extended. Parliament responded by enacting new

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<sup>285</sup> The requirements are set out in s 256C of the *Corporations Act*.

<sup>286</sup> Section 256C(4).

<sup>287</sup> Explanatory Memorandum, *Company Law Review Bill 1997* (Cth) at [368].

provisions in the corporations legislation facilitating the compulsory acquisition of shares.

For a short time the High Court decision did have a major impact. The decision led to the restructuring of one of the most significant corporate transactions underway at the time the High Court handed down its judgment – the demutualisation of NRMA. The decision was also influential in terms of the debate and the responses it generated. Ultimately, however, the impact of the decision has been restricted by courts and Parliament with the result that the decision has largely been confined to the factual situation that was before the High Court in *Gambotto*.

There are many unusual aspects of *Gambotto*. First, it is unusual for a High Court decision to raise so directly key issues going to the balance of power between majority and minority shareholders, including the rights attached to shares and the circumstances when these rights can be removed against the will of the holder of the shares. Second, it is unusual for a corporate law decision to receive such widespread discussion – both in the media and in the academic literature although this can be explained by the importance of the issues raised in the decision. Third, it is unusual for Parliaments, both at the Commonwealth and the State level, to legislate to restrict the application of a High Court decision – as occurred with *Gambotto*. Fourth, it is unusual for a High Court corporate law decision to be considered in so many subsequent judgments.

Our research indicates that the responses to *Gambotto* were largely negative. Initial commentary in the media and subsequent academic commentary was mostly critical with concerns expressed about the potential for the decision to impede commercial transactions of benefit to companies. These concerns also underpinned the response of Parliament. It is likely that the overwhelming reluctance of courts to extend the principles in *Gambotto* is explained at least in part by courts also sharing these concerns although in many of the subsequent decisions courts were able to point to statutory protections available to minority shareholders as a reason for not applying the principles in *Gambotto* to a range of commercial transactions involving the compulsory acquisition of shares. In summary, few of those who discussed and considered the decision in *Gambotto* liked it and through a variety of responses, a High Court decision that had the potential to have major implications for corporate law and commercial transactions has been so restricted by courts and Parliament that its influence is now very limited.

Finally, when we analyse *Gambotto* by placing it in the broader political context of the role of the High Court at the time of the decision, we see that *Gambotto* was decided when the High Court was in a period of unprecedented judicial activism. The court had undergone a significant transformation and saw itself as an agent for change, being less constrained by legal precedent, and delivering judgments that emphasised fairness and individual justice rather than certainty. Subsequently the High Court retreated from this judicial activism and our research documents similarities in how other courts restricted the application of *Gambotto*.