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Abstract

Shareholder agreements reflect a reassertion of contractualism in corporate law at a time when statutory regulation is more extensive than ever. Though not displacing the s140 statutory contract between members, shareholder agreements have a role to play both in direct contract between parties but also in setting reasonable expectations that may play a role in oppression actions or winding up on the just and equitable basis. As contracts they are prima facie enforceable but also subject to statutory overlays in the form of the laws of misleading and deceptive conduct and unconscionable conduct. Finally they are subject to some limitation in that the common law suggests that a company cannot in a shareholder agreement deprive itself of its power to alter its own constitution. There is also some doubt about the extent to which directors' duties can be attenuated by shareholder agreement and whether shareholder disputes can be made the subject exclusively of commercial arbitration and kept out of the courts.

SHAREHOLDERS AGREEMENTS AND SHAREHOLDERS' REMEDIES

CONTRACT VERSUS STATUTE?

MICHAEL J DUFFY*

Precis

Shareholder agreements reflect a reassertion of contractualism in corporate law at a time when statutory regulation is more extensive than ever. Though not displacing the s140 statutory contract between members, shareholder agreements have a role to play both in direct contract between parties but also in setting reasonable expectations that may play a role in oppression actions or winding up on the just and equitable basis. As contracts they are prima facie enforceable but also subject to statutory overlays in the form of the laws of misleading and deceptive conduct and unconscionable conduct. Finally they are subject to some limitation in that the common law suggests that a company cannot in a shareholder agreement deprive itself of its power to alter its own constitution. There is also some doubt about the extent to which directors' duties can be attenuated by shareholder agreement and whether shareholder disputes can be made the subject exclusively of commercial arbitration and kept out of the courts.

Introduction

Corporations are a mix of contractual, legislative, property law and other strands that make them susceptible to endless analysis by legal theorists. It can be argued that the origins of corporations lie equally in contract (the nexus of contracts view) and in statute.¹ It might be observed that the legislature originally provided the corporate shell but that contract law did much to fill out the contents of that shell in terms of the relations between the various stakeholders contained therein.

The rise of the shareholder agreement might be seen in a sense as a reassertion of contractualism in corporate law, however its scope remains limited given the amount

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¹ For an analysis of the concepts and history see generally John Farrer, *Corporate Governance Theories, Principles and Practice*, Third edition, at 9.

of ground that has now been given over to statutory regulation of the company. Whether it can displace the 'statutory contract' between members created by s140 in any real sense is a matter of some doubt given the weight and power of statute's hold on corporate law. On the other hand, the increasing popularity of shareholder agreements must be testament to their utility.

This paper deals with a subset of that issue in relation to remedies. Does the existence of a shareholders agreement change the ordinary position for statutory or other shareholder remedies? Whilst it certainly changes the position in relation to contractual remedies it is submitted that it may not cause substantial change for the company law remedies (such as oppression).

This paper proceeds to some degree from the litigator's perspective which may, on the one hand, be desirous of obtaining specific performance and on the other may seek to argue invalidity of the shareholders agreement on various grounds. The paper is therefore somewhat varied in focus and does not seek to argue a specific case.

In a general sense it is argued that shareholders agreements are unlikely to make illegitimate or inequitable conduct legitimate or equitable.² On the other, hand the agreements may have a role in establishing what the 'legitimate expectations' of shareholders are in a particular company and so bear upon the issue of whether such 'legitimate expectations' are being met or are being thwarted. Where the latter is the case it seems likely that the traditional shareholder remedies will be available (whether in the ordinary courts or in the context of a commercial arbitration of the matter which may take place pursuant to the terms of the shareholder agreement).

Shareholders agreements generally

Shareholder remedies in the context of shareholder agreements present a novel slant on the issue of shareholder remedies generally. The traditional remedies have evolved at common law and been substantially codified and modified in statute. The right to a remedy is of course not strictly dependent on contract even though contractual relationships are inherent in the corporate entity. The remedies

² It has been argued that a 'straightforward contractual action based on a shareholder agreement' is unlikely to be 'subjected to the equitable considerations appropriate to winding up and oppression remedies.' See L.S. Sealy. The Enforcement of Partnership Agreements, Articles of Association and Shareholder Agreements. Chapter 4 of *Equity and Commercial Relationships* (Finn. P.D (editor) 1987 p108. I will resist the temptation to try and define 'illegitimate' or inequitable conduct (which will depend upon the facts of individual cases) other than to observe that the courts usually know it when they see it.

themselves reflect the mixing of strands of both legislative force and contractual agreement that are inherent in corporate personality as well as equitable considerations. The particular remedies are discussed in more detail below.

The statutory contract

Companies operated historically with a memorandum and articles as well as later legislative inclusions such as Table A internal governance rules. Table A has since 1998 been replaced by the replaceable rules and company constitution (if any). Section 140 provides that:

1) A company's constitution (if any) and any replaceable rules that apply to the company have effect as a contract:

(a) between the company and each member; and

(b) between the company and each director and company secretary;
and

(c) between a member and each other member;

under which each person agrees to observe and perform the constitution and rules so far as they apply to that person.

Thus, at the outset, there is a 'shareholder agreement' between shareholders in relation to the matters contained in the constitution and replaceable rules. The replaceable rules are in fact particular provisions of the Act³ which have statutory force but which can be displaced or modified by the company's constitution. In a sense the displacement or modification is a form of contractual variation but buttressed by legislative force.⁴ In general shareholders can sue in contract for a breach by the company or by the other shareholders of the statutory contract (though there are limitations to this where they make claims that are not in their capacity as shareholders but in their capacity as employees or others - see *Eley v Positive Government Security Life Assurance Co*⁵).

³ There are forty two sections dealing with various matters classified under the various topics of Officers and Employees, Inspection of Books, Directors Meetings, Members Meetings, Shares and Transfer of Shares.

⁴ Though in one sense the operation of the democratic process through majority and special majority voting militates against perfect direct contracting between members in the corporation (though the agreement to be bound by such voting is obviously a form of direct contractual consent).

⁵ (1875) 1 Ex D 20. In which the claim was in the shareholder's capacity of 'life solicitor' for the company.

It would seem to follow that shareholder agreements must, to the extent that they wish to exclude or modify the replaceable rules, also be supported by a company constitution that specifically excludes or modifies the replaceable rules.

What can be done in a shareholders agreement?

Shareholder agreements can seek to do various things but some of the most common are to

- Maintain the status quo (or balance of power) between founding directors.
- Maintain a particular structure for the company (including recognition of special member categories or rights of key persons).
- Deal with succession issues.
- Provide for compulsory acquisition of shares in certain situations.
- Attempt to state priorities, values and policies.
- Attempt to clarify managements role vis a vis shareholders.
- To confer rights on shareholders which would not be enforceable if contained in the constitution (eg personal rights conferred on a shareholder other than as a member such as rights under a contract of service).⁶
- To regulate relationships between shareholders that may be unconnected with the general administration of the company.
- Set up 'joint venture' arrangements.
- Contain buy-out options and guidelines.
- Contain veto rights.
- Contain pre-emptive rights to be offered new shares.⁷
- Deal with deadlocks.
- Deal with valuation issues and procedures.
- Provide for private arbitration of disputes.
- Protect minority rights.
- Preserve confidentiality.

⁶ Noting that *Eley's Case* (ibid) suggests these are otherwise not enforceable.

⁷ Though this is already a replaceable rule for proprietary companies. See s254D *Corporations Act 2001* (Cth).

It has been argued that at each level of authority in a corporation the principle of majority rule prevails and that 'the primary purpose of a shareholders agreement is to eliminate the tyranny of the majority.'⁸

Similarly the US Courts have long accepted shareholder agreements as allowing a small group of investors to 'adopt the decision making procedures of a partnership, avoid the consequences of majority rule (the standard operating procedure for corporations) and still enjoy the tax advantages and limited liability of a corporation.'⁹

The controversy tends to arise where shareholders attempt to place fetters on a company's normal statutory powers including, importantly, its power to alter its own constitution and its power to alter share capital – particularly through the issue of new shares. Conversely, problems may arise where a shareholders agreement goes beyond normal rights and procedures and seeks to validate conduct which might otherwise infringe the norms of company law – such as the alteration of a constitution to expropriate existing shares.¹⁰

There are different views on shareholder agreements ranging from a highly critical ¹¹ view to a supportive 'liberty of contract' view. The debate has been played out to some degree in England though not so much in Australia.

The libertarian view has developed following the decision in *Russell v Northern Bank Development Corporation Ltd*¹² where the House of Lords found that though a company cannot deprive itself of its power to alter its constitution, the members of the company could agree in a shareholders' agreement as to how they will exercise their voting rights on a resolution to alter the articles/constitution. The *Northern Bank* case involved a shareholders agreement that was to take priority as between the shareholders over the articles of association and provided that no further share capital would be issued without the unanimous written consent of all parties to the agreement. Russell took action objecting to resolutions being passed to increase the

⁸ A Elson, 'Shareholders Agreements: A Shield for Minority Shareholders of Close Corporations' (1967) 22 *Business Lawyer* 449.

⁹ *Blount v Taft* 246 S.E.2d 763 at 769 (1978) (per Chief Justice Sharp of the Supreme Court of North Carolina).

¹⁰ This may infringe the principles established in *Gambotto v WCP Ltd* (1995) 13 ACLC 342.

¹¹ For a critical stance see K Schmitthoff, 'House of Lords Sanctions Evasion of Companies Act' (1970) 1 *Journal of Business Law* 1. The critical view is arguably a more old fashioned stance which has been given an airing mostly in the UK whereas the modern trend seems to be supportive.

¹² [1992] 1 WLR 588.

share capital in contravention of the agreement. The House of Lords found the agreement enforceable (so long as it did not purport to bind future shareholders) as between shareholders though not enforceable on the company itself. The limitation was thus that the company itself cannot be a party to that agreement.

The basis of this view is merely an extrapolation of the common sense position that shareholders can make contracts between themselves on any other matters so why should they be prevented from making this type of agreement.

Obviously shareholders cannot make an illegal contract as this will by definition be void so that shareholders therefore could not make an agreement permitting directors to breach their duties to the company (though some directors duties may be allowed to be 'attenuated' by a shareholders agreement in some cases – this is discussed below in the context of the statutory derivative action). Whether other particular matters are illegal may of course be more complicated to determine. It has been suggested that this may go further and that a shareholders' agreement also cannot fetter directors' discretion (for example by an undertaking that the director will act in the interests of a particular faction of members, or of a creditor whom he has been appointed to represent).¹³

As to the question of whether the company should properly be a party following the *Northern Bank* decision, Ferran in the UK has commented that though the decision does not mean that companies must now not be party to such agreements 'considerable caution is required if they are: any covenants whereby a company promises not to exercise a statutory power will be invalid as against the company and, unless severance is possible, as against the other parties; if severance is not possible the whole agreement may be at risk.'¹⁴

Steering the way between contractual libertarianism and judicial intervention American courts have observed:

since consensual arrangements among shareholders are *agreements* – the products of negotiation- they should be construed and enforced like any other contract so as to give intent to the effect of the parties as expressed in their agreements, unless they violate the express charter or statutory provision, contemplate an illegal object, involve ... fraud, oppression or wrong against

¹³ Sealy above n 2 p109. Referring to the authority of *Clark v Workman* [1920] 1 I.R. 107.

¹⁴ Eilis Ferran, 'The decision of the House of Lords in *Russell v Northern Bank Development Corporation Limited*' 53 *Cambridge Law Journal* 344 1994.

other stockholders, or are made in consideration of a private benefit to the promisor.¹⁵

In Australia there are numerous cases and proceedings involving disputes under shareholder agreements¹⁶ but the *Northern Bank* Case has been referred to relatively little and with no real analysis.¹⁷ There is also a lack of cases where shareholder agreements are attacked per se.

However, Austin and Ramsay note the relevance of the *Northern Bank* case to Australian law, and they make the point that though a company cannot promise not to alter its own constitution the members may make an effective contract among themselves outside the constitution as to how they shall exercise their voting rights.¹⁸ Austin and Ramsay recognize that such agreements can be common in proprietary companies regulating the relationship of shareholders in relation to management and control. They state that the shareholder agreement suffers from the fact that is not binding on new share transferees or on any non assenting members.¹⁹

At a theoretical level it has been suggested by economics scholars that because investments are made in a situation of dynamic moral hazard and uncertainty, shareholder agreements can assist in that they allow for efficiency in ex ante (prior) investments in the firm.²⁰ It is said that they do this by constraining continual renegotiation which might otherwise cause alteration of the parties 'pay-off'.²¹ On the other hand if disputation commences and the courts become involved it has also been suggested that part of the solution lies in courts forcing parties to resolve problems

¹⁵ Per Chief Justice Sharp of the Supreme Court of North Carolina. See *Blount v Taft* 246 SE 2d 763 (1978) at 771. Quoted in V R Goldwasser, 'Shareholder Agreements – Potent Protection for Minorities in Closely Held Corporations (1994), 22 *Australian Business Law Review* at 276.

¹⁶ Some recent unreported decisions include *Toll (FHL) Pty Ltd v PrixCar Services Pty Ltd & Ors* [2007] VSC 187 (9 April 2008); *Kawasaki (Australia) Pty Ltd (ACN 000 748 621) v ARC Strang Pty Ltd (ACN 062 605 850)* [2008] FCA 461 (9 April 2008) and *Allmere Pty Ltd v Burbank Trading Pty Ltd* [2008] VSC 139 (2 May 2008) .

¹⁷ See *Medical Research and Compensation Foundation v Amaca Pty Ltd* [2004] NSWSC 1227 and see *Dick v Convergent Telecommunications* [2000] NSWSC 331.

¹⁸ R P Austin and I M Ramsay, *Ford's Principles of Corporations Law* 13th Edition Butterworths Australia 2007 para 6.330.

¹⁹ *Ibid.*

²⁰ G Chemla, A Ljungqvist and M A Habib, 'An Analysis of Shareholder Agreements' March 2007, Vol 5 No 1, *Journal of the European Economic Association*. P 93 at 93.

²¹ *Ibid* p116.

through 'private ordering'.²² The latter implies at least some level of renegotiation, with or without the benefit of a shareholder agreement.

In the US, research has also suggested that it is desirable to address exit rights in advance of the breakdown in the parties' relationship. Section 7.32 of the Revised Model Business Corporation Act (a model set of laws prepared by the Committee on Corporate Laws of the American Bar Association and adopted by many US states) goes so far as to say that an agreement among shareholders is effective even if inconsistent with one or more provisions of the corporate statute.²³ It has thus been claimed that such agreements can affect or eliminate the powers of the board of directors.²⁴ The agreements must be approved unanimously and are valid for ten years. This is unlikely to be the position in Australia however.

Can a shareholders agreement override the statutory contract in Australia?

It is submitted that a shareholder agreement cannot override the statutory contract in Australia.²⁵ At best there may be two agreements which are inconsistent. A court might be asked to rule on which is the true agreement between the parties however it is also likely that unhappy shareholders would bring concurrent actions for relief that may not rely on the contract(s) (such as oppression or winding up). In this sense the contractual argument may become moot. If not then the court would look at the parties' intentions, however to the extent that these reflect the shareholders agreement more than the constitution, it remains the fact that it will be difficult for a court to ignore the force of s140. This is why it is possible that a court may prefer to dispose of such a matter on non contractual grounds such as oppression (if such is found to exist).

In *Forrest v Appleyard* ²⁶(2006), faced with a shareholders agreement and another 'buyout' agreement Brereton J of the NSW Supreme court seemed to accept that the latter in time (the buyout agreement) could supervene the earlier shareholders

²² M J Whincop, 'A relational and doctrinal critique of shareholders' special contracts' [1997] *SydLLRev* 18.

²³ S K Miller, 'How should UK and US minority shareholder remedies for unfairly prejudicial or oppressive conduct be reformed?' *American Business Law Journal* Summer 1999 Vol 36 Issue 4 page 579.

²⁴ *Ibid.*

²⁵ Though enthusiasts for shareholder agreements have argued that such agreements can be 'an agreed superstructure to supplement and prevail over the articles which form the basic infrastructure'. See Stedman G and Jones J. *Shareholders Agreements* 2nd edition Longman 1990 at 53.

²⁶ [2006] NSWSC 281.

agreement. That reasoning may not be of much assistance however when one of the agreements is statutory in nature.²⁷

Another possibility which seems to have been left open by the court in *Northern Bank* is that of severance. In that case the company's contractual undertaking under the shareholders agreement was found to be unenforceable but it was independent of and therefore severable from the other shareholders' undertaking. It may be that a shareholders agreement will be left standing by the courts to the extent it is not directly inconsistent with the statutory contract and/or that the courts may remove the company as a party.²⁸

Action that is consistent with a shareholder agreement but inconsistent with the statutory contract (constitution and/or replaceable rules) is likely to be open to challenge. There is the possibility of altering the constitution to bring this into accord with a shareholders agreement however this has difficulties of its own. In *Gambotto v WCP Ltd*²⁹ the High Court said that an alteration of the constitution that involved expropriation of shares or valuable rights attaching to shares would need to be for a proper purpose and fair in all the circumstances. In that case an expropriation to ensure taxation and administrative advantages for the majority was not found to be a proper purpose. As to fairness this connoted a fair procedure for valuation of the shares including disclosure of relevant information as to price. The High Court also held in that case that an alteration to the constitution that did not involve expropriation of shares would be valid unless it was either beyond any purpose contemplated by the constitution or oppressive. The court did not give examples of the latter but they may be of potentially wide application in the context of changes to the constitution to bring it into accord with a shareholders agreement.

The effect of commercial arbitration clauses

One of the relevant issues raised by shareholder agreements for shareholder remedies is the fact that a shareholders agreement may provide that disputes will be dealt with in the form of private commercial arbitration under the law of a particular

²⁷ Though opinion seems divided on whether the 'statutory' nature of the statutory contract makes it more or less of a 'real' contract. Mantysaari remarks 'Although articles of association are regarded as a contract, articles of association are regarded only as a unique statutory form of contract and not as a normal contract.' See P Mantysaari, *Comparative Corporate Governance: Shareholders as a Rule maker*: Springer, Berlin, Heidelberg New York 2005. Certainly though it is more of a 'statutory' contract it is less of a 'true' contract.

²⁸ For a useful discussion on the severability argument in the *Northern Bank* Case see Goldwasser, above n 15 at 273-274.

²⁹ (1995) 13 ACLC 342.

state of Australia. Such clauses will tend to be enforceable.³⁰ If, however there was a dispute outside the shareholder agreement, such as the question of the validity or enforceability of the agreement itself due to alleged misrepresentation then it may be that if the other party resists then some element of the dispute might find itself before the courts. It should also be noted that given the range of matters that might be raised and the fact that the company cannot be a party to the shareholder agreement, a commercial arbitration clause in practice is no guarantee that a matter will be kept out of court.

In *A Best Floor Sanding Pty Ltd v Skyer Australia Pty Ltd*,³¹ the parties to a joint venture agreement had agreed to arbitrate any dispute, difference or question touching, inter alia, the dissolution or winding up of the 'association' which was their joint venture entity. Warren J in the Victorian Supreme Court declined an application for an order staying a winding up proceeding, under the Victorian commercial arbitration legislation, on the ground that the arbitration clause was null and void because it had the effect of 'obviating the statutory regime for the winding up of a company' (at paragraph [18]). Her Honour's decision was said to be partly based on public policy considerations surrounding the process of winding up a company pursuant to court order. An additional ground was that a winding up order operates to affect the rights of third parties, not merely the rights of the parties to the arbitration clause.

In *Acd Tridon v Tridon Australia*³² Austin J in the NSW Supreme Court commented on whether arbitration clauses were confined to contractual disputes or extended to disputes under the *Corporations Act* and equitable principles. By analogy he noted the views of Gleeson CJ in *Francis Travel Marketing Pty Ltd v Virgin Atlantic Airways Ltd*³³ that disputes under the *Trade Practices Act* could go to arbitration. Gleeson CJ had there stated:

First that it is possible and lawful for parties to agree to refer to arbitration a dispute under the Trade Practices Act 1974 (Cth), secondly, an arbitrator to whom such a dispute has been referred may, in general, exercise the discretionary powers which the Act confers upon the Supreme Court or the Federal Court, and, thirdly, that there is no reason to read down an otherwise comprehensive arbitration agreement in order to avoid a conclusion that this is what the parties have agreed to do ...³⁴

³⁰ See section 28 *Commercial Arbitration Act 1984 (Vic)*.

³¹ [1999] VSC 170.

³² [2002] NSWSC 896.

³³ (1996) 39 NSWLR 160.

³⁴ *Ibid* at 166.

Austin J also noted the above decision of Warren J in the Victorian Supreme Court but came to the following view:

I accept, as well, that public policy considerations operate against referring to arbitration a determination to wind up a company on the grounds upon which a court may order that a company be wound up. However, I would not regard these public policy considerations as preventing parties to a dispute from referring questions to arbitration merely because those questions arise under the Corporations Act. I see nothing special about the Corporations Act that would distinguish it, as a whole, from other legislation such as the Trade Practices Act.³⁵

He concluded:

Specifically, the public policy considerations held by Warren J to be applicable to a disputed claim to wind up a company do not seem to me to prevent the parties from referring to arbitration a claim for some merely inter partes relief under the oppression provisions of the Corporations Act, or for access to corporate information under s 247A.³⁶

Thus commercial arbitration will be allowable for inter partes relief though it may become problematic when the relief involves winding up action. In terms of the common remedies (as discussed below) it thus seems that to the extent that an oppression action seeks winding up as a form of relief there may be doubt as to whether the matter can, in the absence of mutual consent, be kept out of the courts. It would be unusual to seek winding up as a remedy in a statutory derivative action however to the extent this was sought it would also suffer from the same problem.

It seems to follow also that a dispute that was wider than that governed by the shareholders agreement and/or which involved other parties (such as the company) would not be required to be dealt with under the commercial arbitration clause.³⁷

Nevertheless it is likely that many disputes will, at least at first instance, not be dealt with by courts but dealt with by commercial arbitrators. This is unlikely to change things in substance however as they will be obliged to enforce the relevant law as agreed in the shareholder agreement as well as having regard to the substantive law as it may apply. Thus, the fact that there is agreement for commercial arbitration

³⁵ [2002] NSWSC 896 at para 192.

³⁶ Ibid at para 194.

³⁷ This is potentially problematic for commercial arbitration as the company is likely to be joined as a defendant in oppression or winding up action and will be, in a sense, the nominal plaintiff in a statutory derivative action.

would not of itself negate the existence of the shareholder remedies which could still normally be pursued in that commercial arbitration context.

Shareholder remedies

Contractual remedies

Parties to a shareholder agreement will have the full panoply of remedies for breach of contract including injunctions, specific performance and damages. Prior to that point too there is scope for argument about the contents of a shareholders agreement. It is likely that the parol evidence rule will be strongly operative in regard to the latter, however the possibility of incorporation of oral terms cannot be entirely eliminated (see *J Evans & Son (Portsmouth) Ltd v Andrea Merzario Ltd*³⁸). Indeed there is no necessary requirement (apart from compelling evidential considerations) that the shareholder agreement be written at all. *Mopeke Pty Ltd v Airport Fine Foods Pty Ltd and Ors*³⁹ has been interpreted⁴⁰ as an authority for the existence of an agreement which was not in writing that went beyond what was in the articles however the ‘common understanding’ was also referred to as a ‘legitimate expectation’, bringing it within the oppression cases rather than the contract realm (see below).

Further, the *Corporations Act* philosophy of ‘consumer protection’ for the consumers of financial services and financial products may mean that there is the possibility that a simple shareholders agreement or share sale agreement will not be seen as a straight forward ‘contract among equals’ (where a caveat emptor presumption will apply). Instead, given that shares are a financial product, there will be a focus on the need to protect the acquiror, even though disclosure on sale may or may not be specifically required under section 707 of the *Corporations Act 2001* (Cth).⁴¹

There will also of course be the full array of remedies for pre-contractual conduct including conduct going to the validity of contracts. These include damages for misrepresentation and the extremely wide remedies now available for misleading and deceptive conduct and for unconscionable conduct.

³⁸ [1976] 1 WLR 1078.

³⁹ (2007) 61 ACSR 395.

⁴⁰ Paul Faure, *Drafting Shareholder Agreements*, Seminar paper for Legalwise Seminar Essential elements for effective shareholder agreements. Melbourne, 10 September 2008.

⁴¹ Section 707(1),(2) and (3) require disclosure for offers of securities for sale if the person making the offer controls the body and the securities are not quoted or are not offered for sale in the ordinary course of trading on a relevant financial market or if the sale amounts to an indirect issue. This is subject to the various types of small scale, personal and other offers set out in s708 that do not require disclosure.

I do not propose to give a detailed dissertation on the contractual remedies or remedies for pre-contractual misrepresentation however the significance of these for contractual certainty (or lack thereof) will be noted.

It should also be noted that the ultimate enforceability of the remedies will depend upon them being able to be reduced to court orders. This is because, in the absence of enforcement by consent, there is no machinery to enforce the outcomes of commercial arbitration.

1 *Specific performance and injunction*

The most desired remedy under a shareholders agreement is likely to be the equitable remedy of specific performance (and to a lesser extent, injunction).⁴² Thus a shareholder may wish to hold another shareholder to the terms of the agreement and will ask the court that it require the other shareholder to perform a specific act or acts as stated in the agreement. Whilst this may be the most desired remedy, in practice it may often be difficult to obtain as there are various situations where the remedy cannot be granted. Discretionary factors include:

- a) the need to show that the plaintiff is ready and willing to perform the contract;
- b) there must be mutuality between plaintiff and defendant (ie it must be shown that the defendant could have enforced as well);
- c) there should not be severe hardship or unfairness caused to the defendant;
- d) the plaintiff must come to the court with clean hands (specific performance being an equitable remedy); and
- e) there must not have been any misrepresentation, mistake or unconscionability.

In a shareholders agreement, the unavailability or impracticality of specific performance may itself become evidence of a breakdown in the relationships between shareholders that itself may be grounds for the more traditional company law remedies of oppression or winding up on the just and equitable ground (see below). Likewise multiple breaches may tell in favour of a breakdown in the relationship. Attempting to obtain specific performance for multiple breaches may also make this a more ambitious remedy.

⁴² Goldwasser has stated (in 1994) that 'nearly all of the recent decisions in the United States recognise that shareholder agreements are properly enforceable by a decree of specific performance or by injunctive relief.' See Goldwasser above n 15 p 279.

In relation to both specific performance and injunction (though more commonly in relation to the latter which is more often granted on an interim basis) the plaintiff will need to be prepared to provide an undertaking as to the damages of the defendant in the event that the plaintiff does not succeed at trial. Whilst this would be true of any interim remedy including interim relief granted under the company law remedy of oppression the need for such an undertaking may cloud the desirability of the contractual remedy where there is substantial disputation as to the contents and enforceability of the shareholders agreement itself.

2 *Damages*

Where specific performance is not available an action for damages for the breach is likely. This may have problems of its own as it is necessary to quantify the value of the loss to the plaintiff that is caused by and flows from the defendant's breach.⁴³ This may be difficult to quantify in a shareholders agreement depending upon the nature of the breach. Further, multiple breaches will require calculation of damages for each breach which in some cases may overlap. Lastly, the 'damage' to the extent it exists may flow to the company itself.

3 *Rescission*

In some cases, a breach by another shareholder of a fundamental term of the shareholder's agreement may give an entitlement to rescind the entire agreement. If this occurred damages would be required to put the innocent shareholder back into the position he would have been in before he entered into the contract. This may be difficult to assess in the context of a shareholders agreement. The person may have been a shareholder in the company before the shareholders agreement was entered into, it may have been entered into at the same time as the incorporation of the company or the shareholder may have entered the agreement at the time he acquired his shares. In all cases the measure of loss may be difficult to calculate.

In the case of multiple breaches it will be necessary to identify which breaches will justify the remedy.

Avoiding the shareholder agreement

Just as one party may desire to enforce specifically the shareholder agreement it is quite possible that the other party, in resisting this may seek to avoid the contract in its entirety. The means by which this could occur include the following:

⁴³ *Hadley v Baxendale* (1854) 9 Ex 341:156 ER 145.

Misrepresentation

A false statement of fact made by one shareholder to another prior to entry into the shareholders agreement may entitle the innocent party at his option to rescind from the contract and rescind. By contrast there is no law to suggest that the statutory contract can be rescinded (though rescission for misrepresentation may be available on the initial share subscription providing that the company is not in liquidation⁴⁴).

Misleading and deceptive conduct

Misleading or deceptive conduct engaged in relation to a financial product (which includes shares) which contravenes s1041H of the *Corporations Act 2001* (Cth) and causes loss or alleged loss may form the basis for action under s1325 which may include the remedy of variation of the shareholders agreement, a refusal of the court to enforce all or any of the provisions of the shareholders agreement or a declaration that the shareholders agreement is void.⁴⁵ Thus a shareholder who complains about misleading conduct at the time he entered a shareholders agreement may have entitlements to avoid the agreement or have it varied.

Unconscionable conduct

Unconscionable conduct engaged in relation to the supply or possible supply of financial services (which includes dealing in financial products such as shares) which contravenes s12CB or 12CC of the *ASIC Act 2001* (Cth) and causes loss or alleged loss may form the basis for action under s12GM(7) of that Act, which may include the remedy of variation of the shareholders agreement, a refusal of the court to enforce all or any of the provisions of the shareholders agreement or a declaration that the shareholders agreement is void. Thus a shareholder who complains about misleading conduct at the time he entered a shareholders agreement may have entitlements to avoid the agreement or have it varied.

The company law remedies

It is submitted that a shareholder agreement may have no direct effect on the ability of a member to seek any of the main shareholder remedies, at least where the shareholders agreement does not include the company as a party (as it probably should not do according to *Northern Bank*). There may be indirect effects in that the shareholders agreement may form the backdrop for the legitimate expectations of shareholders against which the question of unfairness or inequity will be judged.

⁴⁴ See *Crosbie; Re Media World Communications Ltd v Naidoo* (2005) 216 ALR 105; (2005) 52 ACSR 346; (2005) 23 ACLC 281; [2005] FCA 51.

⁴⁵ See ss 1325(5)(a), (b) and (c) of the *Corporations Act 2001* (Cth).

There is also the possibility of a member who has sought to contract out of his statutory and common law rights. Even here it seems unlikely he will be shorn of all those rights as many of them are substantive and the contractual surrender might be void for illegality.

1 *Oppression*

The Australian oppression remedy has wide scope. In *Wayde v New South Wales Rugby League*⁴⁶ Ltd Brennan J said in relation to the then oppression provision (section 320):

The operation of s320 may be attracted to a decision made by directors which is made in good faith for a purpose within the directors' power but which reasonable directors would think to be unfair. The test of unfairness is objective ... the test assumes (whether it be the fact or not) that reasonable directors weigh the furthering of the corporate object against the disadvantage, disability or burden which their decision would impose, and address their minds to the question whether a proposed decision is unfair.⁴⁷

Further in *Saykan v Elhan, Re Unique Doors Pty Ltd*⁴⁸ Nettle J said in respect of the modern oppression provision:

As was explained in *Aqua-Max Pty Ltd v MT Associates Pty Ltd*, s 260 of the Corporations Law (the precursor of s 234 of the Corporations Act) represents the results of a series of amendments made to precursors, which included s 186 of the Companies Act 1961 and s 320 of the Companies Code, that have had the effect of broadening the operation of the section to include conduct which is unfairly prejudicial to or unfairly discriminatory against a member or members rather than merely oppressive, and to include discrimination against a member other than as a member. Thus, as it has been said, the section as it is now exposes to legitimate complaint any conduct of the company which is unjustly detrimental to any member of the company whatever form it takes and whether it adversely affects all members alike or discriminates against some only.⁴⁹

There does not appear to be direct Australian authority on direct conflict between a shareholder agreement and oppressive conduct. There are however cases on the interaction of the company constitution with the oppression provision. In *Caratti*

⁴⁶ 1982) 180 CLR 459.

⁴⁷ Ibid at 472.

⁴⁸ [2006] VSCA 230.

⁴⁹ Ibid at para 32.

*Holdings Co Pty Ltd*⁵⁰ it was made clear by the Western Australian Supreme Court that though a company constitution could empower the majority shareholder to acquire shares compulsorily from the minority shareholder, this could still be disallowed for other reasons such as oppression.

Similarly in *Re Medfield Pty Ltd*⁵¹ the chairman had a casting vote under the constitution however this did not prevent an injunction being granted to restrain him from exercising that casting vote on a motion to require one of the 'partners' to deliver up a secret formula. It was found that at the time of incorporation none of the other directors had knowledge of this casting vote which was considered to be significant.

In *Re Wondoflex Textiles Pty Ltd*⁵² the company was found to resemble a partnership. Smith J considered the relationship between a company's articles and oppression.

It is also true, I think, that, generally speaking, a petition for winding-up, based upon the partnership analogy, cannot succeed if what is complained of is merely a valid exercise of powers conferred in terms by the articles; ... to hold otherwise would enable a member to be relieved from the consequences of a bargain knowingly entered into by him; ... but this, I think, is subject to an important qualification. Acts which, in law, are a valid exercise of powers conferred by the articles may nevertheless be entirely outside what can fairly be regarded as having been in the contemplation of the parties when they became members of the company; and in such cases the fact that what has been done is not in excess of power will not necessarily be an answer to a claim for winding-up. Indeed, it may be said that one purpose of [the just and equitable provision] is to enable the court to relieve a party from his bargain in such cases.⁵³

A recent case, *Campbell v Backoffice Investments Pty Ltd*⁵⁴ is an illustration of shareholder agreements gone wrong and there is no suggestion in the case that the oppression remedy would not be available because it was a shareholder agreement case (though the shareholder agreement/oppression point was not specifically argued and nor was the *Russell v Northern Bank* decision mentioned). Indeed the learned judges on appeal all accepted the trial judge's conclusions that there had indeed been oppressive behaviour.

⁵⁰ [1975]1 ACLR 87.

⁵¹ (1977) 2 ACLR 406.

⁵² [1951] VLR 458.

⁵³ *Ibid* at 467.

⁵⁴ (2008) 66 ACSR 359.

The case concerned various agreements including the shareholder agreement, a share sale agreement and service agreements. The shareholder agreement provided that Mr Campbell and Mr Weeks were to be co-directors with equal voting power and were to be joint managing directors having the day-to-day conduct and management of the company. Within months the relationship of the two broke down and Weeks was applying for orders that Campbell repurchase shares on the basis of oppression.

Interestingly in that case there was also mention of s72(3) of the *Fair Trading Act 1987* (NSW)⁵⁵ which allows contracts to be declared void. This argument was run as an alternative remedy to oppression. In the case damages were ultimately awarded for misleading and deceptive conduct in relation to the giving of contractual warranties by the vendor of the shares. This illustrates reliance on contractual principles (and misleading and deceptive conduct in relation to same) as an alternative to the statutory (company law) actions. It also illustrates however that the idea of contract itself as a tool to reduce uncertainty may be somewhat illusory given the numerous statutory and other overlays to the law of contract itself.⁵⁶

The case does show the mixing of contract law with the shareholder remedies where there is a shareholder agreement. Damages of \$850,000 were awarded for the breach, alternately to be returned following the voiding of the contracts under 72(3) of the NSW *Fair Trading Act* (a remedy under that Act for the misleading and deceptive conduct). Though largely regulated by the 'consumer protection' measures of the *Corporations Act* the whole fact of bringing contractualism into the argument between shareholders also raises the spectre of the traditional common law issues for contracts – including misrepresentation, identification of terms and warranties and so on – into the realm of internal company disputes.

Can a shareholders agreement be harsh, unfair or prejudicial? This would seem to be the case if its consequence is that it leads to situations that are usually the subject of oppression actions. These are in summary:

- Where directors running a company in their own interests & ignoring interests of shareholders - *Re Spargos Mining NL*⁵⁷
- Directors improperly issuing shares to themselves to outvote other shareholders – *Hannes v MJH Pty Ltd*⁵⁸

⁵⁵ Ibid. Paragraph 13 of the judgment of Gyles J.

⁵⁶ It is also open to question whether misleading and deceptive conduct under the *Fair Trading Act* was jurisdictionally appropriate given that the representations were made in connection with the sale of shares which are financial products and are dealt with under the *Corporations Act 2001* (Cth) and *ASIC Act 2001* (Cth).

⁵⁷ (1990) 3 ACSR.

⁵⁸ (1992) 7 ACSR 8.

- Excluding the director of a family company from being involved in management decisions
– *Fexuto Pty Ltd v Bosnjak Holdings Pty Ltd*⁵⁹
- Directors/major shareholders diverting business opportunities to themselves
– *Scottish Co-operative Wholesale Society Ltd v Meyer*⁶⁰
- Directors paying themselves excessive salaries at the expense of dividends to shareholders (though high salaries are not in themselves oppressive)
– *Sanford v Sanford Courier Service Pty Ltd*⁶¹

Thus if the contents of a shareholders agreement allows for one of these types of situations to occur then it seems likely that oppression will be established.

It is already established that conduct which may accord with the company's constitution (ie the statutory contract) can still be unfairly prejudicial. For example in *Sutherland v NRMA Ltd*⁶² the court found that a constitutional provision limiting directors to 70 years of age or under was unfairly prejudicial to or unfairly discriminatory to the applicant.

It seems likely therefore that conduct which may accord with a shareholders agreement may still be unfairly prejudicial and oppressive.

Conversely one of the principal areas for relief in the context of the oppression remedy in relation to proprietary companies is the area of exclusion from management. This situation often applies in the situation of closely held corporations which are incorporated but which were originally set up on the basis of a partnership. It has been argued that shareholders agreements, rather than facilitating the tyranny of the majority, are more likely to have the primary purpose of eliminating the tyranny of the majority.⁶³ In that case a shareholder agreement may provide the legitimate expectation argument for either the prosecution or defence of an oppression action. Exclusion from management is a common example of the undermining of an expectation. It occurred in the case of *Fexuto Pty Ltd v Bosnjak Pty Ltd*⁶⁴ which deserves consideration at some length. The facts were as follows: ⁶⁵

⁵⁹ (1998) 28 ACSR 688.

⁶⁰ [1959] AC 324.

⁶¹ (1987) 10 ACLC 549.

⁶² (2003) 47 ACSR 428.

⁶³ Elson, A. 'Shareholders Agreements: A Shield for Minority Shareholders of Close Corporations' (1967) 22 *Business Lawyer* 449.

⁶⁴ (2001) 37 ACSR 672).

⁶⁵ I have borrowed some elements of the succinct summary of facts and decision that appeared in the Australian Company Director Journal (Oppression Remedy Bites Hard -

Fexuto was the family company of Bob Bosnjak ('Bob'). Along with other family members, it was a shareholder in Bosnjak Holdings, the holding company of a group of related companies that operated Westbus Group, a large private bus company. Bob's company held 2/7 shares in the Westbus Group. Other family members, mainly Jim and Carol Bosnjak, held the balance of the shares.

Their father, the group founder died in 1979. Their mother Anda died in 1992 and tension then developed between the brothers. In 1993 Carol Bosnjak was appointed as a director while Bob Bosnjak was overseas. Carol usually voted with her husband Jim. Together, Jim and Carol Bosnjak held 57 percent of the shareholding. Bob Bosnjak and his company were then increasingly alienated from decision-making and from 1988 onwards Bob Bosnjak unsuccessfully made proposals that the assets of the business should be split between family members.

There were allegations by Bob that Jim and Carol Bosnjak had used the company's resources and information to obtain a lucrative bus services contract for a separate company controlled and owned by them. Bob further alleged that Jim Bosnjak had taken up an opportunity known as 'Transcard', acquiring a 50 percent interest in an international venture without disclosing his interest to Westbus.

Bob won at first instance on oppression but was unhappy with the nature of the orders made which he believed gave too much flexibility to Jim and Carol. The New South Wales Court of Appeal (Spigelman CJ, Priestley and Fitzgerald JJA) ordered more substantive orders in favour of Bob and his company.

In the court's view Westbus Group was in effect a corporate partnership between the members of the Bosnjak family. The brothers could be classified as de facto 50/50 'partners' who traditionally made joint decisions about their family business. The structure had been set up on the basis of a principle of equality between the brothers and their families. Bob Bosnjak was therefore entitled to take an equal part in the direct management of the companies. In reaching this conclusion the court applied a series of cases in which closely held family companies were treated as though they were quasi partnerships with the relevant members having responsibilities towards each other as though they were equal partners.

Law Reporter- September 2001)

<http://www.companydirectors.com.au/Media/Company+Director+journal/2001/September/Oppression+remedy+bites+hard++Law+Reporter.htm> viewed 22 July 2008 which in turn is said to draw from a Butterworths Law Report.

Bob also argued that he had a right of veto. The court did not agree however with Bob's argument that he had a right of veto in relation to the way in which the affairs of the company were being conducted. The court considered that for such a conclusion to exist would have required the proof of an understanding that the majority shareholders in the company (who normally have control) would have such a right specifically qualified. In the present case Bob was not able to point to any document, nor give any evidence of any conversation, by which the 'understanding' for which he contended was created or could be inferred. The fact that Bob and Jim were the only active participants in the management of the company did not by itself create a right of veto or a legitimate expectation of such a right. In the court's view in a quasi partnership of this kind the existence of a right to veto could only be inferred on the basis of appropriate documents or evidence that was quite clear.

This would suggest that, despite success on the 50/50 argument, the existence of a shareholders agreement could have provided the basis for the legitimate expectation or the 'understanding' of a right of veto that Bob Bosnjak sought to argue for. Unfortunately for Bob, no such shareholders agreement existed in this case.

2 *Just and equitable winding up*

As for oppression, any written agreement between shareholders might be unfair or prejudicial if its consequence is that it leads to situations that are usually the subject of just and equitable winding up actions. These are in summary:

- Deadlock
– re *Yenidje Tobacco* ⁶⁶
- Breakdown of mutual trust and confidence in 'partnership' type companies
– *Ebrahimi v Westborne Galleries*⁶⁷ (as can be seen there is in this category an overlap with the s 232 oppression remedy)
- Fraud or misconduct (again there is an overlap with s 232 oppression remedy)
- Failure of substratum of company
– *Re Tivoli Freeholds*⁶⁸

Conversely again, in the context of winding up on the just and equitable ground under s461(1)(k) 'legitimate expectation' arguments were made in *Ebrahimi*.⁶⁹ It has been noted that part of the rationale for relief in these types of cases relies upon the

⁶⁶ [1916] 2 Ch 426.

⁶⁷ [1973] AC 360.

⁶⁸ [1972] VR 445.

⁶⁹ [1973] AC 360.

doctrine of 'legitimate expectation' rather than actual illegality of conduct. The rationale of the ground is that a member's interests should not be disregarded in conducting the affairs of the company.⁷⁰ Thus with the rise in use of shareholders agreements it may be possible for shareholders to rely on such agreements in specifying the understanding existing between the parties to the agreement so that exclusive reliance on articles may not be required.⁷¹

Certainly whether there has truly been a breakdown of trust and relations is an issue that may be illuminated by the contents of a shareholders agreement (as to what it is contemplated should be happening as between shareholders) so that it is likely that such document, together with the conduct of the shareholders, will feature prominently as evidence in this type of proceeding.

It is useful to try to look at practical examples of shareholder agreements and how the shareholders remedies may deal with them. In *Bosnjak*, as has been noted, one shareholder claimed a general right of veto however the court found that there was no evidence of such. Assuming such a right of veto did exist in a shareholders agreement how would it play out in practice? The vetoer would initially seek an injunction to stop the conduct complained of (though this might be sought in the context of out-of-court commercial arbitration). The other party may argue that the veto is itself oppressive or likely to lead to a breakdown in relations by deadlocking the company. This could itself provide the basis for the oppression remedy or the winding up remedy which might take place in court given that the company may need to be a party to get the remedy desired. On the other hand the existence of the veto in a shareholders agreement might be said to provide the legitimate expectations of the vetoer that would defeat the vetoer's oppression action and possibly defeat winding up action (though it might be hard to argue that the company is not deadlocked).

3 *The statutory derivative action*

Any written agreement b/w shareholders can be problematic if it leads to situations that may be the subject of a statutory derivative action. For this to occur the shareholders agreement would have to somehow cause loss and damage or loss of opportunity to the company itself.

The statutory derivative action is an action that the company has against a third party but has neglected or refused to pursue against that third party. A shareholder or

⁷⁰ Sulaimann, Dr A, 'Legitimate expectation, the oppression provision and shareholders' agreement in Malaysia, (2001) 12 *Australian Journal of Corporate Law* 229.

⁷¹ *Ibid.*

former shareholder can, with leave of the court bring the action under sections 236 – 242. It is necessary to show that

- It is probable that the Company will not take action itself
- The Applicant is acting in good faith
- It is in company's best interest for application to be granted
- There is a serious question to be tried⁷²

Conversely again, a shareholders agreement might provide some basis for a company to refute some of the discretionary matters set out in s236-242 and so establish that the applicant cannot make out these requirements. For instance it may be that the shareholders agreement provides a rationale for conduct by a former officer that the applicant now complains about.

In some cases (at least in the case of nominee directors) it had been found that shareholders could unanimously agree to 'attenuate' the fiduciary duties which they would otherwise owe to the company. In *Levin v Clark*⁷³, nominee directors who were nominated to the board of the company by a mortgagee were held to have been entitled to act primarily in the interests of the mortgagee after a default by the mortgagor company. Jacobs J said: that summarised the position thus:

The breadth of the fiduciary duty has been narrowed, by agreement amongst the body of the shareholders.⁷⁴

In *Japan Abrasive materials Pty Ltd & Ors v Australian Fused Materials Pty Ltd*⁷⁵ (another shareholder agreement case) Templeman J in the Supreme Court of Western Australia quoted Jacobs J with approval and noted:

It is always open to shareholders by unanimous agreement to attenuate the fiduciary duties which the directors of their company would otherwise owe to it.⁷⁶

Austin and Ramsay have noted that the attenuation of duty found in *Levin* was sufficient to allow the nominee directors to act in the mortgagee's interests but would

⁷² A practical example of the application of the tests can be found in *Charlton v Baber* (2003) 47 ACSR 31 and more recently in *Chahwan v Euphoric Pty Ltd trading as Clay Michel* [2008] NSWCA 52 (8 April 2008) and *Showtime Management Australia Pty Ltd v Showtime Presents Pty Ltd* [2008] NSWSC 618 (17 June 2008).

⁷³ [1962] NSW 686.

⁷⁴ *Ibid* at 700.

⁷⁵ (1998) 16 ACLC 1172.

⁷⁶ *Ibid* at 1178.

presumably not have been sufficient to allow them to embark on a course of oppressive conduct designed to injure minority shareholders by destroying the company's business.⁷⁷ This may be a warning that the concept of attenuation of general directors' duties is potentially fraught with difficulty.

The attenuation of duty in a shareholders agreement is perhaps a little similar to the ratification defence where the shareholders ratify conduct by its officers (though ratification connotes a majority vote whereas a shareholder agreement is presumably unanimous). The shareholders agreement would not ratify the conduct but may make it explicable and 'reasonable' so that it may no longer be possible to establish a serious question to be tried. An example might be a shareholders agreement that provides that the shareholders endorse the use and appointment by the directors of a particular outside expert who later turns out to be incompetent. This may make it more difficult to argue that the company should take action against the outside expert or the directors for negligence (though there might then be argument about what shareholders knew or were told prior to entering into the shareholders agreement).

A general meeting may ratify certain breaches that have occurred provided the majority was not a participant in the breaches⁷⁸ and providing the company was solvent. In the context of the statutory derivative action ratification does not prevent the derivative action being brought and does not however mean that the proceeding must be determined in favour of the defendant.⁷⁹ It is possible therefore that provisions of a shareholders agreement which may justify or ameliorate such breaches will similarly be taken into account but will not be crucial in a statutory derivative action.

To the extent that it is argued that taking a derivative action is a breach of the shareholders agreement novel questions may arise in contract. Under s236(1) the proceedings are brought on behalf of the company so that action against the shareholder to restrain her from taking derivative action may not necessarily derail a derivative action once it is on foot as it is the company's and not the shareholder's action.

Another novel situation may arise in relation to shareholders agreements and the statutory derivative action in that in some cases it may be arguable that a loss, damages or injury resulting from the breach of the shareholders agreement may be

⁷⁷ Austin and Ramsay above n 18 para 9.440.

⁷⁸ *Ngurli v McCann* (1953) 90 CLR 425.

⁷⁹ Section 239 of the *Corporations Act 2001* (Cth).

suffered by the company rather than by a shareholder.⁸⁰ This will present a novelty where the draftsman has taken a cautious view of the dicta of *Russell* and excluded the company itself as a party to the shareholder agreement as, in such situation, the party to the loss will not be privy to the contract that has been breached. This may leave the company without a remedy.

How would the shareholders agreement allowing for veto rights fare in relation to this procedural mechanism? The vetoer would attempt to exert right of veto and either the vetoer or the vetoee would seek an injunction, probably in the context, initially, of commercial arbitration. The party complaining of a breach of duty to the company however would likely be able to bring the matter before the ordinary courts on the basis that the company is a party to the action and not a party to the shareholders agreement. In either case the issue would likely again be use of the veto to effectively ratify or forgive alleged breaches of duty. As noted the court or arbitrator could take this into account but would not be beholden to such ratification. There is still the possibility of a breach of duty being found.

Procedural issues

As indicated most shareholders agreements will be in small proprietary companies however this will not always be the case.⁸¹ There is the possibility for shareholders agreements in larger entities where there is an historical preference for a non conventional structure such as a co-operative. Under this type of structure there may be a desire for strict controls to remove the possibility that the structure is itself altered. A common rule for co-operative structures is that each member has an equal number of shares to preserve the mutuality of such a firm. New shareholders must agree to the structure before being allocated shares.

In this situation a shareholder dispute might become quite large and procedurally complex. It is likely that large numbers of shareholders seeking to enforce the terms of a shareholders agreement or take action to remove the effects of such an agreement would band together and select a representative shareholder to bring the proceeding.⁸² This would be what is known as a shareholder class action (a phenomenon unlikely in proprietary companies).

Similarly shareholders agreements might seek to affect class rights and in that situation there may be one shareholder bringing action on behalf of the class as a

⁸⁰ Goldwasser above n 15 p279 referring to O'Neal F.H. and Thompson R.B., *O'Neal's Oppression of Minority Shareholders* (2nd edition), Callaghan and Co 1991.

⁸¹ Sealy above n. p108.

⁸² See Part IVA *Federal Court Act* (Cth) and Part 4A *Supreme Court Act* (Vic).

whole.⁸³ One of the tests as to whether a variation of class rights has occurred is whether certain conduct (such as an issue of new preference shares for example) is authorised by the company's constitution as in force when the original preference share issue was made.⁸⁴ It is not clear that the authorisation of same by a shareholders agreement however would constitute authorisation in the same manner so as to prevent the share issue being a variation of class rights. This is perhaps one specific example of the dangers of assuming shareholders agreements have the same standing as the constitution even though in some cases they may act in a similar manner.

Representative proceedings of any type are likely to be difficult and complex (and these days may also have the involvement of litigation funders where relief involves a monetary sum). The well known NRMA case⁸⁵ involved issues of demutualisation and seeming effects on shareholder rights and involved considerable and complicated proceedings before the courts. Ultimately the case made law on matters of corporate disclosure rather than variation of shareholder rights. Likewise various non disclosure cases (eg *King v GIO Limited*⁸⁶ and *Dorajay Pty Ltd v Aristocrat Leisure Ltd*⁸⁷) have involved considerable procedural complexity though it is not clear that shareholders agreements, had they existed, could have played any significant part in such proceedings. Again however, it may depend upon what the shareholders actually agreed and whether those matters bore upon the matters which were ultimately litigated.

Conclusion

Shareholders agreements are increasingly part of the commercial scene as shareholders, mainly in closely held corporations, attempt to plan in advance for contingencies that may occur in the corporation's management and also to protect

⁸³ S 246D (1) of the *Corporations Act* (Cth) provides that if members in a class do not all agree to a variation or cancellation of their rights or a modification of the company's constitution (if any) to allow their rights to be varied or cancelled then members with at least 10% of the votes in the class may apply to the Court to have the variation, cancellation or modification set aside. S 246D(4) provides that the members of the class who want to have the variation, cancellation or modification set aside may appoint 1 or more of themselves to make the application on their behalf. The appointment must be in writing.

⁸⁴ See s246C(6) *Corporations Act*.

⁸⁵ The 'float case' (1994) 52 FCR 1; (1994) 124 ALR 548; (1994) 14 ACSR 656; (1994) 12 ACLC 855; (1994) ATPR 41-346; BC9400259 and on appeal at (1995) 55 FCR 452; (1995) 127 ALR 543; (1995) 15 ACSR 590; (1995) 13 ACLC 132; (1995) ATPR 41-374.

⁸⁶ Various decisions Federal Court 1999-2004.

⁸⁷ Various decisions Federal Court 2003-2008.

and/or solidify existing corporate relations between shareholders. The difficulties of predicting the future or the types of situations that may arise in the future means that there is always the possibility of disputation - the shareholders agreement may seek itself to ameliorate or provide a governance mechanism to resolve such disputes. Nevertheless there is the fact that disputation may not be readily resolved so that the parties are likely to move into a second phase of enforcement of rights under the agreement. This may take place in the courts or commonly may take place under commercial arbitration as agreed between the parties in the shareholders agreement. It is likely however that such disputation may go beyond mere contractual disputation under the shareholders agreement and pick up the more traditional company law shareholders' remedies such as oppression, winding up or the derivative action. Even where the parties limit themselves to contractual disputation there is the possibility of extra contractual litigation in relation to pre-contractual misrepresentations, or misleading or deceptive conduct.