UNANIMOUS ASSENT TO THE DUOMATIC PRINCIPLE: ACCEPTANCE IN NEW ZEALAND

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Introduction

Since the landmark case, *Salomon v Salomon*, which clarified the relationship between a company and its shareholders, a company is often referred to as a separate legal person.[1] It was later noted it is no *ding an sich*.[2] There is no company, except for an intangible statutory construct. Accordingly, a company is not competent to act or refrain from acting, and requires a means by which acts may be attributed to it. It is therefore important how the powers within the company are allocated to the various parties.

The allocation of management powers has been subject to recent discussion in New Zealand appellate courts. The Court of Appeal in *Attorney-General v Ririnui*, was asked to determine whether shareholders could unanimously usurp the management powers allocated to the board of directors.[3] The principle of informal unanimous assent was relied upon to empower the shareholders to act in such a manner. This principle is often, and hereinafter, referred to as the *Duomatic* principle as it was simply stated by Buckley J in the English case *Re Duomatic Ltd* in the following terms:[4]

> … where it can be shown that all shareholders who have a right to attend and vote at a general meeting of the company assent to some matter which a general meeting of the company could carry into effect, that assent is as binding as a resolution in general meeting would be.

It appears rudimentary to clarify this principle merely permits shareholders to do informally that which they may do formally in general meeting. This principle, however, has been misinterpreted as a principle empowering shareholders to manage the company.[5] Indeed, this was a concern of the Court of Appeal in *Ririnui* where the *Duomatic* principle was ultimately held not to apply. Leave to appeal was granted by the Supreme Court which provided an opportunity for the status of the principle to be settled. However, the Supreme Court provided little guidance on the principle, merely doubting the application of the principle under the Companies Act 1993 (1993 Act).[6] This paper will clarify the scope of the *Duomatic* principle and its application in New Zealand.

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[1] *Salomon v Salomon & Co Ltd* [1897] AC 22 (HL) at 51.
[2] *Meridian Global Funds Management Asia v Securities Commission* [1995] 3 NZLR 7 (PC) at 12. "Ding an sich" refers to a thing being as it is in itself, it is not mediated through perception of the senses. Formulated by philosopher Immanuel Kant, it is used in this context to suggest a company does not actually exist in itself as it is a conceptual construct.
[3] *Attorney-General v Ririnui* [2015] NZCA 160.
[4] *Re Duomatic Ltd* [1969] 2 Ch 365 (Ch) at 373.
[5] See Ross Grantham "The Unanimous Assent Rule in Company Law" [1993] CLJ 245 and Susan Watson "*Attorney-General v Ririnui* core company law preserved in the Court of Appeal" [2016] NZLJ 38.
[6] *Ririnui v Landcorp Farming Ltd* [2016] NZSC 62 at [167].

Chapter I will explore the development of the *Duomatic* principle from its inception in partnership law, its application to joint stock companies and its application to the modern incorporated company. The development of the principle by English and New Zealand courts will be assessed to identify its scope.

Chapter II will consider the current status of the *Duomatic* principle in light of the 1993 Act. The shareholders' reserve powers of management will be considered before an assessment of the current statutory allocation of management powers. The shareholders' ability to exercise powers unanimously and informally will be discussed, and the consistency of such informality with the 1993 Act will be analysed. Through this inquiry, the current status of the *Duomatic* principle in New Zealand will be identified.

Chapter III will assess the appropriateness of the *Duomatic* principle in New Zealand. Possible justifications for the principle will be considered as well as its consistency with the objectives of the 1993 Act and corporate regulation.

The thesis advanced by this paper argues the *Duomatic* principle has remained part of New Zealand corporate law, and demonstrably should.

Chapter I: Development of the Duomatic Principle

The formulation of the *Duomatic* principle in England and New Zealand will be assessed so one description of the principle may be identified. Historic formulations of the *Duomatic* principle can be traced through to the most recent formulation and discussion of the principle in New Zealand. Identifying its correct formulation will assist in the assessment of whether the principle has survived the 1993 Act.

A Application to Partnerships and Joint Stock Companies

The informal unanimous assent of shareholders is a principle much older than the case in which it was accredited its name.[7] The *Duomatic* principle was born in partnership law where partnership deeds were found to be subject to the informal unanimous assent of all the partners.[8] In the context of partnership deeds, it was held a written agreement governing a partnership may be varied informally if there is a course of conduct that demonstrates all the partners had agreed to change the original written agreement.[9]

This principle was later recognised in the realm of joint stock companies.[10] In *Re Vale of Neath and South Wales Brewery Company* (*Morgan's Case*) the board sought to enter into an arrangement which they had no power to enter into under the deed of settlement.[11] It was held the directors could not depart from the deed of settlement without the consent of every individual shareholder. Such consent would, in effect, alter the deed of settlement to give the directors the necessary power.[12]

Furthermore, the formalities required under a deed of settlement of joint stock companies could historically be satisfied by implication where all shareholders acted collectively. In *Re British Provident Life and Fire Assurance Society* (*Grady's Case*), the deed of settlement provided for a power of the board to be subject to approval by a majority of shareholders, which was not obtained.[13] It was held, however, all shareholders had knowledge of the arrangement so an inference could be drawn that the formality had been either antecedently supplied or subsequently added to the arrangement.[14]

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[7] *Re Duomatic Ltd*, above n 4.
[8] *Const v Harris* (1824) Turn & R 496 (Ch).
[9] *Const v Harris*, above n 8, at 523.
[10] *Re Vale of Neath and South Wales Brewery Company* (1849) 1 De G & S 750 [*Morgan's Case*] at 776; See also *Re Cameron's Coalbrook Steam Coal Swansea Railway Co* (1854) 5 De GM & G 284 at 297–298 where it was held the board of directors cannot act outside the authority which the deed of settlement provides unless previous authority or subsequent concurrence by all shareholders has been given.
[11] *Morgan's Case*, above n 10, at 776.
[12] At 776.
[13] *Re British Provident Life and Fire Assurance Society* (1863) 1 De GJ & S 488 [*Grady's Case*] at 492–493.
[14] At 196.

The authority relied upon in *Grady's Case* was not directly on issue. *Bargate v Shortridge* was cited as authority for a finding that a requisite formality had been impliedly complied with.[15] In *Bargate*, a transfer of shares had occurred despite the deed of settlement requiring the board to provide its consent, which was not provided. The transfer was upheld as the board could not neglect to comply with its duties under the deed of settlement and later rely on this neglect to invalidate a transfer. This case differed from *Grady's Case* as the board, not the shareholders, had ignored a formality which was later held to not invalidate the transaction. Furthermore, the rights of a third party were in issue and subject to abrogation if the transaction was invalidated. Nevertheless, *Grady's Case* has since been approved and may be taken as authority for recognising the powers of shareholders acting as a collective where only the company's rights are concerned.[16]

B Development in England

The more familiar roots of the *Duomatic* principle are found in *Salomon* where the shareholders acting unanimously and informally validated a transaction between the company and another.[17] Lord Davey stated:[18]

> I think it an inevitable inference from the circumstances of the case that every member of the company assented to the purchase, and the company is bound in a matter intra vires by the unanimous agreement of its members.

This passage illustrates the power of shareholders' informal collective conduct to make decisions on behalf of a company. This case is often cited for recognising a company's separate legal personality, distinct from its shareholders. Although the company is a distinct legal person at law, it is required to make decisions. *Salomon* suggests when the shareholders are acting unanimously, their decision will be the decision of the company even if made informally. This is not inconsistent with the finding of separate legal personality. *Salomon* confirms limited liability operates despite the beneficial ownership of all shares and total control of the company residing in one person.[19]

The informal unanimous assent of shareholders was later employed in the well-known case of *Re Duomatic Ltd* to validate a transaction which would have been valid, but for non-

[15] *Bargate v Shortridge* (1855) 5 HLCas 297 (HL).
[16] See *The Phosphate of Lime Co Ltd v Green* (1871) LR 7 CP 43 at 49.
[17] *Salomon*, above n 1.
[18] At 57.
[19] At 51.

compliance with formalities.[20] This conclusion was reached with reference to two cases. The first was *Re Express Engineering Works Ltd* where it was held a company is bound in a matter intra vires by the unanimous agreement of its members.[21] In reliance on *Re George Newman & Co,*[22] it was submitted in *Express Engineering Works* that individual assents of shareholders given separately are not equivalent to the assent of a meeting. However, this submission was dismissed on two grounds. First, the transaction in *George Newman* was ultra vires and second, the shareholders in *Express Engineering Works* did conduct a meeting, albeit in their capacity as directors.

The second case referred to was *Parker and Cooper Ltd v Reading*,[23] which confirmed the assent of shareholders was able to be given simultaneously or at different times.[24] Astbury J in *Parker* cites no direct authority for departing from the finding in *George Newman* but mentions the suggestion of Warrington LJ in *Express Engineering Works* that shareholders are entitled to waive all formalities to resolve themselves into a meeting. This suggests the shareholders, acting collectively, can waive the requirement of meeting together to pass a resolution.[25] The conclusion of *Parker*, although lacking direct authority, is arguably correct as it is more consistent with the dicta of Lord Davey in *Salomon*. Lord Davey stated there is an "inference from the circumstances" every member of the company gave their assent.[26] This leaves a wide scope for inferring the shareholders' assent, which likely includes the circumstances arising outside a formal meeting.

The *Duomatic* principle was later applied in *Re Horsley & Weight Ltd*.[27] Here, a transaction was completed by two directors without authority from the board. Accordingly, the transaction was invalid unless it had been subsequently ratified. The two directors who approved the transaction were also the only shareholders of the company. Consequently, the Court applied *Salomon*, *Express Engineering Works* and *Parker* to conclude a company is bound in a matter intra vires the company by the unanimous agreement of its members even where that agreement is given informally.[28]

Importantly, the obiter statements by the English Court of Appeal in *Horsley & Weight* suggest a limitation to the *Duomatic* principle. Cumming-Bruce LJ expressed disapproval with the

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[20] *Re Duomatic Ltd*, above n 4.
[21] *Re Express Engineering Works Ltd* [1920] 1 Ch 466 (CA).
[22] *Re George Newman & Co* [1895] 1 Ch 674 (CA).
[23] *Parker & Cooper Ltd v Reading* [1926] 1 Ch 975 (Ch).
[24] But see *Export Brewing & Malting Co v Dominion Bank* [1937] 3 All ER 555 (PC) at [25] where the Privy Council refused to express a view on the correctness of *Parker*. However, the decision in *Parker* has been subsequently followed in *Multinational Gas and Petrochemical Co v Multinational Gas and Petrochemical Services Ltd* [1983] Ch 258 (CA) and *Re Horsley & Weight Ltd* [1982] Ch 442 (CA).
[25] *Westpac Securities Ltd v Kensington* [1994] 2 NZLR 555 (CA) at 565 confirms this position in New Zealand.
[26] At 57.
[27] *Re Horsley & Weight Ltd*, above n 24.
[28] At 454–456.

proposition that the unanimous assent of shareholders could ratify their own negligence which would prejudice the claims of creditors.[29] Furthermore, Templeman LJ proposed the directors, who also hold all the shares of the company, could not excuse themselves of their negligence which inflicted loss on creditors.[30] However, the issue did not directly arise for determination as it was held the directors had not been negligent in this instance.

The English Court of Appeal then applied the *Duomatic* principle in *Multinational Gas and Petrochemical Co v Multinational Gas and Petrochemical Services Ltd*.[31] The majority held the shareholders had unanimously and informally assented to the directors' actions which attributed those actions to the company. As a result, the company lost its right to complain of the directors' acts even if they were negligent. The limitation to the principle mentioned in *Horsley & Weight* was distinguished and the majority held the shareholders acting unanimously may approve a foolish or negligent decision in the ordinary course of business, at least where the company is solvent.[32]

C Development in New Zealand

The principle was first applied in New Zealand by the Court of Appeal in *Nicholson v Permakraft (NZ) Ltd*.[33] During a restructure, the directors paid a capital dividend to themselves as shareholders. The company was put into liquidation two years after this restructure. The liquidator contended the capital dividend should be made available to creditors as the directors breached their duty to the company by not considering its interests or the creditors' interests. The Court of Appeal unanimously held the directors had considered the interests of the company and the company was not threatened by insolvency so the duty to consider the interests of creditors did not arise.

The *Duomatic* principle arose in two instances throughout the judgment. First, the capital dividend was paid in non-compliance with the formalities contained in the company's articles of association and the Companies Act 1955. Nevertheless, it was held the transaction could not be struck down because the unanimous assent of the shareholders to the transaction cured the informality.[34] The application of the principle to cure informalities has since been applied under the operation of the 1993 Act.[35] Second, the Court of Appeal suggested where a payment causes loss to creditors at a time when the directors ought to have known the loss would occur,

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[29] At 455.
[30] At 456.
[31] *Multinational Gas*, above n 24.
[32] At 290–291; see also *Prest v Petrodel Resources Ltd* [2013] UKSC 34, [2013] 2 AC 415 at 491.
[33] *Nicholson v Permakraft (NZ) Ltd* [1985] 1 NZLR 242 (CA).
[34] At 249.
[35] *Levin v Ikiua* [2010] NZCA 509, [2011] 1 NZLR 678; but see *Ririnui (SC)*, above n 6, at [167] where O'Regan J suggests the *Duomatic* principle has not survived the 1993 Act.

this may amount to a misfeasance by the directors.[36] In agreement with Cumming Bruce and Templeman LJJ,[37] the Court of Appeal suggested where a misfeasance of this kind exists, the unanimous assent of shareholders will not excuse the directors of their breach of duty to the creditors.[38] A breach of duty did not arise in this instance and so the Court did not have to determine conclusively whether the shareholders could ratify such a breach.

Nicholson provides some insight into the scope of the principle in New Zealand during the operation of the Companies Act 1955. Under this Act informal unanimous assent only required the unanimous assent of shareholders entitled to vote.[39] It was held this position reflected the statutory context at the time which allowed those entitled to vote to bind a private company without holding a meeting.[40] This statutory provision remains under the 1993 Act.[41]

Perhaps the widest description of the *Duomatic* principle was espoused by the Privy Council in *Meridian Global Funds Management Asia v Securities Commission*, a case appealed from New Zealand. The Privy Council assumed the principle to be a primary rule of attribution.[42] Lord Hoffman stated:[43]

> … the unanimous decision of all the shareholders in a solvent company about anything which the company under its memorandum of association has the power to do shall be the decision of the company.

This passage has been cited as authority for recognising the power of shareholders acting unanimously to make management decisions.[44]

D A Recent Application of the Duomatic Principle

The most recent consideration of the *Duomatic* principle was by the Supreme Court of New Zealand in *Ririnui v Landcorp Farming Ltd*.[45] Landcorp, a state-owned enterprise, proposed to sell a farm property, Whārere. However, Ngāti Whakahemo, a local hapū, asserted they had a claim to Whārere. Landcorp was misinformed by the Office of Treaty Settlements that Ngāti Whakahemo's claim had been settled and Landcorp subsequently completed the sale of

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[36] At 250.
[37] *Re Horsley & Weight Ltd*, above n 24, at 455–456.
[38] At 250 and 255.
[39] *Westpac Securities Ltd v Kensington*, above n 25, at 566–567.
[40] Companies Act 1955, s 362(1).
[41] Section 122.
[42] *Meridian*, above n 2, at 11–12.
[43] At 12.
[44] *Ririnui (CA)*, above n 3, at [53].
[45] *Ririnui (SC)*, above n 6.

Whārere farm. Ngāti Whakahemo sought an order setting aside the agreement for sale and purchase. The relevant contention by Ngāti Whakahemo was that the *Duomatic* principle permitted the shareholding Ministers to intervene in the sale process but they failed to do so. It was contended a failure to intervene would have breached the Crowns obligations under the Treaty of Waitangi, which were given statutory recognition in the State-Owned Enterprise Act 1986.[46] The scope of the *Duomatic* principle was considered in the High Court[47] and Court of Appeal[48] while the Supreme Court briefly addressed whether the principle applies in New Zealand.[49]

In the High Court, Williams J held the *Duomatic* principle empowered the shareholders to intervene in the sale process if allowing the sale to proceed would have breached the Crown's obligations under the Treaty of Waitangi.[50] However, the Court of Appeal disagreed. Ignoring the issue as to whether the *Duomatic* principle has survived the introduction of the 1993 Act, the Court of Appeal recognised the *Duomatic* principle as the legal position in New Zealand.[51] The Court of Appeal stated the question is whether Williams J correctly applied the principle. A distinction was drawn between the *Duomatic* principle and the formulation of the informal unanimous assent principle in *Meridian*,[52] which the Court referred to as the *Meridian* principle. It was held the *Duomatic* principle was a rule of ratification which allowed the shareholders, acting unanimously, to ratify a decision made informally by the company.[53] In contrast, the Court determined the *Meridian* principle attributed a unanimous decision by the shareholders to the company.[54]

1 The correct formulation of the Duomatic principle

With respect, it was incorrect for the Court of Appeal to identify two distinct principles. There is one principle of informal unanimous assent. Lord Davey in *Salomon*, expressed the principle in its simplest terms by stating a "company is bound in a matter intra vires by the unanimous agreement of its members."[55] This reflects the shareholders' ability to alter the allocation of power within the company to bestow upon themselves the authority to bind the company in any matter intra vires the company.[56] The *Duomatic* principle merely allows shareholders to do informally that which they can do formally. This position is consistent with the application of the principle to partnerships, joint stock companies, and the modern company.

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[46] State-Owned Enterprise Act 1986, s 9.
[47] *Ririnui v Landcorp Farming Ltd* [2014] NZHC 1128, [2014] NZCCLR 20.
[48] *Ririnui (CA)*, above n 3.
[49] *Ririnui (SC)*, above n 6, at [155]–[168].
[50] *Ririnui (HC)*, above n 47, at [124]–[136].
[51] *Ririnui (CA)*, above n 3, at [46].
[52] *Meridian*, above n 2, at 12.
[53] At [54].
[54] At [54].
[55] At 57.
[56] Companies Act 1993, s 128(3).

In the context of partnerships, it was held the deed governing the partnership is subject to the informal unanimous assent of the partners.[57] Accordingly, the partners may unanimously agree to any intra vires conduct. In the context of joint stock companies, the unanimous agreement of shareholders was held to alter the deed of settlement governing the company.[58] Similarly, this illustrates the ability of shareholders to unanimously agree to any intra vires conduct. In the context of the modern company, Buckley J held the unanimous assent of shareholders to a matter which a general meeting of the company could carry into effect is as binding as a resolution in general meeting.[59] Shareholders in general meeting may agree to vary the constitution, the company's governing document.[60] Accordingly, the shareholders are able to unanimously agree to any matter intra vires the company by informally and unanimously agreeing to vary the constitution to give themselves the relevant management power. Employing the *Duomatic* principle to ratify decisions is therefore an example of the principle being applied, but it is not the full reach of the principle. This is consistent with the application of the *Duomatic* principle in New Zealand where it has been held informalities may be cured by the unanimous assent of the shareholders.[61] This is the position the Court of Appeal should have arrived at before addressing whether the 1993 Act contemplates such informality.

2 The ultra vires doctrine and the Duomatic principle

The Court of Appeal later found neither the *Duomatic* principle nor the *Meridian* principle empowers shareholders to intervene in the sale process.[62] The Court held both conceptions are always subject to the limitation that the relevant act is one which the company is lawfully able to perform.[63] More accurately, either conception is subject to the limitation that the relevant act is one which is not ultra vires.[64] Ngāti Whakahemo's contention that the shareholders had the power to intervene failed because intervention would have caused Landcorp to act in breach of its legal obligations.[65] It was held Landcorp had no constitutional power to act in breach of its obligations to third parties.[66] Consequently, the act would have been ultra vires the company and there was no scope for shareholders to intervene by informal unanimous assent.

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[57] *Const v Harris*, above n 8, at 523.
[58] *Morgan's Case*, above n 10, at 776.
[59] *Re Duomatic Ltd*, above n 4, at 373.
[60] Companies Act 1993, s 32(2).
[61] *Levin v Ikiua*, above n 35, at [46]; *Westpac Securities Ltd v Kensington*, above n 25, at 564–567; *Wairau Energy Centre Ltd v First Fishing Co Ltd* (1991) 5 NZCLC 67,379 (CA) at 67,383; and *Nicholson v Permakraft*, above n 33, at 249.
[62] *Ririnui (CA)*, above n 3, at [52].
[63] At [54].
[64] Harrison J in *Ririnui (CA)* cited *The Attorney-General for the Dominion of Canada v The Standard Trust Co of New York* [1911] AC 498 (PC) at 504 which provides the unanimous assent principle does not apply where the act is ultra vires in the sense of being outside the legal capacity of the company.
[65] *Ririnui (CA)*, above n 3, at [54].
[66] At [54].

This reasoning of the Court of Appeal is doubtful. It has been suggested a company does have the power to act in breach of its obligations to third parties.[67] The 1993 Act states a company has full capacity, rights, powers and privileges to enter into any transaction, do any act, or carry on or undertake any business or activity.[68] A company may limit these broad powers in its constitution.[69] It follows, a company carrying out an illegal act is not acting beyond its capacity or ultra vires.[70] Accordingly, it would not be ultra vires for a company to act in breach of its contractual obligations as a company has the same power to breach a contract as a natural person. Whether it would, or should, is a separate question.

Lord Davey in *Salomon*, limited the *Duomatic* principle by stating the company is only bound in a matter intra vires.[71] This limitation was espoused at a time where an act was only intra vires the company if it was within the powers and objects set out in its memorandum of association.[72] If an act fell outside these powers and objects it was ultra vires and void.[73] Lord Davey was correct to also prohibit shareholders acting unanimously to enter an ultra vires transaction as the shareholders had no power to alter the powers and objects without prior confirmation by the Court.[74]

The 1993 Act, however, contravenes the doctrine of ultra vires. Section 17(1) provides no act of a company will be invalid merely because the company lacked the capacity to do the act. The company and the shareholders will have recourse against the directors acting beyond their capacity, but the transaction will remain valid.[75] If the directors are able to enter into a valid transaction beyond their capacity, there is no reason why the shareholders, acting unanimously, cannot also act outside their capacity to bind the company. Recourse against the shareholders for this act will be available.[76] However, it will likely be open to the shareholders to amend the constitution so the act falls within their capacity.

Indeed, s 129 also suggests the ultra vires doctrine is no longer applicable.[77] The doctrine of ultra vires acted to protect shareholders from investing in one type of business only to discover the directors had sold the business assets and invested in a completely different type of

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[67] Peter Watts "The power of a special majority of shareholders, or of all shareholders acting informally, to override directors – *Attorney-General v Ririnui*" [2015] CSLB 89 at 90.
[68] Section 16(1).
[69] Section 16(2).
[70] John Farrar and Susan Watson (eds) *Company and Securities Law in New Zealand* (2nd ed, Thomson Reuters, Wellington, 2013) at 118.
[71] At 57.
[72] Farrar and Watson, above n 70, at 113.
[73] Farrar and Watson, above n 70, at 114.
[74] Companies Act 1955, s 18.
[75] Section 17(2).
[76] Section 17(2).
[77] Companies Act 1993, s 129.

business.[78] Section 129 now provides this protection by ensuring any major transaction is given shareholder approval before completion.[79] This conclusion suggests the limitation to the principle, as stated by Lord Davey, is now redundant. Respectfully, Harrison J was therefore wrong to refrain from applying the *Duomatic* principle on the basis the shareholders would be acting ultra vires.

3 The correct conclusion to Attorney-General v Ririnui

Although the reasoning of the Court of Appeal is arguably flawed, the final result in relation to the shareholding Minister's power to intervene was correct. It has been suggested the short answer to the issue in *Ririnui* was that property rights acquired by a third party in good faith, before the shareholders were requested to cause Landcorp to breach its contract, could not be taken away.[80] This conclusion is drawn because the holder of a specifically performable contract has superior rights, not because there is a limitation on the scope of the *Duomatic* principle.[81] Furthermore, if the shareholders were found to have had the power to intervene, their decision not to give the undertaking sought by Ngāti Whakahemo may not have breached the Crown's obligations under the Treaty of Waitangi.[82] The title to Whārere farm was subject to the memorial regime in the State-Owned Enterprise Act 1986.[83] This memorial regime provided a means for the land to be resumed by the Crown on the recommendation of the Waitangi Tribunal.[84] Consequently, the Court of Appeal noted there was no evidence the Ministers decision not to intervene would materially impair the Crown's ability to provide appropriate redress.[85] This issue, however, was not determined conclusively as no such power to intervene was identified.

E The Scope of the Duomatic Principle

To reiterate, the scope of the *Duomatic* principle was identified in *Salomon* and has remained constant in its application in New Zealand. The *Duomatic* principle permits shareholders to unanimously and informally assent to any matter which they may agree to at a meeting of

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[78] David Goddard "Company Law Reform: Lessons from the New Zealand Experience" (1998) 16 C&SLJ 236 at 243.
[79] Section 129(1).
[80] Watts, above n 67, at 90.
[81] Peter Watts, Neil Campbell and Christopher Hare *Company Law in New Zealand* (2nd ed, LexisNexis NZ, Wellington, 2016) at 244.
[82] See *Ririnui (CA)*, above n 3, at [60].
[83] Sections 27–27D.
[84] Section 27B.
[85] At [60]; but see *Ririnui (SC)*, above n 6, at [91] where it was suggested the best opportunity for Ngāti Whakahemo to acquire Whārere was through a commercial purchase. This suggests the decision not to intervene may have materially impaired the Crown's ability to provide redress as indicated in *New Zealand Maori Council v Attorney-General* [2013] NZSC 6, [2013] 3 NZLR 31 at [89].

shareholders.[86] The constitution of a company may, therefore, be varied by the shareholders acting unanimously and informally to allocate themselves management powers. This is arguably what was contemplated by the Privy Council in *Meridian*. Furthermore, the ultra vires doctrine has limited scope in New Zealand and may no longer act as a limitation to the *Duomatic* principle.

Highlighting the scope of the *Duomatic* principle may assist in assessing whether the principle has survived the introduction of the 1993 Act. Such an inquiry was briefly addressed by the Supreme Court in *Ririnui*, which doubted the continued application of the *Duomatic* principle.[87]

[86] This paper will not attempt to outline the limits of shareholder assent; see Watts, Campbell and Hare, above n 81, at 245 for an authoritative review of this developing area.
[87] *Ririnui (SC)*, above n 6, at [166]–[167].

Chapter II: The Duomatic Principle and the Companies Act 1993

The *Duomatic* principle has been confused with a principle empowering the shareholders to exercise management powers. It is first necessary to assess whether the *Duomatic* principle encapsulates the shareholders' overriding reserve power to manage the company. Irrespective of this inquiry, the management powers are expressly allocated to the board by the 1993 Act but are subject to the constitution. It is necessary to assess whether the shareholders are competent to alter the constitution by informal unanimous assent and whether the 1993 Act permits such informality. This inquiry will identify the current position of the *Duomatic* principle in New Zealand.

A Reserve Powers of Shareholders

It has been suggested the *Duomatic* principle originated at a time where the powers of the company were vested in the general meeting of shareholders.[88] The shareholders were the company and it existed for the benefit of shareholders. It was accepted the general meeting could exercise the powers of the company and, as the board acted as a mere agent, powers of management delegated to the board were subject to the overriding authority of the general meeting. It was ultimately argued the *Duomatic* principle was consistent with this formulation as the shareholders had an original power to manage.

Indeed, the legal environment and the jurisprudence at the time the *Duomatic* principle was applied to joint stock companies supported this conclusion. The Companies Clauses Consolidation Act 1845 (UK) delegated the powers to manage the company to the directors but also provided these powers were subject to the control of the general meeting.[89] It was therefore appropriate for Cotton LJ, in *Isle of Wight Railway Co v Tahourdin*, to hold that a meeting of the shareholders had the power to direct and control the board in the management and affairs of the company.[90] This conception of shareholder control, however, was subsequently eroded by the model articles of association provided by the various Companies Acts.[91]

In New Zealand, a company operating under the Companies Act 1955, the predecessor to the 1993 Act, could choose to adopt articles of association which provided the regulations of the company.[92] If a company did not voluntarily register articles of association the regulations

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[88] Grantham, above n 5, at 270.
[89] Companies Clauses Consolidation Act 1845 (UK), s 90.
[90] *Isle of Wight Railway Co v Tahourdin* (1883) 25 ChD 320 (CA) at 331–332.
[91] John Farrar Corporate Governance: *Theories, Principles, and Practice* (2nd ed, Oxford University Press, Oxford, 2005) at 70.
[92] Companies Act 1955, s 20.

contained in Table A would apply as the default articles.[93] Table A provided that the business of a company shall be managed by the directors.[94] It was also provided the shareholders may alter the articles of association by special resolution.[95] The wording of Table A more clearly delegated the management power to the board when compared with the standpoint in the Companies Clauses Consolidation Act 1845.[96]

Some have contended the general meeting of shareholders has retained a residual power to usurp the management power of the board.[97] However, the judiciary noted no matter what the position may have been under the former agency relationship between shareholders and directors, when the articles of association vest the management powers of a company in the directors, a majority in general meeting is powerless to override the decisions of the board.[98]

In *Automatic Self-Cleansing Filter Syndicate Co Ltd v Cuninghame*, a majority of shareholders resolved that the directors were to give effect to the sale of company assets.[99] The directors declined to complete the sale as it was, in their opinion, not in the best interests of the company. The shareholders contended the directors were bound to give effect to the resolution as the directors were the agents of the company and should be bound to obey the directions of the company in general meeting as their principal. In dismissing this argument, Warrington J, at first instance, stated:[100]

> It seems to me on the true construction of these articles that the management of the business and control of the company are vested in the directors, and consequently that the control of the company as to any particular matter, or management of any particular transaction or any particular part of the business of the company, can only be removed from the board by an alteration of the articles, such alteration, of course, requiring a special resolution.

The Court Appeal agreed with Warrington J and held a majority of the shareholders cannot affect or alter the mandate originally given to the directors by the articles.[101] This highlights the directors' original authority to manage the affairs of the company.[102] This conclusion was

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[93] Companies Act 1955, s 22(2); this position is similar under the current regime as s 28 of the Companies Act 1993 provides the company, the board, each director and each shareholder of the company have the rights, powers, duties, and obligations set out in this Act in the absence of a constitution.
[94] Companies Act 1955, sch 3, Table A, art 80.
[95] Companies Act 1955, s 24.
[96] Farrar, above n 91, at 70.
[97] See *Massey v Wales* (2003) 57 NSWLR 718 (CA*)* at [36].
[98] *Automatic Self-Cleansing Filter Syndicate Co Ltd v Cuninghame* [1906] 2 Ch 34 (CA).
[99] *Automatic Self-Cleansing*, above n 98.
[100] At 38–39.
[101] At 42.
[102] See also *John Shaw & Sons (Salford) Ltd v Shaw* [1935] 2 KB 113 (CA) at 464 which is often cited for recognising the distinct and original power of directors to manage the company.

reinforced in the subsequent case of *Bamford v Bamford* where Plowman J stated *Automatic Self-Cleansing*, and the cases that follow, illustrate:[103]

> … a company cannot by ordinary resolution dictate to or overrule the directors in respect of matters entrusted to them by the articles. To do that it is necessary to have a special resolution.

The New Zealand Court of Appeal also recognised this position in the context of the Companies Act 1955. North P in *Black White & Grey Cabs Ltd v Fox*, concluded the articles of association vest the management of the company in the directors and accordingly the directors alone have the necessary power to manage the affairs of the company in the absence of a special resolution altering the articles.[104] In this instance, the provision relevant to the management of the company was expressed in the precise language of the management provision in Table A.[105] It has been suggested the articles relating to management under the former Companies Acts are equivalent to the current management provision in the 1993 Act.[106] Consequently, the authorities on the interpretation of the management provision under the former Companies Acts are relevant to the interpretation of the current provision.[107]

The directors therefore have an original power to manage under the 1993 Act as a result of the jurisprudence relating to the current management provisions. The 1993 Act has also expressly provided for the conclusion of *Automatic Self-Cleansing*.[108] Section 109 empowers a meeting of shareholders to pass a resolution relating to the management of the company.[109] However, unless the constitution provides otherwise, such a resolution is not binding upon the board.[110] Indeed, this was the intention of the Law Commission in drafting the 1993 Act where its report stated there is no residual power of management decision making remaining with the general meeting.[111] This confirms, a majority of shareholders cannot direct the board in its exercise of management powers allocated to it by the company's constitution. The *Duomatic* principle does not reinstate the management power of the majority. It merely allows shareholders to exercise their existing powers informally. Assessment of the shareholders' existing powers is therefore necessary.

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[103] *Bamford v Bamford* [1970] Ch 212 (CA) at 220.
[104] *Black White & Grey Cabs Ltd v Fox* [1969] NZLR 824 (CA) at 832.
[105] At 830.
[106] Watts, Campbell and Hare, above n 81, at 232.
[107] See Watts, Campbell and Hare, above n 81, at 232; see also Watts, above n 67, at 89 where it was recognised *Automatic Self-Cleansing*, above n 98, is the leading case on the wording that is contained in s 128 of the Companies Act 1993.
[108] Companies Act 1993, s 109.
[109] Section 109(2).
[110] Section 109(3).
[111] Law Commission *Company Law: Reform and Restatement* (NZLC R9, 1989) at 41.

B Allocation of Management Powers by the Companies Act 1993

1 The default rule

Section 128 provides the starting point in relation to company management for all companies who have chosen not to adopt a constitution altering the default provision.[112] It is helpful to set the provision out in full:[113]

> **128 Management of Company**
>
> (1) The business and affairs of a company must be managed by, or under the direction or supervision of, the board of the company.
>
> (2) The board of a company has all the powers necessary for managing, and for directing and supervising the management of, the business and affairs of the company.
>
> (3) Subsections (1) and (2) are subject to any modifications, exceptions, or limitations contained in this Act or in the company's constitution.

Section 128(1) acts as a default rule which confers a prima facie power on the board to manage a company's business and affairs.[114] This default rule is justified by commercial practicalities. First, Hodgson JA in *Massey v Wales*, suggested the management of a company should be conducted by a body of persons who each have a fiduciary duty to act in the best interests of the company as a whole, rather than a body of persons where the majority is free to favour its own interests over the interests of the minority.[115] Second, the default rule protects the interests of minority shareholders. A minority shareholder may wish to have greater control over the affairs of the company, which they may acquire through an entitlement to appoint directors to the board.[116] Third, from the perspective of the directors the default rule will ensure the directors decision making will remain largely unquestioned by the majority of shareholders.[117] Forth, a small group of decision makers will facilitate dealings with third parties as it is clear who has authority to bind the company.[118]

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[112] Companies Act 1993, s 128.
[113] Companies Act 1993, s 128.
[114] See Watts, Campbell and Hare, above n 81, at 230 for a discussion on what is included within a company's business and affairs.
[115] *Massey v Wales*, above n 97, at [46].
[116] Watts, Campbell and Hare, above n 81, at 236.
[117] Watts, Campbell and Hare, above n 81, at 236.
[118] Watts, Campbell and Hare, above n 81, at 236.

2 *Rebutting the default rule*

Although this default rule may be justified, it is subject to rebuttal. Section 128(1) confers only a prima facie power as s 128(3) states this power is subject to any modifications, exceptions, or limitations contained in the 1993 Act or the company's constitution. There is a broad scope of matters that may be included in the constitution of a company.[119] The shareholders may therefore allocate the management powers of the company to themselves. However, the words "modifications, exceptions, or limitations" contained in s 128(3) may prohibit the shareholders from removing all management powers from directors as this would involve more than a modification, exception or limitation. Nevertheless, there is nothing to prohibit the shareholders from effecting an ad hoc business transaction by amending the constitution.[120] The result of s 128 as a whole is the management of the company and powers of management are allocated to the board of the company, but the shareholders may alter the constitution to reallocate management powers by special resolution.

This is consistent with the common law position under the former Companies Acts. It is true the common law position stated the directors had an original power to manage the company, but, this has always been subject to an alteration of the articles by the shareholders.[121] This restatement and confirmation of the shareholders' ability to alter the constitution illustrates the view of shareholder primacy within the context of modern company law.[122]

The *Duomatic* principle, therefore, does not empower the shareholders to exercise management powers. Shareholders have statutory authority to do so. As noted above, the *Duomatic* principle allows the shareholders, when acting informally and unanimously, to agree to any matter which they may agree to at a meeting of shareholders. Accordingly, it may be possible for the shareholders to informally and unanimously agree to alter the constitution of the company to reallocate management powers to themselves. Such alteration, if permissible, will engage s 128(3) and subject the directors' management powers under s 128(1) to the alteration. However, an assessment of whether the 1993 Act permits such informality is required.

[119] Companies Act 1993, s 30(b).
[120] Watts, above n 67, at 89.
[121] See *Automatic Self-Cleansing*, above n 98, at 42; and *Black White & Grey Cabs Ltd*, above n 104, at 832.
[122] See Watts, Campbell and Hare, above n 81, at 230–235 for a review of shareholder primacy in the context of modern company law.

C Shareholders' Ability to Informally Alter the Constitution

Ignoring the application of the principle to ratify director's conduct,[123] the 1993 Act does not expressly provide for the *Duomatic* principle nor does it expressly exclude it.[124] Nevertheless, the judiciary has frequently concluded specific statutory requirements are intended to be silently subject to the *Duomatic* principle.[125]

1 Shareholders' ability to informally and unanimously pass a special resolution

In *Re Oxted Motor Co Ltd*, Lush and Greer JJ both held the shareholders had validly passed a special resolution despite non-compliance with the formalities required by the governing statute.[126] The only two shareholders of the company sought to voluntarily wind up the company by special resolution pursuant to the governing statute.[127] Among other things, a valid special resolution required notice to be given prior to a general meeting where the special resolution was to be proposed.[128] The shareholders, however, had passed a special resolution in disregard of the notice requirement. Lush J referred to *Express Engineering Works* and acknowledged that case concerned the waiver of notice regarding an ordinary resolution and not a special resolution.[129] It was agreed, however, a statutorily required formality intended for the benefit of shareholders is capable of being waived by the shareholders.[130] Lush J concluded, although the statute provided express requirements regarding notice, the shareholders could waive this formality as if the resolution were an ordinary resolution.[131] Accordingly, the resolution was valid.[132]

This case may fall short of being authority for the proposition that shareholders may waive all formalities relating to a special resolution. In *Oxted Motor* the two shareholders were held to have waived the requirement of notice but nothing was said about whether the requirement to meet in person or by proxy could be waived.[133] It may be contended the requirement for notice is purely procedural and is therefore different to other formalities. However, the judgment of Greer J in *Oxted Motor* provides some guidance on this issue. It was suggested where a

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[123] Companies Act 1993, s 177(4) provides "Nothing in this section limits or affects any rule of law relating to the ratification or approval by the shareholders or any other person of any act or omission of a director or the board of the company".
[124] Watts, Campbell and Hare, above n 81, at 249.
[125] See Andrew Burton "Dispensing with formalities: the *Duomatic* principle" (2000) 21 Company Lawyer 186 at 186–188.
[126] *Re Oxted Motor Co Ltd* [1921] 3 KB 32 (KB) at 38.
[127] Companies (Consolidation) Act 1908 (UK), s 182.
[128] Companies (Consolidation) Act 1908 (UK), s 69(1).
[129] At 37.
[130] At 38.
[131] At 38.
[132] At 38.
[133] Companies (Consolidation) Act 1908 (UK), s 69(1) also required the resolution to be passed by a majority of at least three-fourths of members entitled to vote as are present in person or by proxy at a general meeting.

formality concerns only the shareholders, such as the present case where the Legislature had given the shareholders the right to voluntarily wind up the company, the shareholders may unanimously waive it.[134] In the context of s 128(3), the Legislature has given the shareholders authority to amend the constitution of the company by special resolution to reallocate the management powers of the board contained in s 128(1). This matter may concern the shareholders alone. Consequently, *Oxted Motor* may justify the shareholders waiving all formal requirements of a special resolution to amend the constitution by informal unanimous assent.

In *Cane v Jones* the requirement for a special resolution was later held to be subject to the *Duomatic* principle.[135] In this instance, the articles of association provided for the chairman of the board to have a casting vote. Later, the shareholders informally and unanimously agreed the chairman no longer had this power. The company subsequently entered a state of deadlock in relation to the management of the company's affairs and the chairman's right to exercise a casting vote was sought to be enforced.

It was contended the agreement was not effective to alter the company's articles as the governing statute stated the articles could only be altered by a special resolution requiring a resolution and a meeting.[136] The shareholders did not meet or pass a resolution which differentiated the situation from that in *Oxted Motor* where the shareholders did meet and pass a resolution but failed to comply with the notice requirement.[137] Nevertheless, it was held distinguishing between the notice requirements and the requirements for meeting and passing a resolution would create a wholly artificial and unnecessary distinction between those powers which can, and those which cannot, be validly exercised by the shareholders acting unanimously.[138] This suggests the extent to which the formalities are ignored is irrelevant.

It was ultimately held the statutory process for altering the articles by special resolution is merely setting out a process for some, but not all, of the shareholders to alter the articles by special resolution.[139] There is nothing in the provision allowing alteration of the articles by special resolution to undermine the *Duomatic* principle.[140] The Court noted the essence of meeting and passing a resolution is to represent a meeting of the minds.[141] Consequently, the shareholders were able to give their assent to the agreement simultaneously or at different times.[142]

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[134] At 39.
[135] *Cane v Jones* [1981] 1 All ER 533 (Ch).
[136] At 538.
[137] At 538–539.
[138] At 539.
[139] At 539.
[140] At 539.
[141] At 539–540; see also *Ho Tung v Man On Insurance Co Ltd* [1902] AC 232 (PC) at 236.
[142] At 539–540.

These two cases represent two different ways in which the *Duomatic* principle has been employed in relation to the exercise of powers requiring a special resolution. *Oxted Motor* suggests the formalities of a special resolution are for the benefit of shareholders which are therefore able to be waived by the shareholders acting unanimously. *Cane* acknowledged that all the formalities of a special resolution may be waived as there is no meaningful distinction between the requirements of notice, meeting together and the passing of a resolution. Arguably, these are for the sole benefit of shareholders. However, *Cane* concluded although the Legislature has specifically provided for the power to be exercised by way of special resolution, this is not the only way the power can be exercised as the shareholders may, informally and unanimously, agree to exercise the power.[143]

2 A limitation to the shareholders' ability to act informally and unanimously

In *Re RW Peak (Kings Lynn) Ltd*, the *Duomatic* principle was held not to apply where the statutory formalities relating to the company's purchase of its own shares had not been complied with.[144] Particular provisions of the governing statute led Lindsay J to conclude it would be anomalous to override the statutory formalities.[145] The provision outlining the procedure by which unanimous written resolutions may be passed was highlighted.[146] It was held even if this process was followed, which was more formal than the assent in question, it was not possible to comply with the required formalities.[147] This assessment was arguably incorrect as it referred to other formalities required by the statute which may have also been waived by the shareholders.[148] Nevertheless, the outcome was likely appropriate as the formalities sought to be waived by informal unanimous assent were not for the sole benefit of shareholders.[149] An arrangement whereby a company purchases its own shares has the effect of lowering the share capital available to creditors should insolvency ensue. Accordingly, the shareholders did not have the ability to waive the statutory formalities protecting creditors.[150]

This outcome was later addressed in *Wright v Atlas Wright (Europe) Ltd*.[151] Potter LJ interpreted the judgment of *RW Peak* to constrain the application of the *Duomatic* principle so that it may not render effective what would have been ineffective if the formal procedure had been followed.[152] This conclusion is consistent with the dicta of Buckley J stating the

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[143] At 539.
[144] *Re RW Peak (Kings Lynn) Ltd* [1998] 1 BCLC 193 (Ch).
[145] At 201.
[146] Companies Act 1985, s 381A.
[147] At 202.
[148] See Companies Act 1985 (UK), s 164(2) which requires the appropriate resolution to be passed before entry into the relevant contract.
[149] As noted at 205.
[150] At 205.
[151] *Wright v Atlas Wright (Europe) Ltd* [1999] 2 BCLC 301 (CA).
[152] At 314.

unanimous assent of all shareholders to a matter which the general meeting could carry into effect is as binding as a resolution in general meeting.[153] Indeed, if the shareholders in general meeting had no power to agree on a matter, informal and unanimous assent would not clothe the shareholders with the necessary power.

Lord Justice Potter then suggested it is necessary to consider the purpose and underlying rationale of the formalities in determining whether they may be overlooked and curable by assent.[154] This led Potter LJ to conclude the underlying purpose of the provision in question was to benefit and protect the shareholders.[155] Consequently, it was held the relevant provision was amenable to the *Duomatic* principle and the statutory formalities could be waived by the shareholders acting unanimously.[156] These cases confirm shareholders may not waive a formality intended to protect a party other than shareholders and the *Duomatic* principle only permits shareholders to do informally that which they may do formally.

3 Employing the Duomatic principle to amend or adopt a constitution

The Supreme Court of Victoria has confirmed that the unanimous assent of shareholders may amend the constitution even where the statutory formalities have not been complied with.[157] In *Re Rectron Electronics Pty Ltd*, a shareholders' agreement, agreed by all shareholders, restricted the number of directors to be appointed. However, the constitution was not formally amended to reflect this. It was accepted the regime brought about by the shareholders' agreement could have been implemented by the shareholders in general meeting by amending the constitution.[158] *Duomatic* was cited to suggest, where it could be shown all the shareholders had assented to a matter that could have been carried into effect at a general meeting, that assent is as binding as a resolution in general meeting.[159] It was concluded the shareholders' agreement was evidence of unanimous assent by the shareholders to amend the constitution to implement the regime contained in the shareholders' agreement.[160] This is particularly important as the *Duomatic* principle may provide a basis for the constitution to be subordinate to a shareholders' agreement. Nevertheless, the conclusion permits the shareholders to disregard the statutory formalities required in amending the constitution to achieve a substantive outcome.

In addition to altering the constitution, as seen in *Cane* and *Rectron Electronics*, the shareholders have been found to have the power to informally and unanimously adopt a

[153] *Re Duomatic Ltd*, above n 4, at 373.
[154] At 315.
[155] At 315.
[156] At 315.
[157] *Re Rectron Electronics Pty Ltd* [2013] VSC 384.
[158] At [69].
[159] At [68].
[160] At [69].

constitution contrary to express statutory provisions. In *Ho Tung v Man On Insurance Co Ltd* the company's articles of association were required to be adopted by a special resolution.[161] However, the articles had not been signed nor formally adopted by the shareholders. Despite this, it was suggested the requirement of a special resolution was simply machinery for securing the assent of the shareholders and did not preclude assent to the articles being inferred by the unanimous assent of shareholders.[162] The assent in this case was inferred from acquiescence and agreement to the articles by the shareholders over nineteen years. This case may require the factors leading to a valid inference to be relatively clear, but the decision remains important as it recognises the articles of association are in the control of the shareholders and the formalities required in adopting or amending the articles are for the benefit of shareholders.[163] Accordingly, shareholders are competent to unanimously waive the formalities relating to the amendment or adoption of a constitution.

(a) Disregarding the Companies Act 1993 formalities to amend or adopt a constitution

It is evident the judiciary has employed the *Duomatic* principle to empower the shareholders to act in disregard of formalities required by statute. This has become constrained to instances where the formality is for the benefit of shareholders alone.[164] Importantly, the shareholders have been able to unanimously adopt and amend the constitution in disregard of formalities.[165] The 1993 Act permits the shareholders to adopt or amend the constitution by special resolution.[166] In addition to those cases dealing with the constitution, it has been confirmed the shareholders may ignore the formalities relating to a special resolution when acting unanimously.[167] This may only be true when the formalities are for the sole benefit of shareholders,[168] but it is suggested the formalities of the 1993 Act relating to adopting and amending a constitution are for the sole benefit of shareholders.[169]

Section 32 gives shareholders the sole power to adopt or amend a constitution.[170] If the section were to cease there, it would be elementary to say the formalities relating to the adoption or amendment of a constitution are for the benefit of shareholders alone. The provision continues, however, to impose an obligation on the board to provide notice of the adoption or alteration to the Registrar for registration.[171] It may be contended this formality is for the benefit of a group other than the shareholders which would preclude the operation of the *Duomatic*

[161] *Ho Tung v Man on Insurance Co Ltd*, above n 141.
[162] At 236.
[163] At 236.
[164] See *Wright v Atlas Wright (Europe) Ltd*, above n 151; and *Re RW Peak (Kings Lynn) Ltd*, above n 144.
[165] See *Cane v Jones*, above n 135.
[166] Section 32.
[167] See *Re Oxted Motor Co Ltd*, above n 126.
[168] *Re RW Peak (Kings Lynn) Ltd*, above n 144, at 205.
[169] As was seen in *Ho Tung v Man on Insurance Co Ltd*, above n 141.
[170] Companies Act 1993, ss 32(1)–32(2).
[171] Companies Act 1993, s 32(3).

principle. The constitution of a company is registered on the New Zealand Companies Register and is therefore a public document. It is open to potential creditors to inspect prior to becoming a creditor. Accordingly, the formal requirement of notice of adoption or alteration may be for the benefit of those other than the current shareholders. Following the dicta of Potter LJ, the shareholders acting unanimously would be unable to waive this formal requirement.[172]

However, the shareholders may be competent to waive the formal requirements of a special resolution to adopt or amend a constitution. As was suggested in *Ho Tung*, a special resolution is merely machinery for securing the assent of the shareholders.[173] This suggests the requirement of a special resolution is for the benefit of shareholders, specifically minority shareholders. If it is possible for the shareholders to unanimously waive the requirement for a special resolution to informally and unanimously exercise the power to adopt or amend a constitution, the formal requirement of notice may still be complied with. First, the provision imposes the obligation to give notice on the board and second, the board must provide the appropriate notice within 10 working days from the adoption or alteration of the constitution.[174] If the shareholders were to informally and unanimously adopt or alter the constitution, the board may satisfy its notice obligations in the same way it may have satisfied its obligations if a formal resolution was passed.

Leaving aside the question as to whether the common law restrictions on the alteration of the constitution by the shareholders survives the 1993 Act,[175] it may be possible for the shareholders to amend the constitution pursuant to s 32 by informal unanimous assent to reallocate the management powers of the board to themselves as contemplated by s 128(3). Although the formal requirements of a special resolution required by s 32 are for the benefit of the shareholders and subject to waiver by unanimous assent, the 1993 Act as a whole should be assessed to determine whether such informality is permitted.

D Consistency with the Companies Act 1993

In *Ririnui*, the Supreme Court found it was not reasonably possible for the shareholding Ministers to intervene in the transaction.[176] Accordingly, the Supreme Court refrained from expressing a concluded view on whether the *Duomatic* principle survives the 1993 Act.[177] Nevertheless, after hearing full argument, O'Regan J helpfully expressed a view on this important issue. Justice O'Regan mentioned the principle does not apply to a state-owned

[172] *Wright v Atlas Wright (Europe) Ltd*, above n 151, at 315.
[173] *Ho Tung v Man on Insurance Co Ltd*, above n 141, at 236.
[174] Companies Act 1993, s 32(3).
[175] See Watts, Campbell and Hare, above n 81, at 125–126 for a description of the common law restrictions and an opinion as to whether they have survived the introduction of the 1993 Act.
[176] *Ririnui (SC)*, above n 6, at [78]–[81] and [155].
[177] At [78]–[81] and [155].

enterprise because it would not be consistent with the scheme of the State-Owned Enterprise Act 1986.[178] Justice O'Regan continued to suggest the principle no longer applies to private companies.[179] Although no concluded view on this point was reached, three factors were referred to in support of this view.[180]

First, O'Regan J interpreted the Law Commission's reports preceding the 1993 Act as indicating a rejection of the *Duomatic* principle. Second, it was suggested the *Duomatic* principle is now limited to the specific actions requiring the unanimous assent of shareholders as stipulated in s 107. Third, the allocation of management powers to the board by s 128 was seen to suggest, subject to the constitution, any assent by shareholders to an action within the power of the board would not be effective. The extent to which these factors may be relied upon in determining whether the *Duomatic* principle survives the 1993 Act requires assessment. Furthermore, additional provisions of the 1993 Act, not referred to by O'Regan J, may also denote the current position of the *Duomatic* principle.

1 Law Commission reports

The Law Commission considered whether shareholders, acting by unanimous resolution, should be able to exercise any powers of the company.[181] It was concluded an explicit power permitting shareholders to act in this manner is generally undesirable as it would cut across the allocation of power in the Act.[182] Furthermore, it was suggested the system for protecting creditors by imposing duties on directors could be undermined if shareholders could exercise the directors' powers.[183]

Indeed, if the Companies Act contained an express provision permitting shareholders to exercise any powers of a company by unanimous assent, the shareholders would be acting within their capacity as shareholders when acting in accordance with that provision. Consequently, the shareholders would not fall within the meaning of a director pursuant to s 126 and would not attract the directors' duties, thus leaving creditors vulnerable to the unanimous acts of shareholders acting under the express provision. It would be more appropriate to leave the operation of the *Duomatic* principle to common law and deem the shareholders to be acting as directors when they exercise management powers reallocated to them by the constitution. Section 126(2) imposes such duties. Alternatively, an express provision may be included which states shareholders exercising a power under an express provision are deemed to be directors and therefore subject to directors' duties.

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[178] At [166].
[179] At [167].
[180] At [167].
[181] Law Commission, above n 111, at 41.
[182] Law Commission, above n 111, at 41.
[183] Law Commission, above n 111, at 41.

The Law Commission later noted that a greater role for the general meeting in the management of a company requires a greater need to develop a concept of fiduciary duty owed by the majority to the minority.[184] A broad fiduciary duty imposed on shareholders could undermine the concept of a share as personal property, entitling the holder to exercise the rights attaching to the share as they wish.[185] This may be accurate, but the Law Commission was incorrect to apply this reasoning to the *Duomatic* principle. If the majority of shareholders were allocated management powers this issue would be important. However as illustrated, the majority have no reserve power to manage therefore no statutory provision should reinstate this power. In the context of the *Duomatic* principle, a fundamental requirement is unanimity.[186] Where the shareholders are unanimous, a minority does not exist and therefore cannot be prejudiced. Accordingly, a fiduciary duty owed by shareholders to other shareholders would not be engaged. Shareholders should, however, owe a duty to the company and to creditors, but this will be imposed by the provisions containing the directors' duties.

The Law Commission then suggested that assessing the good faith of a board is quite different to assessing the good faith of a majority of shareholders, perhaps running into the hundreds.[187] This suggestion implies it would be too difficult to assess the good faith of shareholders in relation to a breach of duty because there are generally many more individual shareholders than directors. Accordingly, the Law Commission appears to suggest the shareholders should not be given management powers because assessing compliance with their duties would be difficult. With respect, this argument is fallacious as the 1993 Act requires a minimum of one director and has no maximum restriction.[188] Consequently, a company may have many more directors than shareholders. The 1993 Act, nevertheless, still imposes duties on a company's directors no matter how many comprise their cohort. This factor mentioned by the Law Commission should, therefore, not preclude the shareholders from acquiring management powers and the associated duties.

Although the Law Commission expressed disapproval of an explicit provision empowering the shareholders acting unanimously to exercise the powers of the company, it was later stated "where unanimous shareholder resolution is effective as a waiver of rights, it will be available as a matter of general law. Express provision for it is unnecessary."[189] No explanation of what rights may be waived by unanimous shareholder assent was provided. The Law Commission may have contemplated the line of authority recognising the shareholders' power to waive

[184] Law Commission, above n 111, at 50–51.
[185] Law Commission, above n 111, at 50–51.
[186] *Re Duomatic Ltd*, above n 4, at 373.
[187] Law Commission, above n 111, at 51 citing L S Sealy "Directors' 'Wider' Responsibilities: Problems Conceptual, Practical and Procedural" (1987) 13 MULR 164.
[188] Companies Act 1993, s 10 which states incorporation requires a company to have one or more directors, among other essential requirements.
[189] Law Commission, above n 111, at 41.

formalities intended for their benefit.[190] If this were so, the Law Commission may have intended the *Duomatic* principle to operate to excuse the formalities required by the Act and permit the shareholders to exercise the power contemplated regardless. The shareholders may, therefore, be permitted to waive their rights to a meeting to pass a special resolution and amend the constitution of a company informally and unanimously.

In its draft Bill, the Law Commission initially prohibited unanimous shareholder assent to ratify a breach of directors' duties.[191] However, a provision was later added which arguably preserved the common law position on this issue.[192]

It should be noted Law Commission reports are not law and act as only extrinsic material. Justice O'Regan may have been wrong to place weight on the Law Commission report and arguably should have taken the 1993 Act for how it was ultimately enacted. It is evident, preceding the enactment of the 1993 Act, the relationship between the Law Commission and the Law Reform Division of the Department of Justice – whose role was to provide advice to the Minister on Legislation, instruct Parliamentary Counsel and service select committees – was strained.[193] As a result of this breakdown, the Bill introduced into Parliament departed significantly from the Law Commission's draft Bill.[194] Accordingly, careful attention should be paid to the Law Commission reports relating to the 1993 Act.

2 Section 107

Section 107 provides for unanimous shareholder assent to certain matters as an alternative to the formalities required by the Act.[195] Justice O'Regan took this provision as an indication of the legislative intent to limit the *Duomatic* principle to the certain matters contained in s 107.[196] This provision was born out of criticism to the Law Commission's draft Bill which suggested it was overly rigid and cumbersome for small companies.[197] The Law Commission agreed and responded by providing a means by which formalities could be ignored where all shareholders agree to, or concurred in, certain types of action requiring compliance with formalities.[198] The language used in this draft provision was deliberately intended to capture informal participation or acquiescence by shareholders.[199] David Goddard, who assisted the Law Commission in drafting the Bill, has since noted this draft provision was unduly narrow and could have

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[190] *Re Express Engineering Works Ltd*, above n 21; *Re Oxted Motor Co Ltd*, above n 126; *Cane v Jones*, above n 135 at 539; and *Re RW Peak (Kings Lynn) Ltd*, above n 144.
[191] Law Commission, above n 111, at 259.
[192] Companies Act 1993, s 177(4).
[193] Goddard, above n 78, at 240–241.
[194] Goddard, above n 78, at 241.
[195] Companies Act 1993, s 107.
[196] *Ririnui (SC)*, above n 6, at [167].
[197] Goddard, above n 78, at 244.
[198] Law Commission *Company Law: Transition and Revision* (NZLC R16, 1990) at 232.
[199] Goddard, above n 78, at 244.

extended to all acts done by the company or the board.[200] However, the Law Reform Division did not approve of permitting informal participation to the matters contained in the draft provision and redrafted the provision to require written agreement which could be withdrawn at any time and, where solvency test issues arise, a formal board resolution and certificate.[201]

The background to s 107 suggests it was initially intended to allow shareholders' informal and unanimous assent to certain matters. If the provision was enacted in this manner, perhaps O'Regan J would be correct to limit the *Duomatic* principle to the matters contained within the provision. However, the provision as it currently stands requires the unanimous assent of shareholders to be written.[202] This may suggest the matters contained in s 107 are more important and are therefore elevated above all other matters which may be unanimously assented to informally. This interpretation would be consistent with the *Duomatic* principle surviving the 1993 Act. Instead of the principle being limited to matters contained in s 107, it is limited to all matters not contained in s 107.

Even though s 107 requires the unanimous assent to be in writing, the shareholders may be permitted to waive this formality and carry out the matters contained within the provision informally if the requirement is for the sole benefit of the shareholders. However, the exercise of the matters contained in s 107 are subject to the board being satisfied that the company will satisfy the solvency test after the exercise of the relevant power.[203] This formality may not be waived by the shareholders as it is beneficial to creditors. This was indeed the interpretation of the formalities relating to a company purchasing its own shares, a matter now contained in s 107.[204]

The requirement of a certificate stating the company will satisfy the solvency test after the exercise of a power contained in s 107 further supports the contention that the matters contained in s 107 are more important than others and require express separation from all other powers which may be unanimously assented to informally. Furthermore, it may have been Parliament's intention for shareholders not to attract directors' duties when unanimously agreeing to a matter contained in s 107. When assenting to a matter contained in s 107, the shareholders are exercising a power allocated to them in the 1993 Act and therefore do not come within the scope of s 126.[205] In contrast, if the shareholders unanimously and informally assent to a matter outside their powers as allocated by the Act, they will likely attract directors' duties. In any

[200] Goddard, above n 78, at 244.
[201] Goddard, above n 78, at 244.
[202] Companies Act 1993, s 107(4).
[203] Companies Act 1993, s 107(1).
[204] See *Re RW Peak (Kings Lynn) Ltd*, above n 144.
[205] David Goddard "The Companies Act 1993: Pitfalls and Prospects for Reform" (paper presented to LexisNexis Corporate Law Masterclass, Auckland, November 2004) at 8–9.

event, it is unlikely s 107 is standalone authority to conclude, as O'Regan J did, the *Duomatic* principle no longer applies under the 1993 Act.

3 Section 128

Justice O'Regan then turned to the default provision allocating management powers within a company. Justice O'Regan correctly concluded assent by a simple majority of shareholders to an action requiring a board resolution would not be effective. As illustrated by the judiciary prior to the 1993 Act,[206] and by the 1993 Act itself,[207] a majority of shareholders has no reserve power to make management decisions as s 128 confers an original power to manage on the board. However, as O'Regan J recognised, this is subject to a reallocation of powers by the company's constitution.[208] A document which is firmly in the control of the shareholders.

Section 128 may therefore suggest, as s 109 implies, a majority of shareholders may not do an act, or instruct the board to do an act, within the power of the board. However, shareholders may still employ the *Duomatic* principle to alter the constitution to reallocate management powers to themselves, as permitted by s 128(3). With respect, s 128 does not consequently support the exclusion of the *Duomatic* principle as O'Regan J interpreted it to indicate. To the contrary, s 128 facilitates the use of the *Duomatic* principle to empower the shareholders acting unanimously to make management decisions. In the absence of s 128(3) the *Duomatic* principle would struggle to find a footing in the 1993 Act to enable shareholders to make management decisions informally. Accordingly, s 128 does more to support the view the *Duomatic* principle has survived than to support the view it has not.

Respectfully, the factors relied upon by O'Regan J, when assessed closely, do not support his conclusion. Other provisions of the 1993 Act may also shed light on whether the *Duomatic* principle has survived the 1993 Act.

4 Other relevant provisions of the Companies Act 1993

As mentioned, s 109 permits a meeting of shareholders to pass a non-binding resolution relating to the management of the company. The correct interpretation of s 109 is likely to make any resolution, approved by a simple majority of shareholders, relating to the management of the company non-binding on the board. It would be an absurd result to render a special resolution relating to the management of the company as non-binding as s 128(3) contemplates such a resolution to be binding on the board. Consequently, s 109 is unlikely to prohibit a special resolution by shareholders to amend the constitution to reallocate management powers to

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[206] *Automatic Self-Cleansing*, above n 98, at 38–39; and *Black White & Grey Cabs Ltd v Fox*, above n 104, at 832.
[207] Companies Act 1993, s 109.
[208] *Ririnui (SC)*, above n 6, at [167].

themselves and does not exclude the use of the *Duomatic* principle to amend the constitution in this way by informal unanimous assent.

Where the constitution of a company provides that the business of the company is to be managed by the board, there is generally no power in the general meeting to commence legal proceedings as this is a matter properly allocated to the board.[209] Section 165(3), however, contemplates that power being exercisable by the shareholders acting unanimously. Section 165(3) permits the Court to grant leave to a shareholder or director if satisfied it is in the best interests of the company that the conduct of the proceedings should not be left to the directors or to the determination of the shareholders as a whole. Although the provision treats the unanimous assent of shareholders as tantamount to the decision of the board, it may be a slender foundation upon which to permit the *Duomatic* principle to apply, even in its narrow sense of ratification.[210]

Lastly, the Companies Act provides a procedure that may be followed to avoid many of the formalities required by the Act in exercising shareholders' powers. Section 122 provides that a resolution in writing, relating to a matter required by the Act or constitution to be decided at a meeting of shareholders, is valid if the required majority signs the resolution.[211] Although this provision offers some assistance to shareholders, it does not permit informality to the same extent as the *Duomatic* principle. To comply with this provision, the shareholders ought to turn their mind to the resolution prior to exercising the relevant power. This does not permit shareholders to retrospectively point to conduct or other informal agreement to validate action later taken. The *Duomatic* principle would permit this as assent need not be in writing.

Some relief may be found in s 122(3A) which provides that any resolution in writing may consist of multiple documents signed or assented to by any of the shareholders. The inclusion of "assent" may allow more informal means of approving a resolution pursuant to s 122. However, the assent must relate to some written communication which restricts the ability of shareholders to all agree to a matter and later rely on that agreement in absence of any formal written evidence. The *Duomatic* principle provides a higher degree of flexibility as it does not require written evidence of an agreement. Evidentiary issues may arise in absence of such documentation. However, this relates to substantiating unanimous assent and should not form a basis to extinguish the principle from applying. Section 122 provides some support in avoiding the formalities of the 1993 Act but does not go as far as the *Duomatic* principle. It is therefore unlikely to override or prevent the principle from applying. Indeed, the existence of

[209] *Massey v Wales*, above n 97, at [45] and accepted in Watts, Campbell and Hare, above n 81, at 639.
[210] Goddard, above n 205, at 17–18.
[211] Companies Act 1993, s 122.

the predecessor to s 122 lead to the recognition of the principle during the operation of the Companies Act 1955.[212]

E Judicial Support of the Duomatic Principle Surviving the Companies Act 1993

There has been implicit support for the *Duomatic* principle surviving the 1993 Act.[213] In *Pioneer Insurance Co Ltd v White Heron Motor Lodge Ltd* the High Court considered whether a guarantee was properly executed.[214] The applicant contended a sole director did not have authority to enter into the guarantee because the shareholders' resolution purporting to give the necessary authority was not properly executed. The shareholders' agreement was signed by a third party as the shareholder's attorney which was arguably not permitted at law.[215] Nevertheless, the High Court concluded, irrespective of whether the shareholders' resolution was properly executed, it was clear the director executing the guarantee had actual authority from all shareholders.[216] This unanimous assent acted to validate the agreement.[217]

The High Court additionally found all shareholders to have concurred in the company entering the transaction, a requirement of s 107.[218] Interestingly, if the third party did not have the power to sign for one of the shareholders then it would be evident the shareholders had not all concurred in writing to the shareholders' resolution, which is another requirement of s 107. It should be noted that between the shareholders' resolution, the loan agreement and the guarantee agreement, all the shareholders had signed at least one of these documents.[219] This may satisfy the need for shareholders' concurrence to be in writing but also illustrates a flexible interpretation of s 107. Despite this, the High Court reiterated the shareholders had all approved the transaction which gave authority to the director to enter the agreement.[220]

F Current Status of the Duomatic Principle

It is likely the 1993 Act has not done enough to cleanse modern company law from the operation of the *Duomatic* principle. It is evident a majority of shareholders no longer has a reserve power to manage the business of a company. The default provision allocating

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[212] See *Westpac Securities Ltd v Kensington*, above n 25, at 566.
[213] Watts, Campbell and Hare, above n 81, at 249 citing *Pioneer Insurance Co Ltd v White Heron Motor Lodge Ltd* (2008) 10 NZCLC 264,407 (HC); see also *Kitchener Nominees Ltd v James Products Ltd* (2002) 9 NZCLC 262,882 (HC) at [32].
[214] *Pioneer Insurance Co Ltd v White Heron Motor Lodge Ltd*, above n 213.
[215] *Pioneer Insurance Co Ltd v White Heron Motor Lodge Ltd*, above n 213, at [57] which states the power of attorney was not produced in evidence and s 31 of the Trustee Act 1956 may have precluded the third party from acting as the shareholder's attorney.
[216] At [63].
[217] At [66].
[218] At [64].
[219] At [63].
[220] At [67].

management powers to the board is rebuttable as the provision is subject to the constitution. In assessing whether the shareholders are permitted through the use of the *Duomatic* principle to unanimously do informally what might be done formally by special resolution, the relevant provisions of the 1993 Act were considered. As a result, the conclusion of O'Regan J becomes less compelling and in fact the contrary conclusion could justifiably be reached. The result permits the shareholders, acting unanimously, to informally assent to amend the constitution to reallocate management power originally allocated to the board, to themselves. Consistent with the dicta of Lord Davey in *Salomon*, the unanimous assent of shareholders will consequently bind the company. Accordingly, the *Duomatic* principle likely does apply in New Zealand, but whether it should apply is a different inquiry.

Chapter III: Should the Duomatic Principle in New Zealand?

The fundamental issue in relation to the *Duomatic* principle is whether the formalities required by statute are to be treated with the utmost sanctity so that any disregard of them would act to strike down any subsequent decision to which the formalities related, or whether the formalities are required for a particular purpose and when that purpose is fulfilled the formalities serve no other useful purpose and may be disregarded. The most appropriate interpretation is the latter.

The *Duomatic* principle may find justification in equity or contract. Importantly, however, the recognition of the principle may realise significant economic benefits. The consistency of the principle with the 1993 Act and corporate regulation should be assessed while ensuring fundamental company law concepts are not eroded by the imposition of such a principle.

A The Effect of the Duomatic Principle

The *Duomatic* principle has been confused with a principle bestowing on the shareholders the power to make management decisions.[221] This is understandable as the expression of the principle in *Meridian*, which stated the unanimous decision of shareholders will be a decision of the company, lends itself to that conclusion.[222] However, the principle does not empower shareholders with the ability to usurp the management powers originally allocated to the board. Indeed, *Automatic Self-Cleansing* confirmed this. Some commentators have contended the principle is no longer justified as it is premised on a concept of shareholder primacy that no longer exists.[223] It is true, the principle was applied at a time when shareholders were thought of as principals to the agent directors.[224] However, the position expressed in *Automatic Self-Cleansing* was also the position at the time the *Duomatic* principle was applied to joint stock companies.[225]

The water may have been muddied by the Companies Clauses Consolidation Act 1845 where the board's power to manage was expressly subject to the general meeting of shareholders.[226] However, this power no longer exists and is abrogated by the 1993 Act.[227] The 1993 Act confirms the position under the preceding Table A articles of association that shareholders may vary the constitution of the company.[228] Section 128(3) then clarifies that the original allocation of management power to the board is subject to the constitution. Accordingly, the shareholders

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[221] *Ririnui (CA)*, above n 3, at [54].
[222] *Meridian*, above n 2, at 12.
[223] See Grantham, above n 5; and Watson, above n 5.
[224] J Hill "Visions and Revisions of the Shareholder" (2000) 48 American J of Comp Law 39 at 42; and see this article generally for a description of the evolution of the shareholders' role.
[225] See *Burnes v Pennell* (1849) 2 HLCas 497 (HL).
[226] Companies Clauses Consolidation Act 1845 (UK), s 90.
[227] Section 109.
[228] Section 32.

possess the power to usurp the management powers of the board, not through the *Duomatic* principle, but through the statutorily confirmed power to alter the constitution.

The *Duomatic* principle does not entitle the shareholders to ratify acts of directors either. Directors' duties are owed to the company; an entity separate from its shareholders. However, in a solvent company the interests of the shareholders have been equated to the interests of the company.[229] It is therefore open to the shareholders to ratify a breach of directors' duties owed to the company. An important limitation was suggested in *Horsley & Weight* where Cumming-Bruce and Templeman LJJ doubted whether shareholders could ratify a decision concerning the interests of creditors.[230] This is consistent with the recent decision in *Prest v Petrodel Resources Ltd* where Lord Sumption JSC noted the shareholders may approve a foolish or negligent decision in the ordinary course of business where that company is solvent.[231] Of course, when a company is insolvent or when a company is nearing insolvency, the interests of the company's creditors become intertwined with the interests of the company.[232] The shareholders are therefore not competent to ratify an act done by an insolvent, or close to insolvent, company as their interests are no longer equated with the interests of the company. Nevertheless, shareholders remain able to ratify a breach of duty owed to a solvent company.[233]

The *Duomatic* principle merely allows shareholders to do informally that which they can do formally. Any justification of the principle is therefore not based on a historic conception of shareholder primacy. Such arguments are properly directed at justifying the rule that gives shareholders exclusive control over the constitution. The rule is confirmed by the 1993 Act so disputes as to the shareholders' power to usurp the management powers of the board are frivolous. Additionally, arguments directed at the shareholders' power to ratify breaches of directors' duty are properly directed to the authority that equates the shareholders' interests to the interests of a solvent company. The *Duomatic* principle only permits these powers to be exercised informally and requires justification to retain a place among corporate regulation.

B Possible Justifications for the Duomatic Principle

1 Equitable Estoppel

The *Duomatic* principle may be justified by the doctrine of equitable estoppel. Promissory estoppel operates in a situation where one party has led another party into a belief that was relied upon to an extent that would make it unconscionable for the original party to assert its

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[229] *Greenhalgh v Arderne Cinemas Ltd* [1951] Ch 286 (CA), at 291.
[230] *Re Horsley & Weight Ltd*, above in 24, at 455–456.
[231] *Prest v Petrodel Resources Ltd*, above n 32, at [41].
[232] *Sojourner v Robb* [2006] 3 NZLR 808 (HC) at [102].
[233] Companies Act 1993, s 177(4) confirms the common law position is retained; but compare Law Commission, above n 111, at [87].

legal rights.[234] Where the shareholders have unanimously but informally agreed to an action, whether it be to ratify an act of directors or amend the constitution, they may be estopped from asserting the invalidity of the agreement on the basis that formalities had not been complied with.

In *Waltons Stores (Interstate) Ltd v Maher*, promissory estoppel was applied to prevent a party purporting to resile from an agreement because a formality had not been complied with.[235] Two parties had come to an agreement in relation to a building project. A draft contract was prepared and it was agreed any dispute to the contract would be made the following day. No contact was made and the building project was commenced. Two months later the other party asserted they would not be upholding the agreement. It was not argued a binding contract was in existence as the contract was conditional on the signature of both parties, which was not obtained. Damages were awarded, not for breach of contract, but because there was an understanding the contract would be signed and such understanding was acted upon which gave rise to an unconscionable position. New Zealand courts have continued to apply promissory estoppel to oral agreements.[236]

Despite this, promissory estoppel is not a compelling justification for the *Duomatic* principle. Promissory estoppel does not assert that the shareholders' approval is tantamount to a formal approval. Rather, it operates to prevent shareholders asserting invalidity. Accordingly, the shareholders are prevented from asserting non-compliance but, as in many cases, the liquidator will remain able to assert non-compliance. Furthermore, promissory estoppel requires a detriment as a result of the reliance.[237] When the *Duomatic* principle is invoked there will generally be no detriment to shareholders resulting from reliance on the informal assent of shareholders. Accordingly, this justification is weak.

2 Waiver of formalities

As aforementioned, many cases have found the informal and unanimous assent of shareholders acts to waive formalities intended for the sole benefit of shareholders.[238] Applying the principle in this manner is consistent with the dominant nexus of contracts theory of corporations. This theory was initially developed in an economic context and took on a number of strands when applied to a legal context.[239] The most dominant is the shareholder-centric model in which it is

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[234] John Burrows, Jeremy Finn and Stephen Todd *Law of Contract in New Zealand* (5th ed, LexisNexis, Wellington, 2016) at 140–153.
[235] *Waltons Stores (Interstate) Ltd v Maher* (1988) 76 ALR 513 (HCA).
[236] See *Harris v Harris* (1989) 6 FRNZ 1 (HC); and *Juzwa v Hill* [2007] NZCA 222, (2007) 8 NZCPR 733; but compare *Actionstrength Ltd v International Glass Engineering* [2003] UKHL 17, [2003] 2 AC 541.
[237] See Burrows, Finn and Todd, above n 234, at 140–153.
[238] See Chapter II(C).
[239] Michael C Jensen & William H Meckling "Theory of the Firm: Managerial Behavior, Agency Costs and Ownership Structure" (1976) 3 Journal of Financial Economics 305.

suggested a group of shareholders enter into an agreement together thus creating a corporation.[240] This initial agreement is seen as a private contract and is equated with the constitution of a company. The shareholders then contract with managers to operate as agents on their behalf. To some extent, this resurrects the previous conception of shareholders as owners.[241]

The nexus of contracts theory, therefore, views the shareholders as the source of corporate powers which are then delegated to the board. This theory suggests the constitution of the company amounts to a private contract between shareholders and may explain why the shareholders have retained exclusive control over the constitution.[242] This underlying theory also permits shareholders to waive the formalities required by the constitution based on contract law principles as they are the only parties to the constitutional contract.[243]

The nexus of contracts theory does not exist free of criticism.[244] A further aspect of the nexus of contracts theory argues the private contractual nature of the corporation should preclude any state regulation as the parties to the contract should be trusted to adequately protect their own interests or suffer the consequences of poor judgment.[245] However, a state imposed legal framework inevitability surrounds private agreements. Indeed, limited liability is a fundamental tenet of company law, yet it is unable to be fully contracted for through private agreement.[246] Although this was largely achieved by joint stock companies prior to the conception of the modern incorporated company, this may only be achieved against voluntary creditors.[247] It is therefore evident the state imposes a fundamental regulation on corporations that may not be contracted for privately. Contrary to the nexus of contracts theory, the corporation is as much a creation of the state as a creation of contract.

In stark opposition to the shareholder-centric nexus of contracts theory, it has been suggested the company, as a separate entity distinct from its shareholders, possesses the rights and powers to act.[248] The rights and powers are then allocated to the various parties involved, whether it be directors or shareholders, so they may act on its behalf. Consequently, the shareholders will only have the power to act if authorised to do so. Such authorisation is usually found in the

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[240] Nicolas Juzda "Unanimous Shareholder Agreements" (PhD Dissertation, York University, 2014) at 15.
[241] See Hill, above n 224, at 42 for a description of this conception.
[242] Companies Act 1993, s 32.
[243] See Burrows, Finn and Todd, above n 234, at 747–751 for a general description of contract law principles permitting parties to waive contractual terms.
[244] See William W Bratton Jr "The Nexus of Contracts Corporation: A Critical Appraisal" (1989) 74 Cornell L Rev 407 for an extensive criticism of the nexus of contracts theory.
[245] Juzda, above n 240, at 17.
[246] See David Goddard "Corporate Personality: Limited Recourse and its Limits" (paper presented at the Centenary Celebration Conference of *Salomon v Salomon*, Auckland, July 1997) for a discussion on contracting for limited liability.
[247] Watts, Campbell and Hare, above n 81, at 49.
[248] Grantham, above n 5, at 256.

constitution which specifies the extent of the authority granted and the manner in which the powers are to be exercised.[249] When shareholders purport to exercise the powers in non-compliance with the formalities, the shareholders act outside their authority and any attempt to bind the company would be to undermine the company, as a separate entity, being the source of these powers.[250] This conception would preclude the shareholders from waiving the required formalities. However, this argument necessarily rests on the assumption that a company is the source of powers allocated to shareholders and directors.

Although the underlying conceptual theory of a company is unsettled and arguably ambulatory, the 1993 Act encapsulates much of the shareholder primacy beliefs fundamental to the nexus of contracts theory. Shareholders have retained an express power to appoint and remove directors which may or may not be themselves,[251] disprove of major transactions,[252] remove the decision making power of directors,[253] voluntarily liquidate an otherwise solvent company[254] and, importantly, the shareholders have retained exclusive control over the companies governing document.[255]

It would be consistent with the nexus of contracts theory and the conception of shareholder primacy underpinning the 1993 Act[256] to permit the unanimous assent of shareholders to waive the formalities intended for their sole benefit. To require unwavering compliance with formalities is to pay them lip service and offers an overly formulistic approach. Consistent with the dicta of Potter LJ in *Wright*, a more appropriate approach is to consider the purpose and underlying rationale of the particular formalities.[257]

Accordingly, the shareholder-centric drafting of the 1993 Act suggests the shareholders are competent to waive the required formalities. The *Duomatic* principle is therefore likely to find justification in the shareholders' ability to waive formalities required for their benefit.

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[249] Grantham, above 5, at 256; and see *Rolled Steel Products (Holdings) Ltd v British Steel Corporation* [1986] Ch 246 (CA) at 304 where it was stated acts done otherwise than in accordance with the formalities will not be the acts of the company.
[250] Grantham, above n 5, at 256–257.
[251] Companies Act 1993, s 153.
[252] Companies Act 1993, s 129.
[253] Companies Act 1993, s 128(3).
[254] Companies Act 1993, s 241.
[255] Companies Act 1993, s 32.
[256] See Watts, Campbell and Hare, above n 81, at 230–235 for an explanation of shareholder primacy underlying New Zealand company law and its evidence in the 1993 Act.
[257] *Wright v Atlas Wright (Europe) Ltd*, above n 151, at 315.

C Consistency with the Objectives of Companies Act 1993

The underlying objectives of the 1993 Act are contained its preamble.[258] Testing the consistency of the *Duomatic* principle against these objectives will illustrate its appropriateness in the context of the 1993 Act.

The 1993 Act aims to reaffirm the value of the company as a means of achieving economic and social benefits through the aggregation of capital for productive purposes, the spreading of economic risk, and the taking of business risks.[259] A company is an economic vehicle and the policy rationale for its existence is found in the economic benefits it creates.[260] The regulation of companies must therefore be justified on economic terms. The imposition of separate corporate personality and limited liability provide examples of corporate regulation justified in the economic cost savings each provides.

First, separate corporate personality enables capital to be collected while avoiding the administrative costs of transferring the business assets to new participants.[261] Instead, a share representing an interest in the business may be transferred. Second, imposing a default limited recourse rule on all incorporated companies avoids the administrative costs of negotiating such a term in all credit contracts.[262] It should be noted this economic benefit only exists in regard to voluntary creditors as involuntary creditors bare the risk of default which cannot be internalised to the same extent as voluntary creditors. Despite this, limited liability has been extended to all companies dealing with all creditors. Consequently, monitoring costs are lowered as shareholders need not monitor their investments which encourages increased investment and diversified portfolios.[263]

The *Duomatic* principle also results in cost savings. Most SMEs do not have the capacity to comply with unforgiving administrative practices beyond basic bookkeeping.[264] Requiring them to do so will either lead to a decision not to incorporate or to systematic non-compliance.[265] A decision not to incorporate will eliminate any potential economic benefits or capital accumulation. Furthermore, incurring significant compliance costs, or the penalty for non-compliance, will act to increase the price of any commercial activity. Such an environment will discourage commercial activity and growth. Consequently, any tool which assists in avoiding compliance costs will act to encourage economic activity as well as lowering economic costs. The *Duomatic* principle will achieve this as compliance with formalities will

[258] Companies Act 1993, Preamble.
[259] Companies Act 1993, Preamble (a).
[260] Goddard, above n 246, at 8.
[261] Goddard, above n 246, at 9.
[262] Watts, Campbell and Hare, above n 81, 48–50.
[263] Watts, Campbell and Hare, above n 81, at 50.
[264] Goddard, above n 78, at 251.
[265] Goddard, above n 78, at 251.

not be required where unanimity among shareholders exists. This will be particularly valuable for SMEs where unanimous assent will be relatively simple to obtain.

The 1993 Act also aims to encourage efficient and responsible management of companies by permitting a wide discretion in matters of business management while providing protection for shareholders and creditors.[266] The formalities required by the 1993 Act to pass a special resolution may have been imposed as a means of protecting shareholders and creditors. The *Duomatic* principle would therefore permit shareholders to act in disregard of these protections.

When the *Duomatic* principle is engaged the shareholders are disregarding formalities to exercise a power they possess. If shareholders have reallocated management power to themselves, whether in accordance with formalities or in disregard of formalities, the creditor protections contained in the directors' duties are maintained as shareholders will be deemed directors pursuant to s 126(2). The formalities required therefore have no effect on the vulnerability of creditors. Accordingly, the *Duomatic* principle may not be precluded on this basis.

The argument suggesting formalities relating to special resolutions are required for the benefit of shareholders is much stronger. The requirement that a particular majority, above a simple majority, assent to a resolution shows a greater want to protect minority shareholders' rights. The *Duomatic* principle disregards formalities and in doing so, the protection for minority shareholders. However, this concern is illusory as the fundamental requirement of the principle ensures unanimity. Consequently, no minority exists for protection. The *Duomatic* principle therefore does not impeach the provisions protecting shareholders and creditors.

A further aim of the 1993 Act is to define the relationships between companies, directors, shareholders and creditors.[267] It has been suggested, to treat the unanimous agreement of the shareholders as a decision of the company is to treat the shareholders as the company which would be inconsistent with the status of the company being a separate legal entity distinct from its shareholders.[268] This argument was later highlighted by the Court of Appeal in *Ririnui* where Harrison J stated the directors' power to manage a corporation's operations free of shareholder control is consistent with the separate personality of a company.[269] However, it is arguably incorrect to contend the *Duomatic* principle involves a disregard of the separateness of the corporate personality.

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[266] Companies Act 1993, Preamble (d)
[267] Companies Act 1993, Preamble (c).
[268] See Grantham, above n 5, at 259 where it was suggested the unanimous assent of shareholders involves a disregard of the corporate personality.
[269] *Ririnui (CA)*, above n 3, at [57].

There is no inconsistency in a company having separate legal personality and permitting the shareholders to unanimously make management decisions.[270] When the unanimous acts of shareholders are viewed as the acts of the company, this involves no more disregard of the corporate personality than a formal resolution of directors or shareholders.[271] The shareholders are exercising a power vested in them. Specifically, the power to alter the constitution to bestow upon themselves the power to make management decisions on behalf of the company.[272] As this power is vested in the shareholders, when the shareholders exercise it they are acting in their capacity as shareholders. As a result, the shareholders may exercise the company's powers on its behalf but the company and the shareholders remain separate in law.[273] The only difference between the unanimous and informal act of shareholders and a resolution of shareholders or directors is the disregard of formalities, not of corporate personality.

D Consistency with Corporate Regulation

The 1993 Act has been criticised for being overly prescriptive as it sets out precise steps which must be taken to exercise a number of powers.[274] A possible explanation for this over drafting, and tendency to regulate to avoid potential abuse rather than to regulate for what is needed, may stem from the hostility to liberalisation of companies after the share market crash in 1987.[275] However, over regulation imposes significant compliance costs on SMEs.[276] It is possible the 1993 Act has over regulated in this regard if strict compliance with formalities is required. The regulation of partnerships and the further regulation required by incorporation offers an extreme example of minimal corporate regulation which may highlight the need to preserve the *Duomatic* principle to maintain flexibility and simplicity in the 1993 Act.

In contrast to the regulation of companies, the New Zealand Partnership Act 1908[277] is relatively short and simple and contains no mandatory content so far as dealings between partners are concerned.[278] The decision making power may be allocated to one, some or all partners and the rights and duties of partners may be varied by the consent of all partners, whether that consent is express or implied.[279] If the partners wish to conduct their business with the benefit of separate legal personality and limited liability, they may choose to incorporate.

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[270] Watts, above n 67, at 91.
[271] Watts, Campbell and Hare, above n 81, at 248; see also *Meridian*, above n 2, at 11 which clarifies a company exists as a separate entity but requires acts to be attributed to it through the rules of attribution and the unanimous decision of all shareholders was stated to be a primary rule of attribution at 11–12.
[272] Companies Act 1993, s 32.
[273] Watts, Campbell and Hare, above n 81, at 248.
[274] Goddard, above n 78, at 242.
[275] Goddard, above n 78, at 244.
[276] See generally Goddard, above n 78.
[277] Partnership Act 1908.
[278] Goddard, above n 78, at 247.
[279] Partnership Act 1908, s 22.

If a company is formed, certain requirements are necessary. Registration enables third parties to satisfy themselves of the company's existence, who to communicate with on behalf of the company, and who has authority to bind the company.[280] Limited liability needs to be supported by rules which ensure creditors are paid before shareholders, provide for insolvent liquidation and require records to be kept so business assets can be distinguished from the assets of shareholders.[281] Beyond these rules, incorporation does not require any more regulation. Specifically, incorporation does not justify regulation of the internal management of a company. The imposition of limited liability removed the need for shareholders to monitor their investment which encourages a separation of ownership and control, but does not necessitate it. This adaption of partnership regulation provides an extreme example of minimal regulation.

The 1993 Act, however, provides s 128(1) as a default provision which some contend is only rebuttable by following the specified procedure.[282] Preserving the *Duomatic* principle will provide another means by which shareholders may vary the default position. This would import flexibility and allow the 1993 Act to move toward a more liberalising statute. Indeed, this has proved to be desirable. In the United States, the most popular States for company incorporation, ignoring beneficial tax consequences, are those that set few mandatory rules regarding the internal management of the company.[283] The 1993 Act is relatively flexible and simple when compared to the Australian equivalent.[284] The preservation of the *Duomatic* principle however will permit an increased degree of flexibility which would come as a boon to SMEs.

E Statutory Recognition of the Duomatic Principle

It is evident the *Duomatic* principle is a principle permitting the shareholders to do informally that which they may do formally. The shareholders have the power to make management decisions and ratify breaches of directors' duty. The principle merely permits the shareholders to do this in disregard of formalities. The principle is unlikely justified by the doctrine of equitable estoppel, but may be justified by the shareholders' ability to waive formalities. However, such a conclusion is dependent on the underlying conception of the company which is unsettled legal territory. Nevertheless, the principle is justified by alternative means.

The *Duomatic* principle is not wanting of an economic justification. SMEs would realise significant benefits as it may be employed to lower their compliance costs and facilitate economic activity. This economic justification is particularly convincing when it is recognised

[280] Goddard, above n 78, at 248.
[281] Goddard, above n 78, at 248.
[282] See Grantham, above n 5, at 256.
[283] Goddard, above n 78, at 248–249.
[284] Corporations Act 2001 (AUS).

SMEs comprise 97 per cent of all enterprises in New Zealand.[285] The *Duomatic* principle would not impeach or limit any protections the 1993 Act provides for shareholders or creditors and would not conflict with the fundamental company concept of separate corporate personality.

The *Duomatic* principle should, therefore, have a place in New Zealand's corporate regulation. To resolve the uncertainty surrounding the principle in New Zealand, Parliament should not wait for an appellate court to reach the wrong outcome. Instead, a provision relating to informal unanimous resolutions of shareholders should be expressly provided. Such a provision may take the following form:

> **122A Informal Unanimous Resolutions**
>
> (1) A unanimous resolution of shareholders will have the same effect as a resolution passed at a properly convened meeting of shareholders.
>
> (2) A resolution passed pursuant to subsection (1) will be effective whether an ordinary or special resolution is required to be passed at a meeting of shareholders.
>
> (3) Assent to a resolution required by subsection (1) may be given in any informal manner including by giving–
>
> (a) Assent by oral communication; or
>
> (b) Assent by conduct; or
>
> (c) Assent by writing; or
>
> (d) Assent by any other means the Court considers appropriate.

A provision of this kind would be appropriate after s 122 as it extends the informal process by which shareholders may exercise their powers. In addition to the current statutory means of passing a resolution, such a provision will clarify the shareholders' informal and unanimous assent will be tantamount to a formal resolution of shareholders, whether that be an ordinary or special resolution. The provision will cement the *Duomatic* principle as a principle permitting informality and not as a principle empowering shareholders to exercise management powers. Such confusion has led to mixed views on whether the principle has a place in New Zealand corporation regulation. On the proper interpretation of the principle however, it certainly deserves recognition in New Zealand.

[285] Small Business Development Group *Small and Medium Businesses in New Zealand* (MB13532, May 2016).

Conclusion

The *Duomatic* principle is a principle permitting shareholders to do informally that which they may do formally. The development of the principle in England and New Zealand is consistent with this formulation of the principle. The principle does not empower shareholders with any additional powers other than to act informally in the exercise of their powers when acting unanimously. The limitation of the ultra vires doctrine, as suggested by Lord Davey in *Salomon*,[286] no longer has teeth in the New Zealand corporate environment and should therefore no longer form part of the principle.

The shareholders do not possess reserve powers to manage the company. This is confirmed by the 1993 Act which allocates original management powers to the board subject to the constitution.[287] The shareholders, therefore, possess the power to usurp the board by amending the constitution. The formalities required in amending the constitution, or in the exercise of any other shareholder powers, are subject to waiver by the unanimous agreement of shareholders provided the formalities are for the sole benefit of shareholders. This waiver may be implied or express. Accordingly, the *Duomatic* principle operates to permit shareholders to exercise a power through unanimous and informal assent.

This informality is consistent with the 1993 Act. Although the Supreme Court expressed doubts as to whether the *Duomatic* principle survived the 1993 Act,[288] fortunately not enough has been done to rid company law of its operation. The *Duomatic* principle therefore remains part of New Zealand corporate law.

An assessment as to whether the *Duomatic* principle should apply in New Zealand illustrates the justification of the principle. The shareholders' ability to waive formalities is consistent with both the nexus of contracts theory of the corporation and the shareholder supremacy undertones of the 1993 Act. Any doubt as to whether the *Duomatic* principle should apply disappear in light of the economic benefits it would cause. The principle is both consistent with the objects of the 1993 Act and the role of corporate regulation. The *Duomatic* principle, therefore, deserves statutory recognition.

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[286] *Salomon*, above n 1, at 57.
[287] Section 128.
[288] *Ririnui (SC)*, above n 6, at [167].

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