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THE DUOMATIC PRINCIPLE

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SUBMITTED IN FULFILMENT OF THE REQUIREMENTS FOR THE DEGREE OF LLM BY RESEARCH

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Abstract: The Duomatic principle is a well established part of corporate law, enabling shareholders to informally but unanimously make decisions which bind the Company. It traces its history to some of the earliest cases of company law, and the most recent review of company law decided to leave it uncodified. The resulting flexibility has caused some uncertainty as to the precise ambit of this principle. The aim of this thesis is to establish how this principle should interact with modern corporate law, review the judicial history of this principle and provide a modern test for its application. In order to do so, it firstly reviews the background to the modern corporate form, to establish where this principle should fit into the modern decision making framework for a company. It then traces the history of the principle, from its origins in Salomon and partnership law to its modern day application, and compares the judicial treatment of this principle to the normative framework. It then develops the modern, practical test for judicial application of this principle: when the principle can apply, and who needs to do what to make it do so. However, this test seems unsatisfactory as on almost every subject there are cases that conflict with this general position: whilst a modern test can be constructed, there is no certainty that it will be followed. This thesis ultimately concludes that this principle is a subset of equity; a remedy that courts retain discretion to utilise should they see fit and so not one of objective verifiable application - a position which conflicts with the theoretical root of the principle and its apparent modern day application.
Author's Declaration

I declare that, except where explicit reference is made to the contribution of others, this thesis is the result of my own work and has not been submitted for any other degree at the University of Glasgow or any other institution.

Jonathan Charles Hardman

3 March 2017
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1. **INTRODUCTION**

The purpose of this thesis is to analyse and evaluate the ability of shareholders to overcome infelicities of procedure and/or substance by acting unanimously and informally together. We will discuss how the law has facilitated this in practice, limitations upon it and circumstances in which it may be argued. This vague concept will be called the "Principle" throughout this thesis.

It well established that “for nearly a century the unanimous assent of shareholders has held the status of an overriding authority, able to ... validate almost any act within the capacity of the company”.\(^1\) In the case of *Re Duomatic Ltd*, Buckley J stated:

> “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 a general meeting.”\(^2\)

This has become known as the “Duomatic Principle”, but is merely the most famous manifestation of the Principle. Despite recommendation that this be codified to provide certainty as to its application,\(^3\) when the Companies Act 2006 was implemented it was decided not to codify the Principle but instead maintain its flexibility of application. Various other common law provisions were codified at this time.

Nevertheless, the Principle has been tested before the courts in numerous situations (in respect of the Companies Act 2006, the Companies Act 1985 and previous Companies Acts), and apparent clarity over the situations in which it can be applied has emerged.

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2. *In re Duomatic Ltd* [1969] 2 Ch 365, 373
The Principle has been criticised as “a principle without form”, whose flexibilities are also its weaknesses. It has also been argued that the Principle "sits uncomfortably alongside many of the central principles of company law". Courts have provided an apparent, consistent and object application of the Principle that appears to sit comfortably with the normative underpinnings of company law. However, it is argued that, when examined closely, there are many grey areas and uncertainties as to the application of the Principle, which leads to the conclusion that instead it is a tool of the court to achieve a just outcome.

The Principle relates to corporate decision making. Accordingly, any examination of the Principle requires to explore the decision making framework of the modern company: particularly how decisions can be made and who they can be made by. Accordingly, Chapter 2.1.1 firstly analyses the origins of a modern company. By concentrating on separate legal personality, this thesis will show that the modern company (incorporated by registration) is in fact a hybrid of a partnership and a corporation given legal personality by statute. This dual nature creates an opportunity for different views of various elements of the modern corporate form, including from which sources modern company law draws to complete any normative gaps. Chapter 2.1.2 identifies and discusses the agency costs that arise from having a separate legal vehicle, whilst Chapter 2.1.3 discusses the options open to law to minimise, or preferably eliminate, such agency costs.

Chapter 2.2 reviews theories of company law and concludes that a company should be run for its shareholders with maximum protections for third party creditors. Chapter 2.3 develops this analysis by examining which internal organ of the company should make decisions on behalf of the company. Having identified this should be a default rule in favour of directors, Chapter 2.4 discusses the level of formality of decision making that should

\[4\] Jason Ellis, ‘Unanimous consent of shareholders: a principle without form?’ 2011 The Company Lawyer 260
\[5\] Grantham (n1) 271
\[6\] Prior to incorporation by registration, a specific act of Parliament or charter was required for incorporation. Any such historic entity will be referred to as a “Corporation”
be required and concludes that this, too, should be a default rule for formality which can be waived by the shareholders unless such rule is designed for the protection of third parties. Chapter 2.5 reviews how shareholders should make decisions. From these theoretical foundations this thesis draws a normative conclusion about how the Principle should operate in Chapter 2.6. Chapter 2.7 discusses a theoretical concept that underpins discussion of the Principle: the English law rules of equity.

Chapter 3 discusses the historical development of the Principle and analyses historic case law in light of the normative framework outlined in Chapter 2. Having traced the judicial development of the Principle, Chapter 4 will examine situations in which the Principle will currently apply and when it will not, concluding that the Principle under UK law appears to fit neatly into the normative framework for company law, especially in respect of the protection that it offers to third party stakeholders. Chapter 5 discusses the nature of the Principle and concludes that it is, ultimately, a subset of equity.

The core hypothesis of this thesis, therefore, is that whilst the Principle generally operates in a manner coherent with the theoretical framework of company law, the flexibility retained by the courts to utilise the Principle to create a “just” outcome undermines its certainty, and therefore its utility ex ante.
2. **Theoretical Toolkit**

The Principle is part of decision making by companies. Before examining the application of the Principle we need to see how the Principle *should* apply. Accordingly, prior to analysing the judicial application of the Principle, this thesis will rehearse the theoretical background to the company itself and corporate decision making. It will do so by reviewing (a) the theoretical origins of the company, (b) in whose interest a company should be run, (c) which category of corporate constituents should be able to make decisions on behalf of a company, (d) the level of formality that should be required in any such decision making and the English law of equity. This chapter therefore provides a theoretical toolkit for the rest of this thesis.

2.1. **The Origins of the Modern Company**

2.1.1. *Where does a modern company come from?*

It has been stated that “the word company has no strictly legal meaning”. ⁷ However, the vast majority of jurisdictions have created a form of business entity with the same 5 characteristics: “legal personality, limited liability, transferable shares, delegated management under a board structure and investor ownership”. ⁸ Most jurisdictions have legislated or recognised a vehicle into which people put money with no risk of being asked for additional money, which is actively managed by a separate group (or subset) of people and which can be exited by individual investors without withdrawing their funds from the organisation. The majority of these characteristics can be achieved contractually (management can be delegated, exit strategies can be negotiated, and trust structures can, subject to discussion below, insulate the assets of shareholders from an investment). It is, however, not possible under English law to contractually

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⁷ Stanley, Re [1906] 1 Ch. 131, see paragraph 1 -1 of Paul L. Davies and Sarah Worthington (ed) Gower & Davies' Principles of Modern Company Law (9th Edn., London 2012)

create a separate legal personality.\(^9\) We must first explore why companies are granted separate legal personality.

There were historically three key rival interpretations of where a company obtains its personality from: the state conceded separate legal personality to entities, that the shareholders contractually agreed to create a new entity, and the company itself was somehow a natural person.\(^10\) Taking these strands in turn:

\textbf{(a) The “State Gift” Theory.}

This theory states that the benefit of a separate legal personality arises from the state, subject to whatever terms and conditions that the state happens to deem fit. Its adherents can point to a 1612 decision in which Sir Edward Coke opined “incorporation cannot be created without the King”.\(^11\) They can also point to the Bubble Act 1720 which prohibited the use of the joint stock company without express approval from the state. These examples can be used to present an argument that, historically and theoretically, legal personality derived as a gift from the state.

\textbf{(b) The “Contractarian” Theory.}

Another interpretation is that legal personality arose because private actors desired it and utilised existing trust and agency rules to achieve it. Mahoney has characterised Coke’s statement above and the Bubble Act as political moves undertaken by a state attempting to regain control over every aspect of civic life, including business organisation. He cites admiralty law developments to demonstrate the common law’s ability to create a form of separate legal personality.\(^12\) Under this view, corporate law involves private

\(^9\) Scottish partnerships enjoy such a benefit - Partnership Act 1890 s4(2)
\(^10\) Brian R. Cheffins, The Trajectory of (Corporate Law) Scholarship, (CUP 2004 ) (“Cheffins Lecture”) 39
\(^11\) Sutton’s Hospital (1612) 77 E.R. 937
\(^12\) Paul G Mahoney, ‘Contract or Concession? An Essay on the History of Corporate Law ’ 34 Georgia Law Review 873
actors voluntarily contracting to create all facets of the modern company, with the state occasionally interfering with this process.

(c) The “Real Entity” Theory.

This theory characterised each of the above as somehow claiming that the company was a fiction, whereas in fact it is a separate entity, entirely separate from its various corporators.\(^{13}\) This had the advantage of recognising an internal aspect to the company, and therefore raised early issues of corporate governance and questions of how a company should make decisions.\(^{14}\)

This debate became rather abstract in nature and accordingly was concluded to be misconceived,\(^{15}\) concluding that a company’s legal personality was more than just an aggregation of people, but less than a natural person.\(^{16}\) It has, however, been noted that modern analysis has obliquely revisited this subject. Hansmann and Kraakman\(^{17}\) have proposed that the purpose of a company is to separate assets of the shareholder from the creditors of the company (referred to as “defensive asset partitioning”) and the assets of the company from the creditors of the shareholder (referred to as “affirmative asset partitioning”). They have posited that the former is contractually achievable; but the latter is more difficult to achieve without legal intervention. Cheffins has argued that this could be viewed as a modern variant of the State Gift theory.\(^{18}\) However, affirmative asset partitioning can indeed be achieved by contractual means. It is easy to point to modern commercial trust structures and see how contractual methods achieve affirmative asset partitioning. As previously noted,

\(^{13}\) Frederick Pollock, ‘Has the Common Law received the Fiction Theory of Corporations?’ (1911) 27 Law Quarterly Review 219

\(^{14}\) Susan Watson, ‘How the company became an entity: a new understanding of corporate law,’ 2015 Journal of Business Law 120

\(^{15}\) John Dewey, ‘The Historic Background of Corporate Legal Personality’ (1926) 35 Yale Law Journal 655, cited in Cheffins Lecture (n10) 40

\(^{16}\) Cheffins Lecture (n10) 39


\(^{18}\) Cheffins Lecture (n10) 72
Mahoney has suggested that measures such as the Bubble Act were only implemented to stymie commercial development in achieving both affirmative and defensive asset partitioning. Adopting Mahoney’s analysis, the state is not required for separate personality, providing a historic victory to the Contractarian analysis (even if there is no normative conclusion on the subject).

Despite the debate on the origin of legal personality being resolved, it is helpful to consider the historical context in which this debate arose. Prior to incorporation of a company by registration, the primary legal forms of business entity were partnerships and Corporations (incorporated by royal charter). Corporate law is generally regards to have “developed seamlessly from the law of partnership”.\(^\text{19}\) Mahoney states that the intervention of the state discussed above meant that the common law of an entity between a statutory corporation and a small partnership was retarded, so when incorporation by registration became more readily available, the courts had to apply the only legal norms available to them to the new entity.\(^\text{20}\) Watson has argued that modern company law is, effectively, a hybrid of legal norms relating to statutory incorporated companies and partnerships rather than a neat descendant of partnership law.\(^\text{21}\) The tension between these two origins of the modern company can be seen in the conflicts between various theories of corporate law which have been reviewed above and which are to be reviewed over the course of this thesis. State Gift theorists can look to statutory incorporations for their analysis, whereas Contractarians can take their justification from norms rooted in partnership law. Any tension which arises from an attempt to apply one set of rules to a modern company is traceable to this historic debate, which is in turn linked to the size of company in mind. Implicit within the logic of adherents to the State Gift theory is that the company in question is large with a dispersed shareholder base (i.e. Corporations incorporated by statute), whereas implicit in the argument of the Contractarians is that the company in question is a quasi-

\(^\text{19}\) O’Neill v Phillips [1999] 1 W.L.R. 1092, 1098 (Lord Hoffman)
\(^\text{20}\) Mahoney (n12) 888
\(^\text{21}\) Watson (n14)
partnership whose participants have voluntarily joined together for mutual business ends (and therefore must have some form of knowledge/dealing with each other previously).

The UK could be argued to favour the Contractarian viewpoint in modern UK law, evidenced by the dilution of the *ultra vires* principle. Prior to 1989 it was possible to argue that a company lacked the capacity to undertake a transaction, whereas since 1989 a third party acting in good faith has been protected from such a risk. Further, a company incorporated under the Companies Act 2006 no longer even requires to state its corporate objects.\(^{22}\) This is a victory for Contractarians as, from their viewpoint, a company should be able to do anything that its corporators at a given time wish it to. A State Gift advocate would instead limit a company’s capacity to acts within the purview of the reason it was granted separate legal personality (such advocate would believe that there are actions that should not be within a company’s capacity).

It has been argued that scholars tend to view corporate law as either a matter of public law or private law.\(^{23}\) This can also be viewed as an extension of the hybrid dimension of the corporate form. Corporations obviously have a quasi-public law link, as they only obtain their legal nature from the state, subject to whatever conditions the state deems fit. Partnerships, however, have a distinctly private law outlook as they are privately and voluntarily formed. These lines of reasoning can extend into a company’s capacity - if it obtains its personality by concession from the state then the actions that a company can undertake can be limited by the state as part of such gift, whereas if it obtains its personality by agreement between the corporators then there should be no limit on it undertaking any otherwise legal actions. The arguments outlined so far are actually false dichotomies: those envisioning a large company are more likely to see these issues as a matter for public law with its personality arising from the state

\(^{22}\) Eg Gower & Davies (n7) p167
and those envisioning a small company are more likely to see these issues as a matter for private law with its personality arising by way of contract.

2.1.2. AGENCY COSTS

Whichever theoretical and historical norms resulted in the creation of a separate legal personality for companies, a modern company is a new entity separate from all relevant constituents (its residual owners, its managers and those who interact with it). Jensen and Meckling stated that where:

“one or more persons (the principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent”

there arises a risk of self dealing on behalf of the agent. They define the costs incurred by the principal in minimising such self dealing as agency costs, and argue it is inevitable that such costs will arise for a modern company. For modern companies, these agency problems arise in three main areas:

(a) Conflicts between shareholders and managers

A 1932 publication by Adolf A. Berle and Gardiner Means reviewed the position for American public companies and concluded that the corporate form has created a “separation of ownership and control”, with dispersed shareholders with small stakes in the business delegating all powers to a centralised board of directors. Throughout this thesis, such a company shall be referred to as a "Berle/Means Company". Bainbridge states that this “creates the potential for shareholder and managerial interests to diverge”, going on to ask:

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25 Kraakman et al, (n8) p2
“Suppose the board of directors of Acme, Inc., is musing over the following question: “I can either spend $100 million on a new corporate jet or I can distribute the $100 million to the shareholders by increasing the size of the dividend.” Can anyone doubt that some board will buy the jet?”

Accordingly, costs in this category are those incurred by shareholders or the company in minimising self dealing by management.

Potential agency costs in this category are increased where there is a dispersed share ownership, no individual controlling shareholder and a large number of shareholders who are not directors. For close companies with a commonality of directors and shareholders, this category of agency costs are minimised.

Contractarians believe that shareholders are capable of protecting themselves via contracts. Accordingly, Contractarians have no issue with agreed agency costs in this area (for example high levels of executive remuneration) based on pre-set metrics. In other words, agency costs in this category which the shareholders have agreed will be acceptable to the Contractarians. Any self dealing outside of those agreed by shareholders, however, will be highly objectionable to Contractarians as it perverts the underlying corporate contracts. State Gift theorists are more likely to see a general need for protection against any agency costs by the state, as any agency cost will undermine the public reason for the corporation being allowed to exist. State Gift minded thinkers, however, will be less concerned by this particular category as they will expect shareholders’ interests to be compromised by management in certain situations (see discussion at paragraph 2.2.2 below).

(b) Conflicts between shareholders and other stakeholders

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Shareholders’ ability to direct the activities of the company (which is discussed more fully at section 2.2.1 below) risks agency costs arising between shareholders and other stakeholders. This is exacerbated by the presence of limited liability for the modern corporate form, which encourages more risky business ventures. The lack of recourse to shareholders in the event of insolvency means that shareholders get any upside but creditors “bear the risk of business failure”.

Accordingly, costs in this category are those incurred by other stakeholders or the company in minimising shareholders’ directing the company to maximise the return/value to the shareholders at the expense of other stakeholders.

State Gift thinkers will be particularly concerned about this category of agency costs, for reasons discussed in paragraph 2.2.2 below. Contractarians, however, are likely to be ambivalent on this category of agency costs because they assume that creditors price such a risk into interactions with the company. This is because the systemic risk to financial creditors of shareholder self-interest is well known and so this can be priced in to dealings with corporate actors. This analysis can be applied to any transactional counterparty of a company, as it is able to balance the importance of the interaction against the inherent risk in striking the bargain. Despite worries of imperfect information about specific corporate transactions, one of the effects of a company being generally required to include ‘limited’ in its name has the effect of ensuring that a voluntary stakeholder is aware of this risk.

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29 E.g. ibid 127
30 Companies Act 2006 ss58 and 59
(c) Conflicts among shareholders

Majority decision making by shareholders\textsuperscript{31} creates the possibility that majority shareholders will abuse their position to maximise their return from the company to the detriment of minority shareholders. This is exacerbated as shareholders owe no fiduciary duties to the company in respect of how they vote.\textsuperscript{32} In a UK context a minority shareholder retains protections from fraud by the majority,\textsuperscript{33} unfair prejudice in the running of a company\textsuperscript{34} and the ability to undertake a derivative action in the event that the actions of the majority shareholder has the possibility of being detrimental to the company as a whole.\textsuperscript{35}

2.1.3. HOW TO SOLVE AGENCY PROBLEMS

Having identified a key category of issues that arise in a corporate context, attention should be turned to the most efficient manner to resolve such issues. Cheffins has identified three types of rules that can be employed in general under corporate law, and especially to reduce agency costs. He identifies these as mandatory, permissive and presumptive (or default).\textsuperscript{36} Cheffins ultimately advocates utilising mandatory and permissive rules with caution.\textsuperscript{37}

Cheffins concludes that, in the ordinary course, rules should be default rules in the corporate sphere. It seems evident that a rule should only be default if it effects only those who can opt-out of the specific legal rule. If there are (and will always be) high negative effects to a third party then any

\begin{itemize}
  \item[31] E.g. ordinary resolutions require majority decision making, whilst special resolutions require 75\% to pass the resolution.
  \item[33] E.g., Atwood v Merryweather (1867) L.R. 5 Eq 464n.
  \item[34] Companies Act 2006 ss 994-999
  \item[35] Companies Act 2006 Part 11
  \item[36] Cheffins Theory (n28) 217 - 264, and also Jonathan Hardman 'Necessary and Balanced? Critical analysis of the Legal Writings (Counterparts and Delivery) (Scotland) Act 2015' 2016 (3) Juridical Review 177, 186-188
  \item[37] Cheffins Theory (n28) 249
\end{itemize}
prohibition on such course of action should be mandatory rather than default (as otherwise decision makers who only received an advantage from opting out would always opt out, leaving those who were harmed by the opt out entirely unprotected by a rule ostensibly protecting them). Those that should be able to opt out of a default rule should be those that it is designed to protect. Therefore default rules to protect shareholders should be able to be waived by the shareholders, but default rules designed to protect creditors should not – instead the creditors should be the only ones entitled to waive such default rule. It may prove impossible to identify all potential participants to such category, and will prove equally as difficult to allocate voting rights.\textsuperscript{38}

2.1.4. Conclusion

There remains an unresolved conflict on the fundamental theoretical basis for the existence of a company, which has arisen from historical uncertainty. The two sides of the debate are, however, beginning from slightly different assumptions about the entity that they are discussing. There has been a recent trend in corporate law towards maximising the freedom of the company in the UK, which would be more consistent with a Contractarian analysis of the basis for a company.

Agency costs are a commonly used corporate law analytical tool and will be vital for normative analysis of the Principle. Rules should be default and waivable by those who they are designed to protect. Any protections designed for third parties should, however, either be mandatory rules or only waivable by those third parties.

2.2. In whose interest should a company be run?

Whilst the theoretical origin of a company risks being unnecessarily abstract, the presence of this separate legal entity raises an evident

\textsuperscript{38} For example, tort victims may not be known. Even if they, it is difficult to quantify their claims to allocate voting (should a claim of £1,000,000 with a 10% chance of success carry the same weight as a £100,000 claim with a 100% chance of success? How would this be calculated?).
question: in whose interests should this entity be run? This has been described as the “Ends of Corporate Governance”39 (as opposed to the means of corporate governance which will be discussed below in this thesis). This may seem only relevant to director decision making and not shareholder decision making (which is the focus of this thesis). However, if a company should be run exclusively for the benefit of the shareholders, then it logically follows that such shareholders should have the maximum flexibility to control decision making by the company. They therefore should be entitled to instruct or override the directors and to do so with a level of formality that they decide amongst themselves. In other words, the Principle should be very strong if a company should be run exclusively for shareholders. If, however, a company should be run in the interests of other categories of actor then the shareholders should not exclusively have decision making rights in respect of the company and so the Principle should, normatively, be weak. This question has also been subject to some debate. There are two main schools of thought (with some variation within each such school), being those who believe in the Shareholder Value model40 and those who believe in the Stakeholder model. Taking these in turn:

2.2.1. SHAREHOLDER VALUE MODEL

This school holds that a company should be run almost exclusively in the interests of its shareholders. A company is seen as merely a “nexus of contracts”41- with the primary contract being with the shareholders who invest their capital into the firm. Shareholders have the residual value of the company. Whilst every other entity interacting with the company has a fixed claim against the company, shareholders are entitled to any upside that is left. Therefore, provided that the company is solvent, shareholders are the only party with a direct interest between a company making £5m profit and £10m profit. This means that shareholders are the only

39 Bainbridge (n27) 23
40 Sometimes called “Shareholder Primacy”. This definition, however, can also be used in respect of interaction between shareholders and directors. To avoid confusion, references to “Shareholder Primacy” will include not only primacy of shareholders over other stakeholders, but also primacy of shareholders over directors.
41 Jensen and Meckling (n24)
constituency who benefit from any increase in the marginal success of the company and therefore the appropriate guardians of its interests. This helps minimise agency costs, as directors are directly (and exclusively) acting as agents of the shareholders and are therefore directly accountable to them. Hansmann and Kraakman have suggested that this model has become the dominant normative global model. They cite as reasons for this the intellectual cohesion of the argument, the failure of all other models and pressures of global competition (when faced with a decision of which jurisdiction to invest in, a shareholder is likely to favour those jurisdictions which hold shareholder’s interests as paramount). This can be seen as an extension of Contractarian analysis - if the company is a private entity voluntarily created by the shareholders, then only the interests of those shareholders should be taken into account when deciding the actions of that company. It therefore agrees that other constituencies price any systemic risk into their interactions with the company.

2.2.2. Stakeholder Model

The Shareholder Value model is heavily criticised. Even Hansmann has noted that “there continues to emanate....a broad disquiet about the standard shareholder-orientated model”. Freeman has explained that pure Shareholder Value could require directors to undertake “actions which are immoral or unethical, as well as illegal”. Instead, he explains that companies have many stakeholders that should be taken into account in corporate decision making, including employees, customers, suppliers, environmentalists and shareholders, and that is the way to maximise the value of the firm. It has also been pointed out that Shareholder Value is incorrect on its fundamental assumptions - there are many involuntary

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creditors (e.g. tort victims) who are not able to price potential risks into their interactions with the company.\textsuperscript{46} Even if they were, the disparity of bargaining power and information would make such ability almost meaningless.\textsuperscript{47} Therefore in order to protect those who interact with the firm, the company must be managed in the interests of all of the stakeholders.\textsuperscript{48} Millon suggests that this can be achieved by expanding the category of actors to whom directors owe fiduciary duties to include stakeholders.\textsuperscript{49} Mitchell has stated this would more accurately and fairly reflect the impact that a company has in society:\textsuperscript{50} consider the disproportionate effect closing a plant has on a small town with no other employment - if an entire community can be decimated it does not seem equitable to only allow the interests of shareholders to be taken into account for such decision. Blair & Stout go even further and state that rather than a company using shareholder funds for profit, it receives specific investments from all constituents/stakeholders and that corporate activity is therefore a “team production”.\textsuperscript{51} It is not only shareholders that benefit from increased marginal profit from the firm - this may result in the hiring of extra employees, expanding operations, incurring or repaying credit. Blair and Stout demonstrate that allocating “ownership” to one member of the team results in less effort from both the owner (as they will own the fruits of the enterprise regardless of their input but require the input of others) and other constituencies (as they will not own the fruits of the enterprise regardless of their input). They therefore propose that the directors should be appointed by the various “team members” and that the role of the board should be to be a “mediating hierarchy” amongst the team members. This

\textsuperscript{48} L L Dallas ‘Working Towards a New Paradigm in Progressive Corporate Law’, in Mitchell ibid
\textsuperscript{49} See David Millon, ‘Communitarianism in Corporate Law: Foundations and Law Reform Strategies’ in Mitchell ibid. Fiduciary duties do not have to fully align to decision making powers, however as these tend to correlate it remains helpful analysis
\textsuperscript{51} Margaret M. Blair and Lynn A. Stout, ‘A Team Production Theory of Corporate Law’ (1999) (2)85 \textit{Virginia Law Review} 247
is a rejection of Contractarianism - a company is more than merely a private creation of shareholders; a belief that a company somehow has inherent additional responsibilities (a partnership or sole trader, for example, does not have to take into account the interests of their employees). This implies a more public element to the company than attaches to other forms of legal organisation, which echoes State Gift theory - if the Stakeholder model is not merely a continuation of the State Gift theory then it at least shares the same basis and utilises very similar arguments.

2.2.3. Evaluation of Stakeholder Theory

Advocates of the Stakeholder model usually start with a critique of Shareholder Value. Stakeholder arguments have their own weaknesses. Freeman’s arguments are a reason for management to ensure stakeholder happiness to maximise the value of the firm - which is achievable in a Shareholder Value model (and Freeman implies that its purpose is to maximise shareholder value). Freeman’s analysis is limited to a company’s “turbulent times” - even Shareholder Value advocates acknowledge that in such circumstances interests of creditors become superior to shareholder interests. Further, as discussed previously, voluntary creditors are able to price systemic risks of corporate form into such interactions. Lack of information or bargaining power is irrelevant - the risk applies to the entire corporate form. This analysis does not, of course, apply to involuntary creditors (eg tort victims). However, there are several points to note in this regard. Firstly, any involuntary interaction is unplanned and so would not have been avoided because of corporate form. This means that the relevant creditor could not chose which entity it wished to form this relationship with. As law recognises a limitation of liability through bankruptcy, any such risk would apply to every situation. In addition, the involuntary nature of the interaction means that the relevant parties (management,

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52 Freeman (n45) 3
53 Easterbrook and Fischel (n42) p69
54 E.g., if an individual’s car is hit by a bankrupt uninsured driver, they have no recourse for this involuntary interaction
shareholders and the stakeholder) may not be aware that the relationship has formed - given this uncertainty as to who falls into this category it is even more difficult to assign decision making rights to this category of actors.

Stakeholder theory asserts that stakeholders bear risks of company failure as well as shareholders and therefore stakeholders participate in the marginal risk of companies. However, it rarely deals with the principle underpinning of Shareholder Value - that, as residual claimants, shareholders are the only constituents whose interests are directly aligned with the company. This can be further seen as it is only the shareholders’ interests in the company that can be sold to a third party and which has a chance of appreciating in value. Increased success of the company may result in increased success for other stakeholders, but only shareholders have a marketable claim increased by the success of the company and therefore remain the only true residual claimants. All other stakeholders want to avoid a negative (a reduction in the recoverability of their claim) rather than actively seek a positive (the increase in the success of the company). It is therefore a fallacy to equate the interests of other stakeholders to the interests of shareholders. However, Kelly and Parkinson point out that income generated by a company for any specific act by an employee is theoretically variable but, in practice, is fixed by bargain as a wage. Replacing this fixed level of remuneration with a variable rate removes the argument of Shareholder Value theorists that shareholders’ interests are unique: this is a descriptive rather than a normative argument. There is, however, a normative explanation for stakeholders choosing to so structure their interactions with a company. To fully equate their interests with shareholders, a stakeholder would not just have to participate in marginal reward of a company’s

55 Choses in action in respect of torts and receivables can be sold, but these claims are for fixed, certain sums: the quantum of the claim will not appreciate with an increase in success of the firm.

success, they would also have to participate in the marginal risk of a company’s failure. Stakeholders may prefer to fix their returns from the company at a pre-agreed level for the purposes of certainty rather than participate in this risk. Stakeholder theorists falsely assume that adopting a stakeholder approach would automatically improve the position for stakeholders. Currently, each stakeholder other than shareholders has their interests protected by other aspects of the legal system. Insolvency law ensures that creditors recover before shareholders in insolvency, employment law protects employees, environmental law protects the environment, consumers have protections from consumer law, and so on. The only constituency without a direct legal protection is a community whose only plant is shutting. However, the community are only concerned that the plant remains open, not with the corporate form itself - if this asset is sold to a third party to continue then the community will be satisfied even if this results in the dissolution or insolvency of the company. These protections for other stakeholders exist because a form of shareholder value currently exists in the UK. Any attempt to include other stakeholders in corporate decision making reduces the rationale for them having such protections: if directors had to balance the interests of all stakeholders when making any decision, why should those constituents also enjoy their current legal protections? Instead their only protections would be to hope that the directors prioritised their interests, without recourse if they failed to do so having regard to the interests of all other stakeholders. This presents another frequent critique of the Stakeholder model - agency costs between directors and other stakeholders would increase without any certain remedy for any stakeholder.

Adopting the Stakeholder model will increase agency costs for the company and risk worsening stakeholders' protections without redress. Merely adding

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57 i.e. receiving more from the company should it perform well
58 i.e. receiving less from the company should it perform badly
59 Companies Act 2006 s 172 - directors should take into account various considerations when making decisions, including effects on stakeholders. However, this duty is owed to the company and a breach of this can be ratified by the shareholders normally. Despite appearing to provide stakeholder empowerment, the lack of a remedy means that this is a variation on Shareholder Value.
to the number of principals does not automatically increases agency costs. However, the more categories of principals that the same person is agent for, the harder it is to apportion decision making amongst the principals. The more heterogeneous the principals are, the less likely they are to have the same priorities and so there is an increased chance of conflicting instructions to the agent. Stakeholders are better relying on their existing legal protections rather than trying to amend corporate law, which may prejudice their existing rights.

There are two further points to make. Firstly, a Shareholder Value approach does not preclude entities being created to follow a Stakeholder model at the option of the shareholders. Those promoting new entities can create charities, co-operatives, mutual societies and friendly societies (all such stakeholder-centric entities will be known as “Alternative Structures” for the purposes of this thesis) if the shareholders so wish. Conversely, a legal system which adopts a Stakeholder approach must preclude a Shareholder Value company being established as the broad category of stakeholders that currently and in the future will exist includes those that cannot be known. If they cannot be known then they cannot agree to alienate rights. Finite, identifiable shareholders are clearly capable of alienating the rights which attach to shares they own: it is more difficult to conceive how a structure could waive decision making rights for future tort victims. Parallels abound to the theoretical categories identified - Contractarians see no issue in promoters creating Alternative Structures if that is what they have contracted to do. State Gift theorists believe the terms of any corporate vehicle to be established by the state, and therefore incapable of contractual variation. Secondly, empirically there has been a decline in

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60 (n38)
61 For discussion of Alternative Structures, see Jenny Harrow and Susan D. Phillips 'Corporate Governance and Nonprofits: Facing up to Hybridization and Homogenization' in Mike Wright, Donald S. Siegel, Keven Keasey and Igor Filatotchtchv (ed), The Oxford Handbook of Corporate Governance (OUP 2014)
Alternative Structures.\(^{62}\) This shows that, despite some hope of increased demand for a Stakeholder approach,\(^{63}\) this is not occurring in practice.

In conclusion, a company should be run in the interests of its shareholders with strong protections in other legal disciplines for its other stakeholders. The role of company law should be to facilitate a company being run in the interests of shareholders so long as so doing does not violate the legal protections that other stakeholders enjoy.

2.3. **How should a company organise its affairs?**

Having established that a company should be run for the interests of its shareholders, we now turn to which organs of the company should make decisions and how. Having dealt with the “ends”, we now examine the “means” of corporate governance.\(^{64}\)

If the company is run in the shareholders’ interests, then surely the shareholders are the best placed to direct the affairs of the company? This, however, is not generally seen to be the case. As noted at the start of this chapter, one of the fundamental basics of the company is that management is delegated by shareholders to directors/management. It is often impractical for shareholders to take a daily interest in the activities of the company so most articles of association delegate management of the company to the directors.\(^{65}\) Cheffins states:

“*[t]he almost universal practice is for a company’s articles of association to endow the directors with the power to manage the company.*”\(^{66}\)


\(^{63}\) E.g. J. Armour, S. Deakin and S. Konzelmann ‘Shareholder Primacy and the Trajectory of UK Corporate Governance (2003) 41 *British Journal of Industrial Relations* 531

\(^{64}\) Bainbridge (n27) 23

\(^{65}\) E.g. Model Articles for Private Companies limited by shares Art 3

\(^{66}\) Cheffins Theory (n28) 603
The efficiency savings of such delegation outweigh its agency costs.\textsuperscript{67} For publicly traded companies, the speed of potential changes to shareholdings make it impractical for the shareholders of a company to have any active role in the business of the company. Bainbridge states that, normatively, the shareholders of a company should not be involved in the management of a company. Bainbridge draws on Arrow’s analysis that an organisation has to be either run consensually or by imposition of authority.\textsuperscript{68} Having seen that consensus is impossible, Bainbridge argues that the only entity which can provide authority is the board. He also draws on Berle & Means to highlight that shareholders may have a rational apathy as to how a company is run and so should not be involved in the management of the company. Having seen empirical issues with stakeholders being able to influence appointment of directors, Bainbridge concludes that corporate law should (and does) embody “director primacy” with the directors being the main constituency in a company. He therefore takes issue with Blair & Stout’s theory of the company as a matter of “team production” on two grounds - firstly the interests of the company should be wealth maximisation for the shareholders, and secondly (and more importantly) the board of directors “hires the factors of production, not the other way around”\textsuperscript{69} so the directors cannot be said to be accountable to the relevant factors of production that they will pick.

Bainbridge’s analysis has a few weaknesses. Firstly, it is based on specific elements of US law which are not replicated in the UK. Section 141(a) of the Delaware General Corporation Law provides that the company shall be run by the directors. In the UK there is no equivalent general statement of the law, merely the model articles (and previously Table A) which empower the directors to manage the company: the UK adopts a default rule on the subject. It has been argued that the UK position is an anomaly.\textsuperscript{70} Bainbridge’s analysis is based on a classic Berle/Means Company with its

\textsuperscript{67} Easterbrook and Fischel (n42) 4 - 8
\textsuperscript{68} Kenneth J Arrow, The Limits of Organisation (Norton, 1974)
\textsuperscript{69} Bainbridge (n27) 63
\textsuperscript{70} Watson (n14) footnote 94
wide shareholder base. He acknowledges that claims to director primacy “fare poorly whenever there is a dominant shareholder” where there is a lower risk of shareholder and the dominant shareholder has control over the board. Accordingly, the argument that the board of directors should control the activities of the company is limited to situations where the shareholders are unable to do so. It is implicit in Bainbridge’s analysis that shareholders should make decisions and only when they cannot (which will be the normal position) does the primacy of directors arise. Given that the legal norms in question must cover the entire spectrum from Berle/Means Companies to closely held companies, management by directors should be the default position, with shareholders being able to opt out should they see fit. This is the position that we have in the UK: directors obtain their power from the articles which can be amended by the shareholders. Directors have ostensible authority to bind the company so that third parties do not need to examine the chains of authority when contracting with a company.  

2.4. Formality of Decision Making

The next issue to discuss must be the level of formality that decision making should take.

The traditional method to make decisions by any organ of the company has been for that organ to hold a meeting of its members. For shareholders, this is known as a general meeting. Decision making by meeting is important because it gives the decision makers an opportunity to deliberate on a specific topic. As Simmonds stated:

“It is plausible to suppose that such confrontation and collective deliberation opportunities would enhance the voting decision.”

71 Bainbridge (n27) 12
72 Gower and Davies (n7) 175
73 Gower and Davies (n7) 436
74 R Simmonds, ‘Why must we meet? Thinking about why shareholders meetings are required’ (2001) 19 Company and Securities Law Journal 506
In a shareholder context, if a company wrote to each shareholder for agreement on a matter, that would separate the shareholders from each other. This creates a power disparity between the board of directors (one unified body) and the general meeting (acting by each individual shareholder). The options presented to each shareholder are merely to assent or dissent, without any insight into the views of the other shareholders. By contrast, a properly convened meeting has the opportunity to discuss, debate, reason and actively chose other courses of action. This analysis assumes that a formal meeting is the only opportunity for discussion; without a meeting the participants would have little information and little opportunity to deliberate. It presupposes that there is a separation between the ownership and control of the company. Boros summarises that the purpose a meeting (especially shareholder meeting) is to hold the relevant managers accountable.\textsuperscript{75} Shareholder meetings act as an opportunity to reduce agency costs between shareholders and directors. It follows that shareholders meetings are more important when there is higher risk of agency costs between shareholders and directors. We have seen above that these agency costs are likely to be higher in a Berle/Means Company with a strong separation of ownership and control, so there is a higher requirement for formality in decision making when shareholders are less able to act in concert. The argument for formality in decision making is stronger in larger companies with more shareholders. This is an extension of the debate outlined above as to which organ of the company should make decisions. In deciding both issues, there are different considerations between Berle/Means Companies and closely held companies. In the former, there is more of a need to empower the directors in order to maximise the value to the shareholders, but in order to protect shareholders from the directors there is a need for increased formality in shareholder decision making. Conversely, in the latter the shareholders have no need for such protection, and so a reduced need for formality. In line with the conclusion as to which organ of the company make decisions, the default position

\textsuperscript{75} Elizabeth Boros, ‘Corporate Governance in Cyberspace: Who stands to gain what from the virtual meeting?’ (2003) 3 Journal of Corporate Legal Studies 149,162 - 164
should be towards formality unless waived by the shareholders. Such waiver should be able to be undertaken informally by the shareholders if they so wish.

This analysis extends beyond agency costs between shareholders and managers. The same issues arise where there is a disparity of power between principals. Accordingly, the argument for formality in decision making amongst shareholders is stronger when there is a dominant but not sole shareholder (creating minority shareholders who require to monitor the actions of the dominant majority shareholders). Any requirement for shareholders to act unanimously in waiving a default rule removes these risks for minority shareholders and therefore removes the requirement for formality. Similar analysis applies to the external dealings of a company: its interaction with other stakeholders. We have seen little value in any other stakeholder's claim to participate in general decision-making by a company, but that they do have a right to ensure that their interests are protected, so this agency cost analysis is applies to them as well. Whilst stakeholders do not have a normative claim to participate in decision making by a company, they do have a right to certainty in their interaction with such company in order that they can price any risk into their interactions. Stakeholders should thus be protected where formality has been waived by the shareholders. Stakeholders should be able to rely upon the ostensible authority of directors to bind the company, but also of the shareholders actual authority as the ultimate decision makers in respect of the company when they purport to exercise such. The absence of such reliance would mean that stakeholders would have a strong argument to insist upon formality in decision making so that they can follow the clear decision making chain of the company and ensure that the company is bound. Stakeholders should be entitled to rely on a decision by the shareholders to waive their requirement for formality. In any rule as to formality in either shareholder or director decision making which is designed to protect stakeholders from the decisions or actions of shareholders or the company must be a mandatory rule in order to avoid the purpose of the rule
being undermined. In conclusion, a rule designed to protect shareholders (either from each other or from the directors of a company) should be a default rule which can be waived by the shareholders acting unanimously, whereas any company law rule designed to protect third parties should be a mandatory rule in order to protect them from decisions made by the shareholders. This oversimplifies matters considerably as it assumes that the shareholders are a homogenous class whose interests will be directly aligned. This is not normally the case and accordingly it is necessary to explore how shareholders usually make decisions.

2.5. **Majority Rule in Shareholder Decision Making**

As discussed in paragraph 2.3, decisions must be made either by consensus or by authority- in the case of shareholder decision making, authority is achieved by majority. Decision making by majority\(^76\) presupposes that it is too expensive or impractical to achieve consensus on any particular subject. Authority is only required in a corporate setting if consensus is not achievable. As we have discussed, shareholders have a strong claim to be the ultimate decision makers in the actions of a company. The way that shareholders create authority amongst themselves is therefore by adopting an approach of majority rule. Consensus overrides and fits within these structures as a resolution passed by all of the shareholders is equally as valid for these purposes.

If shareholders were obliged to consider the interests of others when casting their vote then there may be little further to be said on the matter. However, shareholders are able to cast their votes however they see fit.\(^77\) As shareholders are the constituents who should retain residual control over a company to direct its affairs, this causes a strong risk of the agency costs outlined at paragraph 2.1.2(c) above arising. We have seen that formality in decision making is primarily a method to reduce agency costs. Therefore, in respect of the agency costs listed in paragraph 2.1.2(c) above, formality

\(^76\) See Bainbridge (n27) 37
\(^77\) (n32)
requires to be observed. Similarly, if majority rule is adopted by shareholders when waiving formality, then agency costs may arise. Accordingly, any act to waive formality by shareholders must be a unanimous decision and cannot be a majority decision. Any operation of the Principle must be unanimous by the shareholders.

This of course does not preclude a majority from estopping themselves from complaining about a certain course of action if they have informally agreed to it. However, this should only estop them personally and will not extend to binding the shareholders as a whole. As no decision of the shareholders generally can be said to have been made, it therefore follows that the estoppel will not extend to any transferee.\(^7\)

2.6. **Conclusion**

The normative root of a modern company is not clear, which in turn produces different arguments as to who the modern company should be run in the interests of. We have seen, however, that the arguments for a company being run exclusively in the interests of the shareholders remain the strongest. Regardless of this, other stakeholders should have protections against the actions of a modern company as provided for by other areas of law. Seen in this light, the role of corporate law must be to facilitate the advancement of shareholder interests unless they impinge upon protected interests of other stakeholders, in which case corporate law should prevent the company undertaking such a course of action.

Arguments in favour of mandatory delegation by shareholders in favour of a board of directors are fundamentally arguments of convenience. Accordingly, where it is practical for them to do so, there is no reason why shareholders should not retain the ability to direct the management of the company. Formality is only required in order to protect shareholder interests from increased agency costs - i.e. in situations that shareholders

\(^7\)However, decisions shareholders bind their successors. Accordingly, any unanimous decision of the shareholders in such circumstances should bind on future transferees.
are practically incapable or unwilling to participate in management themselves and to protect minority shareholders from oppression by majority shareholders.

Any requirements as to decision making being made by the board and/or being made through any specific procedure must be normatively seen as optional on shareholders and therefore waivable by them. The only situations where shareholders as a whole should not be able to do this are those in which a third party stakeholder has a legal protection against a company - in these situations the company (acting through any organ) should not be able to violate the rights of such stakeholder. Therefore rules designed to protect shareholders should be default rules, whereas rules designed to protect third parties should be mandatory rules. There should be some restrictions on the right to waive any requirements as to formality: shareholders should only be able to waive such rights unanimously (to prevent agency risks for minority shareholders) and third parties should be entitled to rely upon such waiver of default formal channels and be certain that rules designed to protect them will not be given away by disinterested shareholders.

This is key for analysing how the Principle fits into the normative background of company law. To do so, we should observe the following:

1. any rule, whether a rule of substance or procedure, which exists solely for the benefit of shareholders as a whole should be a default rule which can be waived by action of the shareholders as a whole. Therefore the Principle should apply to rules which only exist for the benefit of the shareholders or company;

2. the Principle should require unanimous action of shareholders to avoid the risk of agency costs/oppression of a minority of shareholders by the majority. The Principle therefore should
derogue from the usual position of majority rule for decision making by shareholders;

3. non-shareholder stakeholders should be able to argue that the Principle applied if all of the shareholders have acted in a way which made such stakeholders believe that the usual default rule has been waived. Shareholders should not be able to rely on internal formality that they have ignored in order to avoid a form of action that they consented or acquiesced to. This approach also opens the possibility for third parties to use the Principle as a way to enforce decisions of all of the shareholders against a specific company; and

4. any rule, whether a rule of substance or procedure, which exists for the benefit of creditors should either be a default rule which can be waived by them (which would take such a rule outside the scope of this thesis) or be a mandatory rule. Therefore the Principle should not apply to situations where a rule is designed to protect non-shareholder stakeholders,

in other words, the Principle should be objectively applied, require unanimity of shareholders and should be able to apply in every circumstance of corporate decision making other than in respect of rules which are designed for the protection of other parties than shareholders.

2.7. LAW AND EQUITY

English law has historically recognised a difference between the common law and equity; a difference between principles of substantive rules and ensuring that those rules are applied equitably. In England two parallel sets of courts developed, one for the law and one for equitable principles,
which were only unified into one unified judicial system by the Judicature Acts 1873 and 1875.\textsuperscript{80} It has been said that:

"In its most general sense, equity refers to a conception of justice that transcends the substantive and procedural rules of the positive law."\textsuperscript{81}

Over time, this "came to mean an ethical standard that the defendant would be held to when he enforced his common law rights."\textsuperscript{82} Ultimately, if there was a conflict between the common law and equity, the rules of equity are to prevail.\textsuperscript{83} Equity can thus be seen as a "gloss" on the law.\textsuperscript{84} It has been used to over-ride any lack of formality required by the common law.\textsuperscript{85} Whilst there are several maxims and doctrines of equity that survive today, the most relevant for examination of the Principle is that "equity looks to the intent rather than the form".\textsuperscript{86} Thus the opinion has been advanced that:

"Courts of Equity make a distinction in all cases between that which is matter of substance and that which is matter of form; and if it finds that by insisting on the form, the substance will be defeated, it holds it to be inequitable to allow a person to insist on such form, and thereby defeat the substance."\textsuperscript{87}

It should be noted that, should a court apply an equitable remedy, this does not mean that the formalities will necessarily be deemed to be complied with, but instead the court could find an equivalent remedy for the relevant party.\textsuperscript{88} It should also be noted that Scots law does not acknowledge the

\textsuperscript{80} For an overview of the history of equity under English law, see Snell, ibid paras 1-006 - 1-107
\textsuperscript{81} Snell, ibid, para 1-002
\textsuperscript{82} Snell, ibid, para 1-009.
\textsuperscript{83} Supreme Court of Judicature Act 1873 s25(11)
\textsuperscript{84} A H Chaytor and W J Whittaker (ed) F W Maitland, Equity also the Forms of Action at Common Law: Two Courses of Lectures (CUP 1929) 18
\textsuperscript{85} Eg Berry v Berry [1929] 2 K.B. 316 - a husband and wife entered into an English deed of separation. Under English law, a deed can only be varied by another deed yet the court upheld an informal variation on equitable grounds: the variation reduced the allowance due to the wife, and she sued to try to obtain the initial, higher amount
\textsuperscript{86} Snell (n79) para 5-013
\textsuperscript{87} Parkin v Thorold (1852) 16 Beav. 59, 66-67
\textsuperscript{88} Snell (n79) para 5-014
concept of "equity", however frequently uses its own routes to achieve a similar end.\textsuperscript{89}

\textsuperscript{89} Eg George L Gretton, 'Trusts without Equity' (2000) 49(3) The International and Comparative Law Quarterly 599
3. HISTORY OF THE PRINCIPLE UNDER UK LAW

Having reviewed the normative basis for a company and corporate governance, it is necessary to examine the history and development of the Principle as applied by the UK courts.

3.1. ORIGINS: SALOMON?

As with much modern company law, the Principle appears first in *Salomon v Salomon & Co.* This case not only established the concept of the veil of incorporation, but according to Grantham laid the foundations for the Principle. The facts of *Salomon* are very well rehearsed. Aron Salomon was a sole trader who sold his business to a private limited company. This new company was incorporated under the Companies Act 1862, which required that there be at least 7 shareholders of any company. It was incorporated with an authorised share capital of 40,000 shares of 1l each, of which 20,007 were ultimately issued. Aron Salomon held 20,001 shares himself, with each of "his wife, a daughter, and four sons, each of them subscribing for one share". The vast majority of voting, control and economic rights were held by one individual, being the individual who sold the business to such company in the first instance. The business faced financial difficulties, became insolvent and entered liquidation. The assets of the company were insufficient to meet all the ordinary creditors of the company in full, but there were sufficient assets to meet secured creditors in full (including Aron Salomon, who held various debentures issued by the company). The matter before the House of Lords was whether the company was a true company or whether its incorporation was a:

"*mere scheme to enable [Aron Salomon] to carry on business in the name of a company with limited liability.*"
The 1890s was a fertile time for the development of company law in the UK. Parliament had commissioned a committee lead by Lord Davey (the “Davey Committee”) which issued a report (the “Davey Report”). The Davey Committee noted the tendency for established businesses of sole traders or partnerships to be incorporated into companies, both in positions of good faith and in situations of “the eve of bankruptcy”. The Davey Committee recommended that the law did not need to be updated. However, they only did so on the basis of the Salomon judgments that had been delivered up to the Davey Report, being up to the Court of Appeal. The Court of Appeal in the Salomon case held that “incorporation would be upheld unless a company was established for an illegitimate purpose”, and that the company in Salomon had been created for an illegitimate purpose, being to ensure that Aron Salomon was not personally liable for the debts of the business. At the time that the Davey Committee was deliberating, it was presumed that the courts would hold a company as not validly incorporated if it was only incorporated to take advantage of the protections of limited liability for shareholders. Watson hints that the Davey Committee and the Court of Appeal in Salomon represent good examples of State Gift theory, as the state is enquiring into the purposes of a particular company and establishing whether to approve it. The Davey Committee stated: “It is further suggested that persons conspiring to defraud by means of such devices as described in Aron Salomon’s case are amenable to the criminal law”. The Davey Report recommended that, for the first time under UK corporate law, protections be introduced for creditors against fraudulent preferences and disposals. It is clear that the Davey Committee believed that the transactions in Salomon would fall within these categories of challengeable transaction. So when the Davey Committee:

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97 Report of the Departmental Committee appointed by the Board of Trade to inquire what amendments are necessary in the acts relating to joint stock companies incorporated with limited liability under the Companies Acts 1862 to 1890, 1895 Command Paper c.7779
98 Davey Report, ibid, paragraph 12
99 Davey Report, ibid, paragraph 16
100 Broderip v Salomon, [1895] 2 Ch. 323
101 Watson (n14) 134
102 Davey Report (n97) paragraph 19
103 Davey Report (n97) paragraph 33
“dismissed from their consideration every suggestion for a public inquiry by the registrar or other official authority into the soundness, good faith, and prospects of the undertaking at this or any other stage of a company’s formation”,

ey they did so because such inquiry was unnecessary: the court would ultimately fulfil this role, as in the *Salomon* case so far. In the mid 1890s State Gift theory was dominant, but the courts were already fulfilling the role of the state in examining whether companies were legitimate or not. If the courts were not fulfilling such a role, the Davey Report recommendations may well have been different and legislative change may have been proposed to re-inforce the State Gift nature of a company. Indeed, Watson suggests that:

“Part of the sanguinity of the Davey Committee may have been brought about by a belief that the Court of Appeal judgments in *Salomon* would not be overturned by the House of Lords. Indeed the Committee appended the judgments of the Court of Appeal to the Report. The Davey Committee therefore clearly endorsed Lord Lindley’s view in the Court of Appeal in *Salomon* that incorporation would be upheld unless a company was established for an illegitimate purpose.”

If courts kept doing so, this would in turn increase the ability for creditors to challenge the actions of a company and result in shareholders being personally liable for the debts of the company, which would undermine shareholders; claim to be the supreme constituency of a company, thus limiting the application of the Principle. The “illegitimate purposes” that the *Salomon* company was established for was considered by the Davey Committee and Court of Appeal to be utilising limited liability to avoid personal liability for the dominant shareholder.

Their lordships, however, threw aside this entire conceptual framework and held that the company was duly formed and that, being solvent at the time

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104 Davey Report (n97) paragraph 42  
105 Watson (n14)134
that it acquired the business for good value, there was no basis on which to hold Aron Salomon as personally liable for the debts of the company. The Davey Report conclusion that no state entity needed to inquire into the good faith purposes of the establishment of a close company was predicated on the fact that this was unnecessary as the court (ie a public body) was already doing so. Therefore, by their lordships deciding that this was not a decision for the court, they removed the court from performing this role just after a serious opportunity to strengthen the role of the state was rejected as not being necessary: the House of Lords collapsed the State Gift edifice of the 1890s. By arguing that, effectively, all creditors of the Salomon company knew that it was a limited liability company and therefore incorporating to utilise limited liability could not be held to be an improper purpose,\textsuperscript{106} they reduced the state’s ability to regulate the purposes for which companies are established, other than in cases such as fraud or other pure criminal conduct. As State Gift theory relies on an argument that the state should regulate the purposes of companies, \textit{Salomon} provided a strong victory to Contractarians. Further, by narrowing the circumstances in which creditors are able to challenge actions of companies when dealing with shareholders, the House of Lords provided a victory to Shareholder Value theorists and, in turn Shareholder Primacy thinkers. Therefore \textit{Salomon} laid the groundwork for strong and widespread application of the Principle.

Grantham cites the judicial history of the Principle as originating from the dictum of Lord Davey\textsuperscript{107} in \textit{Salomon}:

\begin{quote}
"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."\textsuperscript{108}
\end{quote}

This formulation is wide and purports to provide the members acting unanimously the power to make decisions they would not be able to in

\begin{footnotes}
\footnotetext[106]{\textit{Salomon} HL (n90) 27}
\footnotetext[107]{Grantham (n1) 246}
\footnotetext[108]{\textit{Salomon} HL (n90) 57}
\end{footnotes}
general meeting (for example, in respect of powers expressly delegated to the board of directors in the articles). This is a Contractarian analysis, as it acknowledges that shareholders can vary the underlying corporate contract and removes any role for the state other than in setting the boundaries for *intra vires* actions (which their lordships set very widely). It was a victory for Shareholder Primacy as it enabled the shareholders to bind the company entirely. Based on this isolated quote alone the Principle should have almost universal application so long as the company is able to undertake the action that the shareholders wish.

The phrase "from the circumstances of the case", however, may mean that Lord Davey did not intend to make a fundamental statement about the law in general, but instead limited his analysis to the individual circumstances, where there was commonality between directors and shareholders and Aron Salomon made decisions. 109 This thesis has explained different agency costs and protections arise between Berle/Means Companies and closely held companies. It is no surprise that, when dealing with close companies, a more Contractarian line of reasoning is followed.

Grantham suggests that *Salomon* was a "fundamental paradigm shift" 110 as this decision "radically reformulated the corporate concept", 111 as prior to *Salomon*, "genuine partnership was, therefore, a prerequisite to incorporation, both legally and historically", 112 whereas this changed by the House of Lords holding that a company was valid where only one individual was an "active participant". 113 Grantham cites Sir Frederick Pollock, who at the time of *Salomon* opined that when the drafters of the relevant legislation:

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109 Ellis (n4) 260
111 ibid
112 ibid. This thesis views company law as a hybrid between partnership law and the law of Corporations
113 ibid
“spoke of seven or more persons being ‘associated’, they meant such an association as, without the help of the statute, would have made those persons members of an ordinary partnership.”  

Granthon and Pollock’s analysis is that the Salomon arrangements would not have been a valid ordinary partnership (if purporting to be so), and so the court changed what would be held to be a valid company by the Salomon ruling. The offending elements of the Salomon arrangements appear to be the unequal distribution of profit and voting rights, and that several of the shareholders were effectively silent partners who were not involved in the running of the business. However, neither of these is fatal to the constitution of an ordinary partnership. The definition of a partnership under the Partnership Act of 1890 is:

“the relation which subsists between persons carrying on a business in common with a view of profit.”

There is no requirement for an equal share of profits, in fact it is uncertain whether a division of profits is required at all to constitute a partnership, and courts have expressly acknowledged that dormant partners still qualify as partners. Accordingly the Salomon relationship would have constituted a valid partnership if it purported to be such, and therefore the importance of the Salomon decision was to provide a victory for Contractarians over State Gift theorists. This had several linked effects – as well as strengthening, ultimately, the position of shareholders within the company, we have seen that Contractarians look to partnership law for the basis of companies. Accordingly, the House of Lords in Salomon provides a boost to those who believe that company law, including corporate decision making, evolved from the private law of partnerships.

114 (1897) 13 L.Q.R. 6, 6-7, as discussed in ibid
115 Partnership Act 1890 s1(1)
116 R.C. I’anson Banks (ed) Lindley & Banks on Partnership (18th edn, Sweet and Maxwell, 2002) paragraph 2-10, although Sir Frederick Pollock disagreed with this analysis (as discussed within)
117 Cox v. Hickman (1860) 8 H.L.Cas. 268; ibid para 2-05
The Partnership Act 1890 provided a set of default provisions, and it remains usual for partnerships to enter into agreements to vary these rules.\textsuperscript{118} The Partnership Act states:

"the mutual rights and duties of partners, whether ascertained by agreement or defined by this Act, may be varied by the consent of all the partners, and such consent may be either express or inferred from a course of dealing."\textsuperscript{119}

In respect of this provision, Lindley & Banks state "it goes without saying that no variation will be effective if consent of all the partners is not forthcoming."\textsuperscript{120} It is arguable that the Principle shares at least a common root with this provision; the concept of those who contribute equity capital to a business venture unanimously deciding a course of action, and such course of action binding that business venture.

The rationale for the Principle being strong is clear cut for partnerships. In a partnership, each partner is under joint unlimited liability for the debts of the partnership,\textsuperscript{121} the firm itself has no separate legal personality unless located in Scotland\textsuperscript{122} and there are general fiduciary duties owed by partners to the partnership.\textsuperscript{123} Whilst individual partners risk agency costs from the actions of their partners, the unity of management with equity contributors mean that the risk of self dealing by management is removed. Similarly, any third party interacting with the partnership has recourse to the personal assets of all partners. Ownership and control vest in the same people for partnerships, whereas in companies ownership is vested in the shareholders whereas control is vested in the directors.\textsuperscript{124} The analysis in \textit{Salomon} is slightly confused by the fact that the position of the board of directors was unclear. Lord Watson stated that despite averments to the contrary:

\textsuperscript{118} For example, see Lindley (n116) chapter 10
\textsuperscript{119} Partnership Act 1890, s19
\textsuperscript{120} Lindley (n116) para 10-12
\textsuperscript{121} Partnership Act 1890, s9
\textsuperscript{122} Partnership Act 1890, s4(2)
\textsuperscript{123} eg Blisset v Daniel (1853) 10 Hare 493
\textsuperscript{124} Berle & Means (n26) 250
“No evidence was led tending to support the allegation that no board of directors was ever appointed, or that the board consisted entirely of the appellant”\textsuperscript{125}

It is unclear whether \textit{Salomon} would have resulted in the same outcome (or contain such wide-ranging statements of law) if a board of directors existed yet were not consulted in respect of the transactions in question.

\textit{Salomon} demonstrates a fundamental shift in the characteristics of a company. By providing victory to Contractarians and in turn Shareholder Primacists, the Principle should have strong and universal application. However, it is unclear whether the dictum by Lord Davey was intended for universal application or whether it was limited to the specific facts. Whilst all parties agreed that the key corporate actor in this situation was Aron Salomon, it remains unclear in what capacity his dominance arises—he was dominant shareholder, secured creditor and possibly a director of the company. Accordingly, whilst \textit{Salomon} creates a useful starting point for the application of the Principle, it raises as many questions as it provides answers.

3.2. \textbf{EARLY DEVELOPMENT - A ROCKY ROAD}

Initially, it was unclear whether Lord Davey's dictum in \textit{Salomon} would be considered to be a general statement of law, or whether it was more likely that \textit{Salomon} would be considered as fact specific and an alternative line of analysis followed. The case of \textit{In Re George Newman & Co}\textsuperscript{126} involved a company which acquired the assets of a builder (George Newman) and gave "presents"\textsuperscript{127} to its chairman (the same George Newman) using funds it had borrowed at a time when it was insolvent, and it subsequently entered liquidation proceedings. The presents were approved by all directors and all shareholders, but the liquidator sought recovery of the presents (amongst

\textsuperscript{125} Salomon HL (n90) 25
\textsuperscript{126} In Re George Newman & Co [1895] 1 Ch. 674
\textsuperscript{127} Ibid, 684 (Lindley LJ)
other payments) from George Newman on the grounds that transferring the funds was an *ultra vires* act, and accordingly the shareholders could not ratify it.\(^ {128}\) Lindley L.J. agreed, stating:

"The shareholders, at a meeting duly convened for the purpose, can, if they think proper, remunerate directors for their trouble or make presents to them for their services out of assets properly divisible amongst the shareholders themselves. Further, if the company is a going concern, the majority can bind the minority in such a matter as this. But to make presents out of profits is one thing and to make them out of capital or out of money borrowed by the company is a very different matter. Such money cannot be lawfully divided amongst the shareholders themselves, nor can it be given away by them for nothing to their directors so as to bind the company in its corporate capacity."\(^ {129}\)

Lindley L.J. views the ‘presents’ as maintenance of capital issue, notwithstanding that the ‘presents’ were made to directors, and so required restitution by George Newman for this alone. However, he went on to state:

"But even if the shareholders in general meeting could have sanctioned the making of these presents, no general meeting to consider the subject was ever held. It may be true, and probably is true, that a meeting, if held, would have done anything which Mr. George Newman desired; but this is pure speculation, and the liquidator, as representing the company in its corporate capacity, is entitled to insist upon and to have the benefit of the fact that even if a general meeting could have sanctioned what was done, such sanction was never obtained. Individual assents given separately may preclude those who give them from complaining of what they have sanctioned; but for the purpose of binding a company in its corporate capacity individual assents given separately are not equivalent to the assent of a meeting. The company is entitled to the protection afforded by a duly convened meeting, and by a resolution properly considered and carried and duly recorded."\(^ {130}\)

Even if the specific facts of George Newman were *intra vires*, Lindley L.J. would still not hold that the presents were valid. Implicit within this reasoning is a separation between merely giving assent and giving

\(^ {128}\) Ibid, 680
\(^ {129}\) Ibid 686
\(^ {130}\) Ibid
considered agreement to a provision. This is the first case to reject the Principle and did so because of a mandatory rule for formality. It is implicit that rejecting the application of the Principle may not necessarily be a bad thing for shareholders, as requiring debate may empower them. Accordingly, for Lindley L.J., the only application of the Principle was to estop any individual shareholder who had given their consent from "complaining what they have sanctioned", but the assent of all shareholders could never equate to a decision taken at a general meeting. Lindley L.J. focuses on the rights of a liquidator to rely on formality, which is valid because the company was insolvent at the time that the "presents" were given, and therefore the interests of the company ceased to be solely those of the shareholders.

Whilst the outcome in *Salomon* and *George Newman* was different, there is consistency in the underlying reasoning - a form of Shareholder Primacy: *Salomon* by the court refusing to review the underlying decision made by the shareholders, and *George Newman* by using formality to defend the rights of minority shareholders. *Salomon* was decided by the House of Lords after *George Newman*, and therefore on issues which overlap the two cases, *Salomon* is binding.

In *In re Express Engineering Works, Limited*¹²² it was argued that *George Newman* meant that "[f]or the purpose of binding a company in its corporate capacity the mere individual assent of the corporators does not take the place of a resolution properly passed at a duly constituted meeting".¹³³ Lord Sterndale held that there had been a meeting of all shareholders, albeit that it purported to be a board meeting as there was commonality between shareholders and directors, and that this would have been a valid general meeting if purported to be such. Accordingly, following Lord Davey's dictum, the Principle must apply.¹³⁴ Younger L.J. went further:

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¹³¹ Ibid
¹³² *In re Express Engineering Works, Limited*, [1920] 1 Ch. 466
¹³³ Ibid 468
¹³⁴ Ibid 470
"I agree with the view that when all the shareholders of a company are present at a meeting that becomes a general meeting and there is no necessity for any further formality to be observed to make it so. In my opinion the true view is that if you have all the shareholders present, then all the requirements in connection with a meeting of the company are observed."\(^{135}\)

Express Engineering has been cited\(^ {136}\) as establishing the primacy of the Salomon dicta over the George Newman position, but this quote is of greater significance. The three cases cited so far all involved liquidators challenging transactions that close companies unanimously resolved to do - the shareholders themselves were those arguing that the Principle should apply, albeit often in different capacities to avoid personal liability. Younger L.J.'s dictum is not that when all shareholders are together it is open to them to argue that they are meeting as a general meeting, but rather their assembly automatically becomes so. Accordingly, despite superficially empowering shareholders by avoiding the claims of the liquidator, this is the start of a line of analysis which results in the Principle being used against shareholders as well as by them. Express Engineering still required a meeting, which remained the case until Parker & Cooper, Limited v Reading.\(^ {137}\) In this case, debentures had been issued to a shareholder in exchange for the provision of funding. After the Company went into liquidation, the liquidator raised proceedings to set the debentures aside for lack of adherence to procedural formalities. Astbury J. characterised the case as follows:

"The company had the benefit of the money. The debenture was issued with the assent of every shareholder, and the question is whether the plaintiffs, or rather the liquidator, ought to succeed in obtaining a declaration that the debenture and the resolution authorizing it were inoperative and invalid, so that the creditors may get the advantage of the defendant Reading's 1750l. and deprive him of the security on which he made that advance."

\(^{135}\) Ibid 471
\(^{136}\) E.g. Ellis (n4) 60
\(^{137}\) Parker & Cooper, Limited v Reading [1926] Ch. 975
 Unless I am bound by authority to give this relief I certainly do not propose to do so.”

Astbury J. only intended to hold that the debentures were not valid if faced with no other possibility. He then considered Salomon, George Newman and Express Engineering, before concluding that:

"I cannot think that they came to their decision because the five shareholders happened to meet together in one room or one place, as distinct from agreeing to the transaction inter se in such manner as they thought fit... where the transaction is intra vires and honest, and especially if it is for the benefit of the company, it cannot be upset if the assent of all the corporators is given to it. I do not think it matters in the least whether that assent is given at different times or simultaneously.”

This meant that the debentures granted in exchange for a bona fide injection of funds were validly granted. Given Astbury J.'s earlier position, this is unsurprising. When coupled with Express Engineering, however, this created a potentially dangerous position for shareholders. Whilst their ability to direct the actions of the company informally was increased, so was the risk that they could accidentally do so. Not only was it held (in Express Engineering) that whenever shareholders meet in any capacity it is always a shareholders meeting, following Parker & Cooper v Reading they did not even meet to do so. This risks shareholders being retrospectively held to have agreed to a course of action that a company takes without realising at the time that they did so. By the 1920s, the Salomon approach had become settled law with a victory for Contractarians and Shareholder Primacists, with an emphasis on shareholders' ability to waive formality in decision making. The cases have involved both binding the company to third parties, and waiving internal procedural requirements. The test developing was merely whether the proposed act was intra vires or not, with judiciary actively looking to hold a course of action as being so if the company received a benefit as part of the transaction.

138 Ibid 979
139 Ibid 984
3.3. **Duomatic**

“For a number of years there were no cases of real import on this matter”. This changed with the case after which the Principle is commonly named, being *In re Duomatic Limited*, which involved a challenge by a liquidator of a company of payments made to various directors. Initially there were three directors, who were all ordinary shareholders. There was also a preference shareholder (“Dutchco”) who was not entitled to vote. One of the directors (“H”) was not fulfilling his duties. The other directors agreed to pay him £4,000 to resign and transfer his shares to one of the other directors. There were further changes to the directors and shareholders. After the addition of new shareholders, one of the directors (“E”) agreed to only draw remuneration at £60 per week, but drew far more. When the company entered insolvency, the liquidator challenged various payments made by the company as breaching the articles of association (which required approval of director remuneration by ordinary resolution), and that the arrangements had not been disclosed to the shareholders of the company (ie Dutchco was unaware of the arrangements). Dutchco was a shareholder but was not entitled to vote or attend meetings. Preference shares are a grey area in the analysis conducted so far as they have a wide range of potential characteristics. Preference shares with a fully fixed, cumulative return are effectively debt instruments as they enjoy no marginal increase in claim or value as the company gains success. On the other hand, preference shares which have a right to receive equity returns or value on a wind up have a marginal increase. With potential additional complications of different rights arising on dividends and on winding up and voting rights, it is impossible to conclude where preference shares should fit into the normative framework

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140 Ellis (n4) 262
141 Duomatic (n2)
142 Buckley J.’s judgment provides no detail of the consideration paid for the shares transferred, nor whether it represented a transfer at value. There is a risk of confusion whether this £4,000 payment was severance pay or a combined payment to H to exit the company in all capacities
143 So have no normative claim to decision making rights
144 So have a normative claim to decision making rights
for corporate decision making, and whether the holders are “shareholders” or other constituents when it comes to examining theory and the Principle. Unfortunately, the case report for Duomatic does not outline the rights attaching to Dutchco's shares and so makes it hard to examine how Duomatic should have been decided. This is unfortunate, as if Dutchco was a “pure economic shareholder” then the Principle should not have applied as there are agency costs arising from the majority ordinary shareholders waiving formality - whereas if Dutchco was effectively a debt stakeholder then the Principle should be able to apply without Dutchco needing to have decision making rights or even being informed.145

The liquidator’s barrister argued that the authorities “establish that the unanimous consent of the corporators may bind a company as effectively as a formal resolution. In this case there was a holder of preference shares who did not consent”,146 failing which the lack of disclosure of payment to all shareholders should invalidate the payments. This may have been a tactical mistake. Had he pled that the payments were ultra vires given the financial position of the company (a George Newman approach) then the judgement may have been different, and perhaps more limiting on the application of the Principle. In respect of the first ground, Buckley J. formulated the Principle in its most famous iteration:

“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 a general meeting.”147

Buckley J. elaborated further:

“The preference shareholder, having shares which conferred upon him no right to receive notice of or to attend and vote at a general

145 See Jonathan R Macey & Geoffrey P Miller 'Corporate Stakeholders: A Contractual Perspective' (1993) 43(3) The University of Toronto Law Journal 401, 413
146 Duomatic (n2) 368F
147 Duomatic (n2) 373C
These statements provide a limitation to the Principle. They emphasise examining whether the general meeting of the company can effect the resolution so proposed. It has been generally held that the division of power between the board of directors and the shareholders is a matter for construction of the articles of association of such company. This formulation weakens the Principle, as to invoke it means there must be some ability for the shareholders’ to undertake this course of action contained in the company's articles. This clashes with normative position that we would expect the Principle to embody, which would be to empower the shareholders to make any decision on behalf of the company. Accordingly, the formulation of the Principle in Duomatic narrowed its application to the actions of a general meeting rather than any clear ability to bind the company, and re-focused the Principle to situations where resolutions would be valid at general meetings. This in turn provided a boost to those who adhere to Bainbridge’s director primacy, and so curtailed the rights of shareholders to deploy the Principle in general terms. This provided considerable clarity to the category of actors who require to consent for operation of the Principle - only those who are entitled to receive notice of and vote at general meetings. In other words, Duomatic subtly changed the application of the Principle further from unanimity of the corporators, to unanimous action of those shareholders who can vote. Duomatic changed the Principle from being of wide application, to being a way to hold an informal general meeting of the company.

Based on this formulation, it was clear that E had to repay amounts received in excess of £60 per week since that level of remuneration was agreed. It would appear to validate the £4,000 payment to H as Dutchco could not

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148 ibid
149 Shaw & Sons (Salford) Ltd v Shaw [1935] 2 K.B. 113, CA
150 Which had generally been undefined in previous cases
vote and all other shareholders approved the payment. The relevant section of the Companies Act 1948 (section 191), however, required not just approval by the company of payments for compensation but also the details being “disclosed to members of the company”. Buckley J., therefore, ordered H to repay £4,000 to the company, stating:

“That section must, I think, require disclosure to all members of the company, and it must require disclosure while the payment is still a proposed payment, that is to say, before the payment is made; and it further requires that the proposal be approved by the company, which must, I think, mean the company in general meeting.

In the present case it is clear that no particulars of this payment of £4,000 were, before the date that the payment was made, given to all members of the company, for no such disclosure was at any time made to the preference shareholder. There would, I think, be good reason for making such disclosure to him, notwithstanding that he would have no right to attend any general meeting convened for the purpose of approving the payment, because although he was not, by virtue of his preference shareholding, entitled to receive notice of general meetings or attend and vote at them, he might nevertheless wish to make his views known to those who would attend and vote at the general meeting, and therefore notice to him of the proposal to make the payment might well be a matter of some importance to him and of some ultimate consequence in the affairs of the company.”

This contradicts his previous logic: in Dutchco could have been in “no worse position” by informal decision making, but also were entitled to receive disclosure of the proposed transaction in case they would have made their view known to voting shareholders. H had to repay the amounts advanced to him when all who were entitled to had decided that he should be entitled to it, in a situation where statute was not explicit as to whether all members required prior disclosure or not. The decision is guidance that the Principle may not apply where there is an express statutory requirement that precludes it. In Duomatic, the statutory requirement to give disclosure to

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151 Duomatic (n2) 374G
(arguably) all members\textsuperscript{152} meant that the putative application of the Principle was thwarted, despite being ostensibly held to apply.

It has been stated that Buckley J. “sidestepped the inconsistencies in the previous authorities”\textsuperscript{153} He sidestepped widespread application of the Principle, as the lack of disclosure invalidated the shareholder decision making. We cannot verify whether Dutchco should have been normatively included or excluded from the shareholder base for unanimity purposes. The court should be keen to ensure that genuine unanimity of members has been achieved in order to avoid potential agency costs by the majority on the minority. In order to do so, where there is any grey area, the court should therefore be keen to deny application of the Principle. Accordingly the outcome in \textit{Duomatic} matches the normative framework outlined so far. However, the rationale for arriving at this outcome seems unsatisfactory - Buckley J. excluded Dutchco for certain purposes and included them for others, and in doing so contradicted his own logic.

Nevertheless, Buckley J.’s formulation of the Principle has become the defining test for its application\textsuperscript{154}

3.4. \textsc{Post Duomatic}

The narrower interpretation of the Principle developed relatively widespread application and judicial acceptance. In \textit{Cane v Jones},\textsuperscript{155} two sides of a family had 50\% each of the shares in a family company, and fell out. The articles held that the chairman of the board of directors had a casting vote at a meeting of directors, but a prior shareholders’ agreement disapplied this provision. Shareholders had subsequently changed (still with each side of the family holding 50\% of the shares each), with the question being whether the agreement, by application of the Principle, had varied

\textsuperscript{152} Which, if there were no preference shareholders, would be an identical process to the application of the Principle
\textsuperscript{153} Ellis (n4) 263
\textsuperscript{154} eg \textit{Elc Services Ltd v Phipps}, [2004] 2 B.C.L.C. 589
\textsuperscript{155} [1980] 1 W.L.R. 1451
the articles or whether it was a contractual arrangement which did not bind successor shareholders. Wheeler QC held that it did not matter: either the Principle applied and therefore the articles were changed, or alternatively the agreement overrode the articles and, due to its terms, bound the current shareholders - in either case the agreement trumped the articles. This judgement meant that the complex issue of registrations with the Registrar of Companies was avoided.

Not all judicial treatment of the Duomatic iteration has been favourable. In In re Barry Artist Ltd,\textsuperscript{156} the company petitioned for a reduction of capital and cancellation of its share premium account despite no special resolution being passed as required under the Companies Act 1948 - instead all shareholders had signed a written resolution (which was not an acceptable procedure). Nourse J. stated that other than this the petition was “unobjectionable and ought to succeed”,\textsuperscript{157} but as well as the company decision, the court had to approve the reduction and had discretion to do so. He was critical of the company adopting a written resolution, and stated:

“\textit{The court has never before been asked to document a reduction which the company has effected or purported to effect otherwise than by way of special resolution. It seems to me to be most undesirable that a settled practice of many years' standing should be disturbed... it has been represented to me that the company chose to proceed as it has, not in order to test out whether it could proceed in this way, but because it was advised that it could and because it was thought to be more convenient to do so. I will accept that that was the case, although I desire to say that the one and a half hours which it took to argue the point last Wednesday did not suit the convenience of the court... My strong inclination has been to adjourn this petition so that a meeting can be held and a special resolution passed, but it has been represented to me that the company has a good reason... for having the reduction confirmed before the end of this term. In the circumstances, although with great reluctance, I am prepared to accede to the petition today. I would not be prepared to do so in any similar case in the future.”}\textsuperscript{158}
The court acknowledged the presence of the Principle but was not keen on its application in the *Duomatic* formulation. Had Barry Artist Ltd not had good reason for the reduction to be confirmed in short order, it seems likely that this attempt to rely on the correct legal application of the Principle would have resulted in the court rejecting a petition it otherwise would have accepted. This is the opposite of the approach taken by Astbury J. in *Parker & Cooper Limited*, which very strongly emphasised the just outcome in the case before him. This represents a development in judicial attitudes which has resulted in the court taking a much more hesitant attitude to the Principle than was shown in the early days of its development: the court reviewed the merits of the case.

During the 1980s the limitations of the Principle were explored more fully. Thus, attempts to utilise the Principle to defend an action by a liquidator to recover a dividend that was unlawfully paid was rejected as unlawful distribution rules were for the benefit of the creditors and so could not be waived by the shareholders. This matches the normative grounds for rejection of the application of the Principle.

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159 *Precision Dippings Limited v Precision Dippings Marketing Ltd.* John Anthony Wynne-Jones and Peter John Leslie David King 1985 WL 1167741
4. ELEMENTS OF THE MODERN TEST OF THE PRINCIPLE

The modern application of the Principle comprises a two stage test - firstly, is the Principle capable of applying to a particular situation; secondly, did the Principle actually apply that situation.\[160\]

4.1. SCOPE

4.1.1. FUNDAMENTAL TEST

The first element is the “scope” of the Principle. The basic test was contained in *Atlas Wright (Europe) Ltd v Wright & Anor.*\[161\] This case involved a long term service contract with a Mr Wright, who sold his majority stake in Wright Air Conditioning Limited (“WACL”) to Wheway plc, and WACL became a wholly owned subsidiary of Wheway. The CEO of Wheway signed a contract appointing Mr Wright as President of WACL for life (although Mr Wright could terminate the arrangements on 6 months’ notice). Wheway complied until it sold the shares of WACL to Atlas Wright. The new directors of WACL decided to terminate the arrangement. When the arrangement was implemented, section 319 of the Companies Act 1985 was in force which provided that a company could not enter into a service contract with a director for more than 5 years unless the shareholders had received 15 days’ written notice of the proposed term and approved it in general meeting, which had not happened. Atlas Wright tried to rely on s319 to escape the contract. The Court of Appeal reviewed the white paper that proposed the wording of s319 at the start of their discussion of the judgment,\[162\] showing a purposive approach. Despite the case of *Re RW Peak (Kings Lynn) Limited*\[163\] (see discussion at 4.1.2 below) being decided as the case was being argued, the Court of Appeal held that when deciding whether the Principle should apply:

\[160\] eg Nicola Ruutel and Kathryn Saunders “Duomatic Principle Practice Note” - www.practicallaw.com/3-519-4794
\[161\] [1999] B.C.C. 163
\[162\] Ibid 170 - 171
\[163\] [1998] B.C.C. 596
“each such provision requires to be examined on its merits against the criterion of underlying purposes. As already stated, in relation to s164 and the decision in Re RW Peak, there may well be good reasons for refusing to apply the Duomatic doctrine [i.e. the Principle] to a particular provision when its underlying purpose is examined.”

The Court of Appeal held that the Principle could only apply in situations where the rule to which the Principle was purportedly applied was for the benefit of the shareholders. This matches the normative provision for application of the Principle - that shareholders should have maximum freedom to unanimously waive rules which are exclusively for their benefit but should not be able to do so if the rule is for the benefit of others. In *Atlas Wright* the Court of Appeal held in respect of s319 that:

> “it does not seem to me to be plain that there is any statutory purpose underlying the provisions of s319 (3) and (5) beyond the benefit and protection of the shareholders of the company... the underlying intention appears to me to be no more than to require unequivocal opportunity for the shareholders of the company to consider the terms of the agreement approved... it seems to me no more than a ‘back up’ formality in the nature of a notice provision designed to ensure the opportunity for fully informed consent by the shareholders. It is thus amendable to waiver by the class for whose protection it is designed.”

Accordingly, the Principle could apply to this situation. The effect of this is to prevent an argument by the company that it is not bound because it failed to adhere with statutory internal decision making processes. In *Atlas Wright*, this prevented the current shareholders from avoiding a contract that they did not want the company to be in.

Establishing the beneficiaries of any particular rule is straightforward. Thus, the Principle can apply to ratification of breach of duties by shareholders to a company. Statutory procedures for removing directors have been held “at least in part” to be for the benefit of the director and therefore the

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164 Atlas Wright (n161) 175
165 Ibid
166 *Multinational Gas and Petrochemical Co v Multinational Gas and Petrochemical Services Ltd* [1983] Ch 258, and more recently *Sharma v Sharma* [2013] EWCA Civ 1287
167 Jennifer Ann Bonham-Carter, Antoinette Monique Horn v Situ Ventures Limited [2012] EWHC 230 (Ch)
Principle cannot apply. Similarly, requirements in respect of financial information to be provided prior to a distribution, and limitations on unlawful distributions are for the benefit of creditors and therefore the Principle cannot apply. Conversely, the Principle applied to the requirement of shareholder approval for substantial property transactions. Similarly, a pension plan purchases by a company for a retiring director that ignored procedural rules was curable by the Principle. A taxonomy of the cases demonstrates the following in respect of the Principle:

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<th>CASE</th>
<th>RULE</th>
<th>WHO WAS THE PRINCIPLE FOR THE BENEFIT OF?</th>
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<td><strong>Duomatic</strong></td>
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<td>Shareholders</td>
<td>✓</td>
<td>X</td>
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<tr>
<td><strong>Salomon</strong></td>
<td>Grant of security/incurring of Indebtedness with connected parties</td>
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<td>✓</td>
<td>✓</td>
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<td>Creditors</td>
<td>X</td>
<td>X</td>
</tr>
</tbody>
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168 Bairstow & Ors v Queens Moat Houses Plc [2001] EWCA Civ 712 & Re Logic Alliance Limited 2006 WL 3835202
169 Aveling Barford Ltd v Perion Ltd [1989] BCLC 626, 631
170 Eg see Re Torvale Group Ltd [1999] 2 BCLC 605 and NBH Ltd & Anor v Hoare & Ors [2006] EWHC 73 (Ch)
171 Re Horsley & Weight Ltd [1982] Ch. 442
<table>
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<tr>
<th><strong>SRA</strong></th>
<th><strong>Issue</strong></th>
<th><strong>Decision</strong></th>
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<tr>
<td><strong>Express Engineering</strong></td>
<td>Constitutional limitations on grant of debentures</td>
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<td><strong>Parker &amp; Cooper</strong></td>
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<td><strong>Cane v Jones</strong></td>
<td>Amending board proceedings contained in articles</td>
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<td>✓</td>
<td>✓</td>
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<tr>
<td><strong>Barry Artist Ltd</strong></td>
<td>Solvent liquidation</td>
<td>Shareholders</td>
<td>✓</td>
<td>✓ (but judicial reticence)</td>
</tr>
<tr>
<td><strong>Precision Dippings</strong></td>
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<tr>
<td><strong>Atlas Wright</strong></td>
<td>Prohibition on entering into long term directors’ contracts</td>
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<td>✓</td>
</tr>
<tr>
<td><strong>Multinational Gas</strong></td>
<td>Ratification of breach of director’s duties</td>
<td>Shareholders</td>
<td>✓</td>
<td>✓</td>
</tr>
<tr>
<td><strong>Sharma v Sharma</strong></td>
<td>Ratification of breach of director’s duties</td>
<td>Shareholders</td>
<td>✓</td>
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</tr>
<tr>
<td><strong>Bonham-Carter v Situ Ventures Limited</strong></td>
<td>Statutory notice periods for removing a director</td>
<td>Directors (&quot;at least in part&quot;)</td>
<td>X</td>
<td>X</td>
</tr>
<tr>
<td><strong>Re Horsley &amp; Weight Ltd</strong></td>
<td>Statutory procedure for purchase of pension plan for a director</td>
<td>Shareholders</td>
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<td>✓</td>
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<td><strong>Re Torvale Group Ltd</strong></td>
<td>Restrictions on substantial property transactions with directors</td>
<td>Shareholders</td>
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<td>✓</td>
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<td><strong>Aveling Barford</strong></td>
<td>Restrictions on unlawful distributions</td>
<td>Creditors</td>
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<td>X</td>
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<tr>
<td><strong>Bairstow v Queens</strong></td>
<td>Provision of financial information prior to distribution</td>
<td>Creditors</td>
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</tr>
</tbody>
</table>

This neatly shows when the Principle is capable of application. However, there are some rules that it is difficult to identify the "purpose" of.

4.1.2. **Buyback Cases**

*In Re Barry Artist Ltd* showed the courts' hesitancy when applying the Principle to reductions of capital, rooted in company law's traditional
reticence to countenance returns on capital. The Companies Act 1985 introduced detailed rules of substance and procedure when it came to a company approving a buyback of its own shares from capital without obtaining court approval to do so. Certain of these were summarised by Lindsay J in Re R W Peak (Kings Lynn) Ltd as being:

“(1) The company must be authorised to purchase its own shares by its articles (s.162).
(2) Where, as here, the purchase is ‘off-market’ within the meaning of s. 163(1), then the purchase has to be pursuant to a contract which itself has to be approved in advance of the purchase (s. 164(1)).
(3) That contract has to be approved by a special resolution of the company before the contract is entered into (s.164(2)).
(4) That special resolution has to be such that it is either passed without the holder of the shares to be bought voting them or the case being that, even if he had done so, the resolution would have still have been passed as a special resolution (s. 164(5)).
(5) Such a resolution is not effective to authorise the proposed contract unless a copy of the contract, if it is in writing, shall have been available for inspection by members of the company at its registered office for at least the preceding 15 days before and at the meeting at which the restriction is passed (s.164(6)).”

These seem to be rules of procedure rather than substance. All require shareholder approval or prescribe time periods that shareholders have to receive information prior to making such decision, so all seem for the shareholders' benefit and therefore capable of application of the Principle. In addition to these procedural requirements, there was a requirement for directors of the company to confirm the company's ability to pay its debts as they fell due immediately after the buyback and likelihood of doing so for year afterwards. This test, that the company in question remain solvent after the buyback, is a rule of substance for the benefit of creditors and so the Principle should not apply to it.

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172 Trevor v Whitworth (1887) 12 App. Cas. 409
173 Companies Act 1985 Part V Chapter VII
175 Ibid 600
176 Companies Act 1985 s173(3)
In *R W Peak* a father (Ronald) and son (Nicholas) were the only two shareholders of the relevant company. Ronald retired, and it was agreed that the company would purchase Ronald’s shares. The transaction completed in 1991 and but did not meet the procedural rules set out by Lindsay J. above, despite:

“common ground... that the transaction in 1991 could have been arranged so as to have occasioned no doubts as to its legality and efficacy”\(^{177}\)

in other words, the rule for the benefit of the creditors was satisfied. In 1996 Nicholas died. Ronald raised an action to rectify the register of members of the company to undo the buyback transaction on the grounds that this transaction had not complied with the requirements for share buybacks out of capital. This action should have failed for several reasons. Firstly, the rules ignored were for the benefit of shareholders, and were waived by them. Secondly, Ronald was party to the transaction and seemed content until Nicholas’ death - estopping himself from arguing that his contractual counterparty had not followed required procedure. There were subsequent proceedings to establish (as required under the Companies Act 1985) whether granting Ronald’s motion for rectification would prejudice people who had not yet appeared before the court, however Lindsay J held that the Principle could not apply. Several reasons were given, including that the articles of the company did not allow redemption of shares. This does not follow *Cane v Jones*. Another reason given was that Nicholas had not signed the buyback agreement in his capacity as shareholder of the company. This does not follow Younger LJ’s analysis in *Re Express Engineering Works Ltd*: the two shareholders reached an agreement whilst together and therefore were a meeting automatically. Lindsay J went further:

“I add that I would reject the applicability of the Duomatic principle even were I to assume in the defendant’s favour that there was no requirement for a specified and suitable alteration to have been duly made to the company’s articles prior to the contract and even if

\(^{177}\) *R W Peak* (n174) 598
Nicholas’s signature were properly to be regarded as an assent by him qua member rather than, as it could have been, by way, for example, of a director implementing a decision he was acceding to on the company’s behalf under the persuasion of his fellow-director and majority shareholder.”

Lindsay J does not elaborate why, and does not comment on the perverse results - Ronald set aside a transaction that he had signed up to (and which Lindsay J hinted he may have persuaded the company to accept) despite the company's objection. Lindsay J concluded:

“In the circumstances it is not possible, in my view, to regard the provisions of s. 162 and 164, which ensure that time is afforded for a measured informed consideration by members of the wisdom or propriety of any proposed purchase, as merely procedural and for the benefit only of current members.”

This analysis is flawed: rules which exist solely for the benefit of shareholders should be capable of being waived by the current shareholders. The purpose of such formality is to minimize agency costs between shareholders and managers or the other shareholders, which cannot arise where there is commonality between the shareholders and the managers and where all shareholders agree, as in R W Peak. Provided compliance with the rules for the benefit of the creditors (i.e. the company remained solvent) then all other rules in this regime should be able to be subject to the Principle. The result in this case departed from the Principle as seen in Re Express Engineering Works Ltd and Parker & Cooper, Ltd - which rejected Lindsay J’s view that formality of meetings and time requirements were protections that the shareholders could not waive. Lindsay J also objected to the application of the Principle as the shareholders consented at the same time as the contract was entered into, rather than prior to as required under the statutory regime. This is also an incorrect conclusion. Accordingly, this decision seems to be an anomaly. R W Peak was decided during the Atlas Wright case, and Potter LJ discussed R W Peak, and concluded:

178 Ibid 604
179 Ibid 605
“it was logical in the case of Re R W Peak not to apply the Duomatic principle when it would have undermined the clear statutory purpose of s. 164(2) and 164(5), as well as the broader policy considerations of Chapter VII of Part V of the 1985 Act.”

This analysis sidestepped examining Lindsay J’s reasons for concluding that the purpose of the procedural aspects of this regime was to protect others than the current shareholders. In R W Peak, the company was trying to argue that the Principle applied, whereas in Atlas Wright it was a third party arguing the application of the Principle against the company. This creates a possibility that, rather than being a uniformly applied rule, its application depends in part on who is trying to argue the Principle’s application.

The decision in R W Peak has been gradually eroded. In BDG Roof-Bond Ltd v Douglas & Others, a company attempted to buyback shares out of distributable profits rather than out of capital. Due to a qualification by the auditors in the company’s accounts, the court held against the buyback. However, Park J provided some comment on the applicability of the Principle to the buyback regime, particularly the requirement that the contract be available for inspection prior to being entered into: “[this section] is a provision designed solely for the benefit of shareholders. There is no element of creditor protection in it at all.” This conclusion is correct. However, it contradicts R W Peak – either these tests contain an element of creditor protection or they do not. It does not make sense for none of these procedural provisions have any element of creditor protection, but the procedural regime in aggregate having such. The company originally submitted that lack of compliance with this regime resulted in the buyback being invalid – but dropped this following Atlas Wright. Had the company continued pressing this submission, Park J would have held that the Principle prevented the company from making such a submission.

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180 Atlas Wright (n161) 175
181 [2000] BCC 770
182 Ibid 783
The confusion increased with *Kinlan v Crimmin*, 183 where a liquidator of a company tried to recover from an ex-shareholder amounts paid to him under a share buyback that had not complied with the procedural regime. No copies of the buyback contract had been provided in advance to the shareholders, and the agreement of shareholders to the transaction had taken place at the same time as the contract was signed, rather than in advance as required under the regime. In this case Mr Sales (sitting as a deputy judge of the High Court) concluded that “everyone who attended the meeting on 26 January 2001 understood very well what the object of that meeting was (namely, to agree finally the terms of any enter into an agreement for Styleprint [the company] to purchase Mr Crimmin’s shares.” 184 He was of the opinion that:

“I should add that since the events at the meeting on 26 January 2001 [when the buyback agreement was signed] really amounted to a composite transaction to review and approve the [buyback] Agreement, I would not have regarded it as fatal to this analysis even if the resolution had been signed immediately after the Agreement was signed, rather than the other way round...The provision in s 164(6)(a) [which required prior copies of the buyback agreement to be provided to shareholders] is, in my view, clearly one for the protection of the members of the company rather than third parties, and hence is capable of being waived by the relevant members entitled to vote if they are unanimously in agreement that adherence to its terms is not required.” 185

This matches the analysis of this thesis. However, it contradicts *R W Peak*. Mr Sales attempted to distinguish the cases on the grounds that the *R W Peak* articles did not allow for share buybacks whereas the *Kinlan v Crimmin* articles of association did. In light of *Cane v Jones* and Lindsay J’s own opinion in *R W Peak* (which stated he would have concluded the same even if the articles did so), this seems tenuous. Mr Sales states:

“In my view, in relation to the particular provisions referred to, the impact (if any) upon persons other than the current members of Styleprint would have been so marginal and indirect that waiver of the provisions which I have referred to by operation of the Duomatic

183 [2006] EWHC 779 (Ch)
184 Ibid para 39
185 Ibid para 40
principle would in each case have been legitimate. In particular, so far as concerns creditors or future members, they would have been on notice from inspection of the resolution and the notice given to the Companies Registrar...and would have been in a position to assess Styleprint’s general financial position in the usual way by reference to its audited accounts filed from time to time.”

This goes further than the ‘purpose’ test. Mr Sales’ logic would mean that purpose was not the test for the Principle, but instead it was necessary to review the actual impact of the putative transaction on third parties: meaning an unlawful distribution was capable of being remedied by the Principle provided the relevant company did not enter insolvency. This miscategorises the initial test for the application of the Principle. Nevertheless, the majority of Mr Sales’ analysis matches the normative and historical approach to the Principle seen so far, even if it directly conflict with R W Peak.

This conflict is acknowledged. In Peña v Dale a buyback was held invalid because the consideration was to be paid in instalments in breach of the substantive element of the regime. Behrens J stated:

“[Counsel for the company] makes the point that no written memorandum of the terms of the repurchase was either sent to the members or available for inspection at its registered office for the 15 days prescribed by section 164(6). Whilst the submission is factually correct it is far more difficult to argue that the effect of the breach is to render the repurchase void. The difficulty arises from the apparent conflict between the views of Lindsay J in Re RW Peak 9 as explained by Potter LJ in the Court of Appeal in Re Wright v At1as Wright 10 and the views of Park J in Bdg. Initially Mr Kosmin QC [counsel for the company] suggested that Park J cannot have been referred to the views of Lindsay J. However as Park J’s judgment contains quotations from the judgment of Potter LJ where the judgment of Lindsay J is quoted at some length that seems unlikely.

Despite the very full and helpful submissions on the point from Mr Kosmin QC and Mr Bannister QC, I think that the resolution of the

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186 Ibid para 44
187 [2004] 2 BCLC 508
188 It is difficult to confirm the effects of future payments on a company's solvency.
This matter was determinative of the outcome in the case of Dashfield v Davidson. This case involved a company with 3 shareholders, which was being sold. Due to previous experience, one shareholder wished to ensure that the death of a shareholder did not cause the company lapsing into inertia. Accordingly, a new article (“Article 14”) was inserted into the articles which provided that if a shareholder died, their shares would be bought back, valued by the most recent audited accounts of the company, failing which offered pre-emptively. The shareholders agreed to a sale of the company (“Crown”), but during negotiations one shareholder died, prior to the publication of effectively finalised audited accounts. The company had traded strongly over that year, and therefore if these were utilised for the buyback calculation then the shares would be worth more. Completion mechanics of the sale of Crown included a buyback of the deceased shareholder’s shares at completion and the purchase price being reduced accordingly. The balancing payment was held in escrow pending determination of the price to be paid to the estate of the deceased shareholder. One of the issues before the court was:

“whether...By reason that all the members of Crown agreed to the amendment of Article 14 the formalities requisite for compliance with Section 164(2) of [the Companies Act 1985] were deemed to have been complied with the Duomatic Principle”.

McCahill J reviewed the judicial history of the Principle:

“There are, no doubt, limits to the applicability of the Duomatic principle. No doubt it would have to yield to a fundamental requirement imposed by statute. The difficulty lies in identifying such fundamental principles. Moreover, the principle could not be used to validate non-compliance with a provision or requirement which was not exclusively for the benefit of those who in fact assented.”

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189 Kinlan v Crimmin (n183) para 115-116  
190 [2008] B.C.C. 222  
191 Ibid para 38.2  
192 Ibid para 72
McCahill J treated these as two separate tests: they are, instead, part of one test - a ‘fundamental requirement’ is any rule which is not exclusively for the benefit of the shareholders (regardless of whether imposed by statute or not). In discussing R W Peak, McCahill J thought it not clear what constitutes the ratio of the case and what is obiter. He noted two potential views of the case - it was an ‘anomaly’, or the buyback rules were for the benefit of only the current members.\textsuperscript{193} He ultimately concluded that the true ratio of the case was the anomaly argument and therefore fact specific.\textsuperscript{194}

McCahill J explained the conflict noted above between R W Peak and BDG Roof:

“If the protections afforded by Section 164(2) to (7) did provide some public interest or creditor protection, then each of the provisions should have been regarded in this light. Yet, Park J held that Section 164(6) had no element of creditor protection at all.”\textsuperscript{195}

He described R W Peak as a “high water mark”, which had been “eroded” by subsequent cases which, in the buyback context, resulted in an “enlargement of the role of the Duomatic principle”.\textsuperscript{196} McCahill J concluded that, in Dashfield, any breach of the buyback rules had been cured by application of the Principle, and thus distinguished R W Peak. He stated:

“I do not think it is possible to lay down a rule of universal application that s164 serves a particular public interest or the interests of creditors generally. It is necessary to consider each transaction and to examine that statutory provision and its underlying purpose in relation to that transaction. Thus, I do not believe that one can say that the Duomatic principle can never cure a non-compliance with s164.”\textsuperscript{197}

\textsuperscript{193} Ibid para 77
\textsuperscript{194} Ibid para 86
\textsuperscript{195} Ibid para 92
\textsuperscript{196} Ibid paras 118-119
\textsuperscript{197} Ibid para 127
This adopts the normative application of the Principle discussed above. It is couched in negative language, and it would be neater in the positive - the buyback rules are mostly for the benefit of shareholders and therefore the Principle can apply to those. The rules that buybacks must be from distributable profits or be accompanied by solvency confirmations and that not all shares can be bought back are for the benefit of creditors and so the Principle cannot apply to them. McCahill J states:

“However, it may not be hard to envisage situations in which s164 would strike down a transaction... Such an example might be where, long after the directors had caused the company to buy its own shares using distributable profits, the directors sought retrospective ratification of that transaction by all the shareholders. In such a case, it may be the requirement of prior approval would render the transaction void.”

McCahill J compares this situation and Duomatic - in both cases, “money had left a company in disregard of those who were potentially prejudiced thereby”. This is confused, as the buyback rules require actual approval rather than information provided. Further, in line with the critique of the Duomatic decision noted above, it is posited that this is incorrect. If the Principle is capable of application then it should not matter whether permission for a transaction is prior or ex poste - if it is received from the correct people then the transaction should not be struck down. The difficulty of this approach is, of course, the effect on the transaction if the shareholders find out about it after completion and decide not to ratify it. This demonstrates that the Principle acts as a functional equivalent to formality but presents a risk to directors relying on it: they may be exposed if the shareholders chose not to ratify their actions.

4.1.3. PURPOSE MAY CHANGE ACCORDING TO CONTEXT

The purpose of the rule to which the Principle is purportedly applied is not the end of the matter. The interests of the company effectively equate to
the interests of the shareholders, but when the company enters financial difficulties this changes to the interests of the creditors. Then, shareholders are unable to exercise their rights to direct the company, which only vest in them because the interest of the company aligns with theirs. Accordingly, the Principle cannot apply in financial difficulty. The precise point in time that such switch occurs is not clear. It does not require “technical insolvency”, and has even been stated to occur when the company is in “doubtful solvency or on the verge of insolvency”. This is a complex area - it is sufficient to note that the Principle can be stymied by financial difficulty of the company in question in line with the normative analysis reached above.

Thus in *Re: Finch (UK) plc* the company entered insolvency. Prior, some complicated transactions appeared malfeasant - properties from a bare trust that one of the directors was settler of were transferred to the company in exchange for the issue of redeemable shares to such director, which were in turn immediately redeemed. The Chancery Division held that whilst the Principle could have ratified these wrongs, it could not do so whilst the company was insolvent. The purpose of the test is not conclusive for the Principle - it is necessary to review the financial strength of the company, and then in turn whether the Principle was invoked in fact. In addition, the redemption of shares amounted to a preference and therefore the transaction failed. Stakeholders obtain protections of their claims against a company from outside corporate law: and these therefore interact with the Principle in practice.

Most of the cases rejecting the Principle have concerned statutory procedures rather than provisions of articles. This is not surprising - the

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200 Subject to Companies Act 2006 s172
201 *West Mercia Safetywear Ltd v Dodd* [1988] BCLC 250
202 *Re Stakefield (Midlands) Limited and others* [2010] EWHC 3175 (Ch)
203 *Re MDA Investment Management Ltd* [2004] 1 BCLC 217, as discussed in *Re Stakefield*
204 *Colin Gwyer & Associates Ltd v London Wharf (Limehouse) Limited* [2003] 2 BCLC 153, as discussed in *Re Stakefield* (n201)
205 [2015] EWHC 2430 (Ch)
206 *Re Torvale* (n170)
articles are contracts agreed between, and capable of amendment by, the shareholders: the Principle should be able to apply to almost all of their provisions. Conversely, mandatory rules in company law often benefit third parties, and therefore there is a higher likelihood that the Principle will not be able to apply to them. The Principle can apply to other rules, for example waiving formality in shareholders’ agreements and extraordinary general meetings of friendly societies. It also applies to classes of shareholders.

4.2. IMPLEMENTATION OF THE PRINCIPLE

If the Principle is capable of applying to any given situation, it is necessary to evaluate whether it has, in fact, been implemented. There are two practical elements to this test: who needs to be involved, and what they need to do.

4.2.1. WHO NEEDS TO BE INVOLVED?

In the discussion so far, there has been a presumption of unanimity of the actors involved. For example, Lord Davey's dictum in Salomon referred to “every member” and “unanimous consent”. The case of Joint receivers and managers of Niltan Carson Ltd v Hawthorne involved two parents establishing a company, which purchased and operated an unprofitable hotel. The mother (a director of the company) attempted to rent the hotel from the company for use as a children’s home. All were content until the father realised how profitable the venture would be. He then obstructed the children’s home business so that both the business of the children’s home and the business of the company faced financial difficulties. The father procured his appointment as a receiver on behalf of the secured creditors, and raised an action against the mother, claiming that the profits of the children's' home business should belong to the company as the arrangement

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207 Euro Brokers Holdings Ltd v Monecor (London) Ltd [2003] EWCA Civ 105
208 Speechly v Allott [2014] EWCA Civ 230
209 Torvale (n170)
210 Joint receivers and managers of Niltan Carson Ltd v Hawthorne (1987) 3 B.C.C. 454
was a substantial property transactions with directors of a company. Hodgson J characterised the father as follows:

"He has a great taste for litigation, which he obviously enjoys. He is also, in my opinion, and I regret to have to say this, a man of few scruples and a man with a by no means comprehensive acquaintance with the truth. These characteristics have enabled him, both during the events out of which this litigation arises and during the extensive litigation that has followed them, to clothe what had its origins in a domestic dispute with the trappings and technicalities of corporate law. Like most domestic disputes, this one led to nothing but misery and sadness. It was composed of jealousy and hate, together be it said with a great deal of paternal love and affection."

He continued:

"I should make it plain that I wholly accept Mrs Hawthorne [the mother] as a witness of truth, a finding that I regret I am unable to make as far as Mr Nelson [the father] is concerned. Wherever the two accounts differ, I unhesitatingly prefer and accept that of Mrs Hawthorne."

The mother's solicitors requisitioned a general meeting of the company to expressly permit the children's' home business to continue. The father, as managing director, summoned a deliberately (but only arguably) invalid shareholders meeting of the company at which 98.7% of the members attended. In respect of a roughly contemporaneous directors' meeting, Hodgson J commented "it well illustrated the depths of technical rubbish into which Mr Nelson had managed to drag his family", showing his attitude to the father. He took issue with the father's evidence and overly formalistic approach to corporate law. He held that shareholders' meeting valid and therefore any arguments about the Principle were irrelevant. However, he went on to state, obiter:

"Mr Pendlebury [counsel for the mother] concedes that to apply the Principle thus enunciated to this case would be to extend it. He submits that, on the very special facts of this case, such an extension would be justified. First, because plainly Miss Boyd [the missing
shareholder] would have been quite unable to prevent a resolution being passed at a properly constituted meeting. She would have been as powerless as the preference shareholders in Re Duomatic. Secondly, because Miss Boyd was plainly in the pocket of Mr Nelson and, as she would do precisely what he told her to do, her independent voice would not have been heard at any meeting had she attended. I am impressed by this argument but, once again, in view of my decision on s48, I do not need to make a firm finding which would extend a principle of law perhaps more suitably considered in another Division. However, on the particular facts of this case, if I had to extend the (P)rinciple to the extent necessary to do justice in this case, I would do so.”

The Principle was not required in this case and so this paragraph is, at most, obiter. Hodgson J limited this analysis to this specific case. In addition, neither of the arguments advanced by Mr Pendlebury enjoy judicial support. Emphasis on “justice”, however, is highly illustrative to the judicial approach to the Principle. The flexibility of the Principle means that English courts can view it as almost a rule of equity, to overcome an unjust and overly formalistic application of corporate law. Whilst Nilan Carson shows the open-minded attitude that courts take towards the Principle, it is limited to its facts rather than of widespread application. That said, a court has held that the holders of 75% of the share capital may operate the Principle in a case where the remaining shareholder had been liquidated.215 This cannot be correct as the 25% shareholding must have passed to someone. However, this outcome helps demonstrate the flexibility of the Principle and the court’s ability to invoke it whenever it feels that it is required to ensure a just outcome.

Unanimity is easy easily analysed when legal and beneficial ownership in shares align, but in situations where there are beneficial owners which differ from the entities listed in the register of members of the company then the position becomes confused. In that situation, whose vote should be counted towards the Principle?

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214 Ibid 475
215 Randhawa & Ors v Turpin & Anor, [2016] EWHC 2156 (Ch)
In *Demite Ltd v Protec Health Ltd & Ors*, receivers sold the business of a company to a company connected to a director, without the formal approval of the shareholders. The company in question (Demite Ltd) had been a joint venture between a Dr Shober and a Mr Webb Peploe, each using offshore holding vehicles. They fell out. The secured creditor of the company appointed receivers, who sold the business and assets of the company to an entity set up by the secured creditor and Mr Webb Peploe. There were arguments about whether the receivers were validly appointed and, if so, whether the sale was valid to a party connected to the director even though shareholder approval was not sought. An agreement between Dr Shober and Mr Webb Peploe acknowledged that a newco would be established to purchase Demite's business. Park J held that this was insufficient to implement the Principle. He said: "My reason is that Dr Shober and Mr Webb Peploe, who signed the agreement, were not shareholders." He acknowledged that:

"Offshore entities typically look for guidance to principal beneficiaries elsewhere (in this case the UK), and will usually go along with what the principal beneficiaries want. I am also aware that sometimes the beneficiary professes to act where theoretically the offshore entity should, and that in such cases the offshore entity is likely to acquiesce in and adopt what the beneficiary has done. In my judgment that does not mean that, in a case where the underlying assets of the offshore entity are shares, the shareholder is the beneficiary and not the offshore entity. Nor does it mean that in this case the signatures of Dr Shober and Mr Webb Peploe on the 12 July 1996 agreement were the asset of Integro and Schroder Asia Nominees [the registered shareholders]."

He continued:

"the affidavits and exhibits do not clarify the exact relationship between the overseas shareholders and the domestic beneficiaries. Schroder Asia Nominees may hold its shares as a pure nominee for Mr Webb Peploe, but he has not said so in any of his affidavits. It seems fairly clear that Integro is not just a bare nominee for Dr Shober..."

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216 *Demite Ltd v Protec Health Ltd & Ors*, [1998] B.C.C. 638
217 Ibid para 11.3 (b)
218 Ibid para 11.3 (d)
When shares are held by an offshore vehicle there is usually a reason for it, typically a fiscal one, and in other contexts the persons concerned are not slow to asset that the resident individuals, though beneficiaries, are not the owners of the shares. I am not prepared to take a different view in this case.  

This is the correct decision for the wrong reasons. Formality in shareholder decision making is a default rule, designed to protect them from agency costs, which can be waived by them. Park J’s analysis is, even that the two shareholders were bare trustees for the individuals, the Principle could not be invoked by the individuals. The Principle embodies the concept of ignoring formality to identify decisions of substance, in this case if the registered shareholders were bare trustees then the Principle should have been capable of being applied by the beneficial owner, as they were the entity entitled to make ultimate decisions of substance. However, the link between the registered shareholders and the individuals was never explored/clarified: this should block the implementation of the Principle. Park J’s analysis was misdirected: beneficial ownership of shares should be the test for the Principle rather than the register of members.

Deakin & Ors v Faulding & Ors involved a company (wholly owned by the Fauldings) paying bonuses (to the Deakins) informally on an incorrect belief that company law in some manner required equality between managers and shareholders. The company had two shares, one held by Peter Faulding (who managed the company) and one held by his mother, Nora (who “just went along” with her son). When Mr Faulding attempted to recover the bonuses from the Deakins (directors of the company) on the grounds of lack of shareholder approval, the Deakins invoked the Principle. When Faulding argued that the Principle could not be invoked because Nora had not consented, Hart J stated:

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219 Ibid paras 11.3(g) - 11.3(h)
220 Deakin & Ors v Faulding & Ors 2001 WL 825752
221 Ibid para 114
222 Ibid para 119
"We are concerned here with the application of the equitable rule that a fiduciary must not profit from his office without the consent of the corporators. Where a person (Peter Faulding) has an equity to compel a consent, I see no reason why equity should not have regard to the position of the beneficial as opposed to the legal owner in its application of the rule."\(^{223}\)

This analysis viewed the issue as one of equity - a beneficial owner can compel his nominee to act in a certain manner, and therefore the Principle should apply to beneficial owners. Hart J held that either Nora was holding her share as a bare trustee for Peter, or had delegated to Peter her authority in acting as a shareholder - in either event the Deakins were entitled to retain their bonuses. This is more coherent than \textit{Demite}, but it remained unclear as to whether legal or beneficial owners (or indeed both) were required for the Principle to apply.

The issue arose again in \textit{Domoney v Godinho & Others}.\(^ {224}\) In this case, \textit{Deakin v Faulding} was contrasted with an Australian case, \textit{Jalmoon Proprietary Limited (in liquidation) v Bow}\(^ {225}\) which stated that the Principle only looked to the register of members. When reviewing the two interpretations, Lindsay J stated:

\begin{quote}
"There are, indeed, further cases on the point and there may be some contest on the law, but if there is to be here contest on the law, it is one best dealt with on the basis of found fact rather than on the basis of assumptions and possibilities and uncertainties."\(^ {226}\)
\end{quote}

In \textit{Sahar v Tsitsekkos & Ors},\(^ {227}\) Mann J reviewed the same authorities. When reviewing \textit{Deakin v Faulding}, he stated:

\begin{quote}
"It seems that Hart J was plainly prepared to accept that the consent of a beneficial owner of a share was sufficient for Duomatic purposes. In the passage I have cited he seems to treat the matter as
\end{quote}
a question of principle - the beneficial owner (at least on the facts of his case) could have compelled the consent anyway so it was right to take that consent into account. However, it is also right to point out that part of his reasons seems to have been on an agency basis. The beneficial owner was argued to be acting as agent of the nominee - that is apparent from paragraph 121 of his judgment.”

He continued:

"It seems to me that the point of principle relied on by Mr Tager (namely that the Duomatic principle can never apply to the consent of a beneficial but non-registered shareholder) is not clearly right, and it should not be determined on a summary judgment application such as this. In fact my view is that as a statement of principle it is wrong. I do not see why in an appropriate case the principle should not operate in relation to the consent or informed participation of a beneficial owner of shares if the facts justify it. It may well be that the appropriate analysis is the agency argument - in many cases it will doubtless be possible to argue that a nominee shareholder has left all the real decisions to his beneficiary so that technically the consent of the beneficiary is the consent of the registered shareholder.”

Mann J also avoided deciding the issue, instead stating that somehow this question of law is a question of fact. This was not a neat conclusion.

The issue was resolved in Re: Tulesense Limited, which involved a company with 50% of the shares held by each of two branches of the family. The question was whether a director had been appointed by the shareholders via the Principle (in which case he remained a director) or by the board (in which case he did ceased to be a director at the next AGM). At the time of the putative application of the Principle, legal title to both shares was held by the father of the director - one in his own right, and one in his capacity as executor, with the beneficiaries being the other side of the family. The director argued that, as his father held the legal title to both shares, he could invoke the Principle. He further argued that, should that not be correct, then the assent of one of the beneficial owners would

228 Ibid para 64
229 Ibid para 67
230 Re: Tulesense Limited [2010] EWHC 244 (Ch)
suffice as multiple beneficial owners could compel the share to be transferred, jointly, into their own name, and if they did so then any one would be entitled to vote the share at a general meeting. Whilst Newey J appreciated the ingenuity of the argument, he rejected it, stating:

“In the first place, in my judgment if an individual who holds some shares for himself and other shares as a trustee or executor has expressed assent, he is not to be taken to have given that assent in respect of the shares held as trustee or executor if he did not intend or purport to be making a decision in relation to those shares, at any rate if it would have been apparent to an observer that the assent was not intended to extend to the shares held as a trustee or executor. To take an example with similarities to the case before me, suppose that an individual who held one of a company’s 100 issued shares beneficially and 99 as a bare trustee concluded that a director should be appointed. The requirements of the Duomatic principle should not, without more, be taken to be satisfied were it evident that the shareholder had considered that it was for the beneficial owner of the 99 shares, and not for him, to make decisions as regards those shares.”

This does not clearly answer the issue. However, Newey J’s argument is important in the negative - it is not enough merely to be the registered owner of shares in order to implement the Principle. The legal shareholder's need to consider that any decision he makes benefits the beneficial owner should be seen in a broader light: whether a trustee legal shareholder can invoke the Principle depends on the constitution of the trust itself. If the trust authorises the trustee to exercise all rights, then the Principle may be invoked by him. Conversely, if the legal shareholder is acting merely as a bare nominee for a beneficial owner then they will not be able to invoke the Principle: the analysis shifts to the trust rather than onto mere legal ownership. By acknowledging that there is more to the analysis than mere legal ownership, Newey J provided a normatively correct result. He did, however, “assume, without deciding”232 that this was sufficient and therefore did not provide a clear ratio for future application.

231 Ibid para 40
232 Ibid para 42
Newey J then reviewed whether the assent of merely one beneficial owner would suffice. He decided:

"Whether or not, however, the assent of all of the beneficial owners of a share will suffice, I do not think that the assent of just one of a number of such owners normally will. First, while the beneficial owners of a share, acting together, might be able to require the share to be transferred to them (compare the rule in Saunders v Vautier (1841) Cr & Ph 240), no individual beneficial owner could do so. Further, even supposing that a share were transferred to its beneficial owners, with the result that they became joint holders, it would not necessarily follow that any of them could vote in respect of the share. As noted above, article 63 of the 1948 Table A provided for the vote of the "senior who tenders a vote" to be accepted. In the circumstances, it seems to me that, unless perhaps the legal owner of a share had entrusted decisions in respect of a share to just one of its beneficial owners, the assent of only one such owner cannot be enough for Duomatic purposes."233

This follows the normative analysis. Unanimity reduces agency costs amongst shareholders. It would therefore be perverse if unanimity was required only between shareholders and not also between all of those who have a beneficial interest in the shares and have some form of decision making role in the trust.

When someone holds a share other than entirely for themselves, it is necessary for them to actively consider the relevant matter in their capacity as trustee. It is not, however, necessary for shareholders of a company to consciously make a decision as shareholder. Re Conegrade Limited234 concerned substantial property transactions approved at a board, rather than general, meeting. All shareholders were directors and all were present at the board meeting. Lloyd J stated:

"I do not see why, at any rate where there has been a meeting attended by all those who were entitled to attend and vote at a general meeting and that meeting has considered the matter and has resolved, in terms, that the company shall enter into the particular transaction, the fact that the Minute is headed “Board Meeting”

233 Ibid para 43
234 Re Conegrade Limited, [2002] EWHC 2411 (Ch)
rather than “General Meeting” and was not convened on the notice proper for a General Meeting and was attended by a Director who does not hold shares, should make it impossible to regard section 320 as having been satisfied.”

Similarly, NBH Ltd v Hoare & Ors held that the approval to a substantial property transaction by a director who was also the sole shareholder of the company was sufficient to implement the Principle. The judge in this case was Park J, who also adjudicated Demite, where he had expressed doubt as to whether the Principle was capable of application to this particular statutory requirement. Reviewing his earlier analysis of the same authorities, he decided in NBH that the Principle could apply to these provisions. He further concluded that the shareholder had, in some way, given their prior approval (which was required under the relevant section) and therefore the Principle was applied. This is consistent with Younger LJ’s approach in Express Engineering. It also clarifies that, whilst trustees need to consider their capacity before applying the Principle, shareholders otherwise do not need to for the Principle to apply. This matches the theoretical position that would be expected: whilst trustees owe fiduciary duties to their beneficiaries, ‘pure’ shareholders do not owe fiduciary duties to other parties in the exercise of their vote. Third parties can have a legitimate interest in how control of the trust property is exercised (in this case the vote of the share), which is not present in respect of a ‘pure’ shareholder exercising their vote: in the former case, more than just a legal titleholder’s needs to be taken into account whereas in the latter, only that whim is relevant.

Where a decision only needs to be taken by one class of shareholders, the Principle can be implemented by that class alone. In Re Torvale Group Ltd, the consent of the holders of one class of share was required prior to the company granting a debenture. The Principle was applied on the basis of the informal consent of the sole holder of only the required holder of shares.

235 The relevant section of the Companies Act 1985
236 Conegrade (n234) lines 11 - 21
237 [2006] EWHC 73 (Ch)
238 Ibid para 53
Accordingly it is also important to ascertain *whose* consent is required to a certain course of action and apply the Principle to that category of actors.

### 4.2.2. WHAT DO THEY NEED TO DO?

It is necessary to review what the relevant shareholders must unanimously do. There are three elements of this: firstly, whether unanimity is required in all activities; secondly, how the agreement needs to manifest itself; and thirdly, how informed a shareholders' consent requires to be.

Dealing with these in turn:

**(a) Constant Unanimity?**

Just because unanimity is necessary for the Principle does not mean that it is constantly required. Thus in *In re Bailey, Hay & Co. Ltd*, an invalid general meeting resolved to place the company into voluntary liquidation. All shareholders attended, even though some shareholders knew that the meeting was invalid. The resolution was passed by 50% of shareholders, with the other shareholders all abstaining. One abstaining shareholder subsequently raised proceedings as the meeting was invalid. Reviewing *Express Engineering* and *Parker and Cooper*, Brightman J concluded:

"I consider that on the particular facts of this case all the corporators ought to be treated as having assented on December 9, 1965 [the date of the invalid general meeting], to the company being wound up on that day. In my judgment, the case falls within the principle of the decisions in the two cases I have mentioned. Admittedly three of the five corporators did not vote in favour of the resolution, but they undoubtedly suffered it to be passed with knowledge of their power to stop it."  

He continued:

"The conclusion is that they outwardly accepted the resolution to wind up as decisively as if they had positively voted in favour of it. If corporators attend a meeting without protest, stand by without
protest while their fellow-members purport to pass a resolution, permit all persons concerned to act for years on the basis that that resolution was duly passed and rule their own conduct on the basis that the resolution is an established fact, I think that it is idle for them to contend that they did not assent to the purported resolution.\textsuperscript{241}

There are two observations to be taken from this. Firstly, Brightman J viewed the abstaining members as being estopped from objecting to the resolution. This is a just result - if the now-objecting shareholders had voted against the meeting rather than abstained, then the resolution would have failed. Even if not, the shareholders would have made their objections to the course of action clear throughout the process. Secondly, it shows that the Principle operates on two distinct levels. Firstly, the procedural level - shareholders deciding whether to waive formality in respect of a particular question. Secondly, points of substance - the actual answer to the question raised. In the case of Bailey Hay, shareholders waived the formality requirements of the meeting. Having done so, they could not object to the substantial outcome of that informal meeting. It is difficult to envisage situations whereby a shareholder agreed with the outcome of a decision, but objected to the manner in which it was made enough to try to overturn the underlying decision. Accordingly, if shareholders unanimously either accept informal processes, or agree on a point of substance, then the Principle can be held to apply.

This point was appealed in Schofield v Schofield and Others,\textsuperscript{242} where, a father (Neil) and son (Lee) were directors of a company. The father’s Belize holding entity held 99.9% of the shares and the son held 0.1% and was sole director. The father's offshore vehicle requisitioned a general meeting of the company to replace the son as a director. The company secretary convened an invalid meeting, the son voted against the motion. First instance held that the son had not in any way acquiesced to the invalid meeting and therefore the Principle cannot have been invoked. The father

\textsuperscript{241} Ibid 1367B
\textsuperscript{242} Schofield v Schofield and Others [2011] EWCA Civ 154
appealed – as the son had submitted a motion to delay the meeting, he had acquiesced to the meeting and therefore any decision made by it. The Court of Appeal rejected this, holding:

“What all the authorities show is that the Appellant must establish an agreement by Lee to treat the meeting as valid and effective, notwithstanding the lack of the required period of notice. Lee’s agreement could be express or by implication, verbal or by conduct, given at the time or later, but nothing short of unqualified agreement, objectively established, will suffice.”

By attending the meeting in order to object to it and attempt to delay it, the son had not provided his consent to it. Instead:

“Lee’s participation at the meeting was, therefore, conditional. His position throughout was that the meeting had not been properly called, but, if and insofar as (contrary to his stated position) it was a valid meeting, he responded to the various proposals suggested by Mr Berry in the way that he did. That was not an agreement by Lee, as shareholder, to treat the meeting and the resolutions passed at the meeting as valid and effective. There was no objective agreement by him within the Duomatic principle.”

This follows Bailey Hay. In Schofield, there was clearly no unanimity between shareholders in respect of the substantial outcome. Attending an invalid meeting to object to it taking place is not unanimity of process either. This analysis is straightforward for a shareholders’ meeting, but more difficult in the context of a written resolution. For example, if an evidently flawed written resolution were circulated that a dissenting shareholder, noting its flaws, merely destroyed then such shareholder may be held to have acquiesced to the passing of the resolution. However, as a written resolution is passed by a requisite amount of the members as a whole rather than the requisite amount of those who respond, and Parliament explicitly stated that failures by directors to comply with the relevant section of the act will not invalidate any such resolution then these concerns are minimised.

243 Ibid para 32
244 Ibid para 41
245 Companies Act 2006 s296(4)
246 Companies Act 2006 s291(7)
This shows that, whilst unanimity in both substance and process is not required for the Principle to be held to apply, one of the two is required for the Principle to be implemented.

(b) Outward Manifestation

To invoke the Principle, the shareholders must actually do something and outwardly manifest that action in some objectively verifiable way. In *Re D'Jan of London Ltd*, a company director, Mr D'Jan, signed an incorrect insurance form which invalidated the insurance of a premises. Liquidators raised an action against Mr D'Jan for misfeasance by way of negligence, and he argued that whilst the company was solvent its shareholders (he and his wife) would have ratified his misfeasance and so he was not liable. Hoffmann LJ (as he was then) held that this could not be the case:

"Mr D'Jan did not realise that he had given a wrong answer until the insurance company repudiated. By that time the company was in liquidation. In my judgment the Multinational principle requires that the shareholders should have, whether formally or informally, mandated or ratified the act in question. It is not enough that they probably would have ratified if they had known or thought about it before the liquidation removed their power to do so."*248*

This matches the normative position reached in respect of the Principle — the shareholders must apply it whilst they retain the residual rights in respect of a company. But what do they actually have to do?

In *Re Tulesence Limited*, Newey J stated:

"I do not accept that a shareholder's mere internal decision can of itself constitute assent for Duomatic purposes. I was not referred to any authority in which it had been decided that a mere internal decision would suffice. Further, for a mere internal decision, unaccompanied by outward manifestation or acquiescence, to be enough would, as it seems to me, give rise to unacceptable uncertainty and, potentially, provide opportunities for abuse. A company may change hands or enter into an insolvency procedure; in either event, it is desirable that past decisions should be objectively
verifiable. In my judgment, there must be material from which an observer could discern or (as in the case of acquiescence) infer assent. The law applies an objective test in other contexts: for example, when determining whether a contract has been formed. An objective approach must, I think, also have a role with the Duomatic principle."

This requires some outward manifestation of the Principle, and has been quoted with approval in Schofield. In Re Home Treat Ltd, a company's objects did not permit it to carry out the business that the company had always carried out. Its administrators applied to the court to carry on this business, which would realise more for the creditors. Harman J stated:

"That being so, it was thought right to make this application in order that the court might give a direction that the administrators do continue with that course of conduct. It is plainly in the interest of all the creditors, and probably in the interests of the shareholders and members of the company as well, since they have guaranteed the company's obligations under its mortgage to the bank over the nursing homes. It is obvious that the more that is realised by the administrators for the assets, which so far as charged will be payable to the mortgagee, the less call will be made on the members' guarantees. Thus a better realisation of the assets is to the advantage of the members even if there never comes to be enough money actually to pay out any money to contributories as members.

Thus, the object of the application is plainly a beneficial one and if there be any way of allowing this order to go I should seek to make it."

As with so many cases reviewed in respect of the Principle, the court was keen to hold that the administrator was able to continue the business on some equitable grounds. It was suggested that the Principle may be invoked, but there was no evidence of assent. Harman J reviewed certain of the authorities and concluded that:

"The decisions show that the law is that the consent of all members expressed together is as good as a special resolution. It is also clear

249 Turtlesense (n230) para 41
250 Ibid para 32
251 Re Home Treat Ltd [1991] B.C.C. 165
252 Ibid 167
that acquiescence by shareholders with knowledge of the matter is as good as actual consent. In this case the silence of Mr Mahanan is, in my view, as good as acquiescence and establishes that he as much as his wife had assented by conduct to this change in the objects of the company.”

Accordingly, as with Bailey Hay, acquiescence can, count towards assent for the purposes of the Principle.\(^{254}\)

However, it some form of objectively verifiable action or acquiescence appears necessary.

(c) Informed Consent

If inaction can trigger the Principle, how informed does the action or inaction have to be in order to qualify towards the Principle? In *EIC Services & Ors v Phipps & Ors*\(^{255}\) Neuberger J (as he then was) remarked:

> “If a director of a company informs shareholders of an intended action (or a past action) on the part of the directors, in circumstances in which neither the directors nor the shareholders are aware that the consent of the shareholders is required to that action, I do not think that it is right, at least without more, to conclude that the shareholders have assented to that action for Duomatic purposes. As a matter of both ordinary language and legal concept, it does not seem to me that, in such circumstances, it could be said that the shareholders have \"assent[ed]\" to that action. The shareholders have simply been told about the action or intended action, on the basis that it is something which can be, and has been or will be, left to the directors to decide on, and no question of \"assent\" arises.”

It insufficient for shareholders to know that the action is occurring, instead they need to know that their approval (even by acquiescence) of the matter is actively being sought. Neuberger J continued:

> “Before the Duomatic principle can be satisfied, the shareholders who are said to have assented or waived must have the appropriate

\(^{253}\) Ibid 168  
\(^{255}\) (n154)  
\(^{256}\) Ibid para 133
or “full” knowledge. If a shareholder is not even aware that his "assent" is being sought to the matter, let alone that the obtaining of his consent is at least a significant factor in relation to the matter, he cannot, in my view, have the necessary "full knowledge" to enable him to "assent", quite apart from the fact that I do not think he can be said to "assent" to the matter if he is merely told of it."

This matches the this thesis' analysis. Formality reduces agency costs between management and shareholders, and also between dominant and minority shareholders. Accordingly, if Neuberger’s proposition were not the case, managers could swamp shareholders with excessive irrelevant information and rely on a lack of objection to invoke the Principle for some hidden matter. Following Bailey Hay, acquiescence (and, by extension, assent) should only count towards the Principle if the shareholders in question are fully informed of the matter and their need to assent.

In Vinton & Another v Revenue and Customs,258 a tax commissioner had to decide whether an issue of shares was a mere subscription (which was tax disadvantageous) or a reorganisation (which was tax advantageous). The facts were confused- they intended to conduct the transaction in a tax advantageous way (and could have done), but a did not know how to do so. An attempt to invoke the Principle (as all shareholders wanted the transaction to be tax advantageous) failed, with the special commissioner stating:

"I have considered carefully the Duomatic principle and I do not see that it can be applied to this case so as to give the character of a rights issue to what was expressed as a share subscription. It may be helpful in dealing with formalities that should have been complied with at the meeting but I do not see that it is capable...the fact that he suggests alternatives illustrates the level of confusion that exists since it is possible to imagine several ways in which varying degrees of IHT advantages could have been obtained and I do not think that Duomatic can be extended so that, out of a range of possible activities, the one that gives the more suitable IHT result is

257 Ibid para 135
258 Vinton & Another v Revenue and Customs [2008] WL 371054
selected... I do not think that the members of the group did understand the relevant facts. Accordingly I dismiss the appeal."259

This demonstrates that the Principle requires unanimous consent to the specific action itself rather than vague agreement as to the ultimate desired result.

The authorities seem to present a simple and unequivocal picture of how the Principle will work in practice: once it is established that the Principle can apply to a specific situation, it is necessary to see whether all entitled to decide the issue (as shareholder, beneficial owner or by operation of a trust or delegation) have indeed done so, then to establish whether they clearly, objectively and objectifiably did so in full knowledge of the facts and that their approval was required. However, within each area of analysis, there exists a grey area where the authorities often contradict, making it difficult to conclude that the roadmap outlined would always be followed.

259 Ibid, paras 72-73
5. **Nature of the Principle**

Having reviewed the modern test we can discuss the nature of the Principle: firstly in practical terms, secondly to characterise its nature.

### 5.1. **Practicalities**

There are 2 aspects of practicalities of the Principle: the type of company and filing implications.

#### 5.1.1. **Type of Company**

We have only seen 3 cases involving public companies and the Principle. *Re Finch (UK) plc* involved a plc with only two shareholders, *Bairstow v Queens Moat Houses plc* involved directors of a plc attempting to invoke the Principle in respect of decisions of the plc's subsidiaries (private) companies, and *Re Torvale Group plc* involved the discussion of the Principle in respect of one class of shares only, which were all held by one institutional investor in the company: the Principle has not, empirically and as judicially tested, concerned any Berle/Means Companies. Indeed, it has not concerned any companies whose shares were publicly traded. The Principle is likely to apply to close companies.

Bainbridge's arguments for director primacy (as he acknowledges) are weaker for close companies. This is important for the Principle, as close companies are likely to have lower agency costs between shareholders (as a whole) and management. The Principle is only likely to be relevant in respect of agency costs between majority and minority shareholders and between shareholders and creditors. Requirements as to unanimity effectively solve the former, leaving interactions between shareholders and creditors as the relevant agency costs when considering the Principle. These are minimised by
the requirement that the Principle can only be invoked by the shareholders where the rule is for their benefit, and therefore prevents the shareholders from using the Principle to increase agency costs to creditors. Accordingly, where the shareholders are able and willing to take control of the actions of the company, they are not able to hide behind formality that they have ignored. The protections that shareholders have in a company are almost exclusively designed to protect them against self-dealing by management which is irrelevant if shareholders are taking a more active role than they would in a Berle/Means Company.

Ultimately, the Principle embodies the ultimate extension of the Contractarian analysis: shareholders are able to vary the corporate contract. But this freedom that the shareholders have must have a counterbalance - following a variation from the default norm of management by the board, the shareholders should lose their protections of formality.

5.1.2. Filing Obligations?

We have seen that the Principle can operate to change the constitution of a company. Whilst *Cane v Jones* side-stepped the issue, subsequent cases have clarified the issue (for example, in *Re: Home Treat* the Principle operated to amend the objects clause of the memorandum of association of the company). This makes logical sense - in *Ho Tung v Man On Insurance Company Limited*,\(^\text{260}\) Lord Davey opined that a special resolution was only “mere machinery for securing the assent of the shareholders, or a sufficient majority of them.”\(^\text{261}\) The Principle is another procedure which can demonstrate the equivalent assent, and therefore should have the same effect. There are clear reasons for compelling any changes to a company's

\(^{260}\) *Ho Tung v Man On Insurance Company Limited* [1902] AC 232

\(^{261}\) Ibid 236
constitution to be registered at Companies House,\textsuperscript{262} which currently applies to special resolutions of the company.\textsuperscript{263} The same analysis should apply to any equivalent change made by the Principle. Theoretically, the objective nature of the operation of the Principle should mean that there will be \textit{something} to register, as one of the rationales given for requirements of objectivity is that:

“\textit{the importance that an accurate record be kept of the true capitalisation of a company by its shares is such that it is not open to the members to waive compliance with this aspect of the requirements of s164 and s381A in reliance on the Duomatic Principle.”}\textsuperscript{264}

If a special resolution is passed but not filed it does not affect the validity of the resolution, but an offence is committed by every officer of the company.\textsuperscript{265} A director, however, will always be aware of a special resolution: either this will be passed at a shareholders' meeting (which involves directors unless conducted via the Principle)\textsuperscript{266} or the written resolution procedure (which again involves directors unless conducted via the Principle).\textsuperscript{267} No equivalent requirement that a director be made aware of the operation of the Principle exists. Directors could be penalised by the Principle operating as equivalent to special resolutions. However, the courts have been keen to relieve innocent parties in this situation - for example the administrators in \textit{Re Home Treat}. We have seen that the Principle is most commonly implemented where there is a close company with, frequently, commonality between directors and shareholders, which further reduces the risk posed by this line of argumentation. This possible liability on directors for the actions of shareholders could further encourage directors to diligence whether the shareholders have operated the Principle. Third party creditors are also protected from the lack of knowledge of any changes made

\textsuperscript{262} E.g. White Paper (n254) para 2.25
\textsuperscript{263} Companies Act 2006 s30
\textsuperscript{264} \textit{Kinlan v Crimmin} (n183) para 45
\textsuperscript{265} Companies Act 2006 s30(2)
\textsuperscript{266} Companies Act 2006 ss302-305
\textsuperscript{267} Companies Act 2006 ss291-292
by the company so long as they are acting in good faith following the rule in *Turquand's case.*

5.2. **Legal Characterisation**

This thesis identified a test for application of the Principle that appears universal and objective. However, on most issues there are conflicting cases and outcomes when it comes to the operation of the Principle.

In *Duomatic*, directors of the company argued payments made to them should not be recovered by a liquidator due to the Principle. The court held that whilst this was correct from a decision making perspective, a preference shareholder was entitled to receive notice of the payments: failure to provide such made the payments recoverable. This conflicts with *Re Torvale*, where corporate approvals to the grant of security in accordance with the company’s articles were not obtained, and the relevant shareholder could not remember consenting to the grant of security, although had no reason to think that they did not. If the Principle did not apply to *Duomatic*, then *Re Torvale* should have produced the same result. However, the analysis can be reconciled by viewing the Principle as a form of equity. *Duomatic* involved directors receiving *ex gratia* payments from the company, in *Torvale* the director funded the company and received security as a result. It therefore may be "just" that the underlying transaction of the former was rejected by the court whilst the latter was accepted.

*Torvale* also does not sit comfortably with *Re Finch* or *Re D’Jan*. In *Finch*, the court held that the shareholders had only consented after the company entered insolvency, after they lost their ability to direct the actions of the company. In *D’Jan*, the court held that the

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268 *Royal British Bank v Turquand* (1856) 6 El. &Bl. 327
shareholders (also the directors) would have ratified wrongs were they asked to do so, but had never done so. If the Principle were an objective rule of law, these three cases should align: either evidence of shareholder consent is required, or it is not. The difference in outcome once more points to the flexibility of the Principle in achieving what the court believes is a fair outcome in the case as a whole. Thus Deakin v Faulding can be differentiated from Duomatic on general equitable grounds: whilst both involved ex gratia payments made to directors, the court felt that this was a fair outcome in Deakin whereas it did not in Duomatic. The court will decide whether it should bless the transaction on a case-by-case basis, and use the Principle to do so: if it decides to not bless the transaction then it can utilise the technicalities of company law to strike it down, an approach first obliquely seen in Re Barry Artist. Niltan Carson is therefore less anomalous than thought: the court decided that one party should not be able to rely on technicalities of corporate law to challenge conduct by an equitably-innocent party, and used the Principle to bless the transaction. This is the ultimate heart of the Principle.

The courts do not often expressly refer to equity in their discussion of the Principle. Whilst equitable remedies have been raised, and the background to a lot of the analysis concerns equitable concepts, the only case which actively flags an equitable element to the Principle is EIC v Phipps, in which Neuberger J (as he then was) characterised the Principle as:

"where the articles of a company require a course to be approved by a group of shareholders at a general meeting, that requirement can be avoided if all members of the group, being aware of the relevant facts, either give their approval to that course, or so conduct themselves as to make it inequitable for them to deny that they have given their

\(^{269}\) E.g. (n227)  
\(^{270}\) E.g. (n220)
approval. Whether the approval is given in advance or after the event, whether it is characterised as agreement, ratification, waiver, or estoppel, and whether members of the group give their consent in different ways at different times, does not matter.\textsuperscript{271}

Given that we have seen that rules of equity under English law are those which provide a “gloss” on law to ensure its just application, it is difficult to conclude that the Principle is anything but a tool for a court to arrive at an equitable outcome.

Elements of the modern Principle outlined in chapter 4 are only guidelines: the Principle is an option that the court can utilise if it wishes to let something remain valid despite inaccuracies in procedure. Viewing the Principle thus shows why the buyback cases reach contradictory positions: if the Principle were of universal, objective application then \textit{RW Peak} and \textit{BDG Roof Bond} would have concluded the same outcome as \textit{Kinlan v Crimmin} and \textit{Dashfield v Davidson}. The difference in outcomes is due to the Principle’s role as an aid to the court to achieve a just result in the case. This applies to whether a beneficial owner of a share should be able to apply the Principle: if there was an objective, universal application of the Principle then there is no reason for the difference between \textit{Demite}, \textit{Domoney} and \textit{Jalmoon} on one hand, and \textit{Deakin} and \textit{Tulsesense} on the other. Only by acknowledging that the Principle is a part of the court’s discretionary powers to ensure just outcomes can all authorities be reconciled. Hence we can compare the strict approach

\textsuperscript{271} \textit{EIC} (n154) para 122
to shareholder approval taken in *Finch* and *D’Jan* with relaxed approach in *Conegrade* and *NHB v Hoare*: the former two cases involved wrongs by the directors, the latter two cases involved transactions which all sides acknowledged were for fair value.

This approach is not surprising: calls to codify the Principle were rejected precisely to maintain its flexibility. However, the flexibility of the Principle undermines its normative certainty. We cannot be certain that the test outlined above will be followed by a court. This leads to a lack of certainty when applying the Principle. The normative conclusion reached at the beginning of this thesis is that the Principle should apply universally as shareholders should be able to informally conduct the business of the entity to which they retain residual rights and control over. The flexibility of the Principle undermines this. If the shareholders in *RW Peak, BDG Roof Bond, Demite, Duomatic, Vintan v HMRC* (and the other cases where the application of the Principle was rejected) had approved the relevant transactions through formal channels then they would have been valid. As it was, the court was able in each of those circumstances to reject application of the Principle either on the factual grounds of the case (which vary greatly) or on grounds that the Principle was not available to the specific technicalities of company law in question. By attempting to utilise informality, the corporate participants created a possibility whereby a court would look to the merits of the transaction to see whether they should use the Principle, rather than
merely if the appropriate approval was received: as seen in *Re Barry Artist*. If shareholders attempt to rely upon the Principle then the merits of their decisions will be analysed by the court: but not expressly and overtly. The courts hide the equity and fairness analysis behind a veil of formal compliance with the Principle. Thus judicial analysis has concentrated on whether or not the Principle can apply rather than the just nature of its application: even if this involves creative differentiation from otherwise analogous cases. This risks making shareholders believe the Principle is of objective and universal application when it is not. This juridification of the court’s ability to look at the underlying merits of the transaction from the company’s perspective is pernicious: by hiding behind technical analysis, the court is hiding what it is really doing in cases purporting to argue the Principle.

5.3. **Nature of the Principle**

Grantham calls the Principle outdated. He thinks the Principle harks back to a Victorian view that the shareholders retain control over the activities of the company, which they do not under modern company law.\(^{272}\) For Grantham, the Principle confuses divisions between directors and shareholders. Watts disagrees as it remains open to shareholders to amend their articles to assume management of the

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\(^{272}\) Grantham (n1) 269-270
company.²⁷³ It is respectfully submitted that both miss the point. We have seen that normatively, Grantham's view is incorrect. Further, the cases have been concerned with decision making by shareholders: when ascertaining whether the shareholders have properly approved a transaction. The primary exception been in respect of the activities of directors: whether shareholders ratified their wrongs. The Principle has applied to decision making by the company, but not actions undertaken by the company: it has only arisen in circumstances where action of directors has been challenged due to infelicities of internal procedure, and has not arisen because shareholders have undertaken action directly. The question is mostly whether shareholders approved the action, not whether the shareholders have undertaken the action themselves. Seen this way, the Principle can be viewed as an aspect of the rule in Turquand: a good faith third party is entitled to assume that the company has complied with its own internal procedure. Given the flexibility of the Principle outlined above, however, this is merely one facet of the Principle that can be displayed in a particular case.

Ellis has described the Principle as being "a principle without form", noting that despite the lack of codification under the Companies Act 2006:

²⁷³ Peter Watts, 'Informal unanimous assent of beneficial shareholders' (2006) 122 Law Quarterly Review 15, 19
"the fact that many of the procedural formalities which existed under the previous Companies Act still remain under the 2006 Act (even for private companies) indicates that Parliament still considers formal procedures to have significant worth. As such, the tension between compliance and waiver still remains and the courts are still being asked to make distinctions between adherence to statute and “justice” if the circumstances demand it.

It is submitted that these tensions should be resolved. However, a suitable solution may be difficult to come by. Codification of the principle may fail to bring about any true certainty and it is arguable that this would only perpetuate the current situation.

Perhaps, instead, it is time for the principle to be abolished (despite the views of the Company Law Review). A less drastic approach would be to limit its application to lack of compliance with the articles. This would, at least, be a virtuous circle. Alternatively, if the courts are capable of treating certain statutory provisions as otiose in certain situations, why is it not possible to do the same through legislation?"\(^{274}\)

This analysis accepts and acknowledges the flexibility of the Principle, but proposes that it be limited to only items under the articles. The halfway house proposed by Ellis is unsatisfactory, as it acknowledges that aspects of the articles should be waivable by the shareholders, but refuses to apply this principle to any provision of statute that exists (however explicitly) for their benefit. It would be a resource-intensive exercise to provide an exhaustive list of areas of application of the Principle, which would quickly become outdated. Despite the downsides the flexibility of the Principle, it may be better that such flexibility exists, so long as shareholders are clear that utilising informality will risk a court examining the merits of the specific proposed transaction in a manner which could be avoided by merely undertaking activities formality.

\(^{274}\) Ellis (n4) 266
When it comes to Australian law, Meagher JA held that the essence of the Principle was one of waiver.275 On the other hand, Ford's Principles provides 3 views of the Principle: the limited view (that shareholders can meet without the proper notice requirements), a wider view (that the Principle is a form of equitable estoppel) and an even broader view (that the Principle involves the lifting of the veil of incorporation, with the shareholders binding the company).276 Ford's Principles avoids a general conclusion for the reason that the Principle can be held by the court to be any of the 3, depending on the context. Ultimately, the legislature and the courts have maintained the flexibility for the Principle to be waiver, estoppel, agreement, ratification, or any other formulation of this wording, depending on the circumstances. This flexibility makes the Principle difficult for study, as it is not certain that satisfying the guidelines identified will ensure that a court holds the Principle as applying. The court’s ability to decide the Principle’s application differently in analogous circumstances, provides its practical strength and normative weakness. It would be easier if courts began acknowledging the Principle’s role as a tool to achieve an equitable end. The Principle is, therefore, not an embodiment of a Contractarian position, Shareholder Primacy or even Director Primacy: it embodies judicial primacy in informality of shareholder decision making.

275 Herman v Simon (1990) 8 ACLC 1094, as per EIC (n154)
6. **Conclusion**

The Principle has firm theoretical groundings in economic examinations of the historical and modern company: Contractarian analysis provides for it to be applied strongly. It has been present and implicit in company law ever since *Salomon*. Its theory and history can be reliably traced through the case law to the modern day. It is even possible to establish workable guidelines to establish when it is likely that it will be applied. The way to do this is firstly to establish whether the relevant rule exists for the benefit of the shareholders. If it does, then the next step is to ascertain whether the right people gave the correct level of consent in an objectively verifiable enough manner.

Yet this analysis cannot definitively predict a court's attitude in any given circumstance. Closer examination of the discrepancies between cases on the same subject area leads to the unsatisfactory conclusion that courts decide whether to apply the Principle depending on how just the outcome of doing so would be, rather than strictly applying the legal tests to the factual matrix. There are two primary issues with this approach. Firstly, this thesis commenced its analysis by normatively concluding that there are certain circumstances in which the shareholders of the company should be able to invoke the Principle. The court's approach conflicts with this normative position. Whilst the Principle remains in its current form, shareholders would be better advised to utilise prescribed formality for transactions as that will prevent a court from subsequently analysing its merits. This undermines their ability to rely on the Principle, and makes it fit less neatly into the Contractarian normative framework of modern company law.

The second issue is more serious. The nature of the Principle (being an *ex post* blessing of a transaction which was effected informally should the circumstances make the court feel it is just to do so) is currently hidden. Courts apply a textual analysis of the authorities on the Principle, despite its flexibility providing maximum discretion to the court, encouraging participants in corporate life consider the Principle a right the shareholders
have, rather than a court’s ratification of an informally approved transaction after the fact on the transaction’s merits. The current textbook treatment of the Principle mischaracterises it as being invokable by shareholders: instead it remains a purely judicial remedy to overcome potential invalidities in otherwise valid transactions. This mischaracterisation is not in the interests of students of corporate law or shareholders.

This thesis’ reluctant conclusion, therefore, is that despite the normative analysis suggesting maximum opportunity for informality at the options of shareholders, despite a historic chain of cases that purport to provide a strong lineage and consistency to the Principle, and despite a body of case law that provides an apparent set of guidelines for the Principle’s application: if shareholders want certainty that a court will not seek to re-open the merits of transactions which require their approval then they should undertake this through prescribed formal means and avoid attempting to rely on the Principle. The Principle instead remains a tool for an English court to achieve an equitable outcome: given that we have seen that Scots law does not contain a concept of “equity”, it can only be a matter of speculation as to how a Scottish court can utilise the Principle.  

277 A question, very sadly, outside the scope of this thesis.
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