SUPREME COURT OF QUEENSLAND

CITATION:	*Bundaberg Sugar Ltd & Anor v Isis Central Sugar Mill Co Ltd* [2006] QSC 358
PARTIES:	**BUNDABERG SUGAR LIMITED ACN 077 102 526** (first plaintiff) and **BRANCHVALE PTY LTD ACN 061 770 152** (second plaintiff) **v** **ISIS CENTRAL SUGAR MILL COMPANY LIMITED ACN 009 567 078** (defendant)
FILE NO:	BS1591 of 2005
DIVISION:	Trial
PROCEEDING:	Trial
ORIGINATING COURT:	Supreme Court of Queensland
DELIVERED ON:	5 December 2006
DELIVERED AT:	Brisbane
HEARING DATE:	25, 26 and 30 October 2006
JUDGE:	Chesterman J
ORDER:	**A declaration that article 32(1) of the defendant's constitution is invalid to the extent that it permits the defendant to dispose of, except by sale, shares forfeited for non-compliance with a notice given pursuant to article 29(2).**
CATCHWORDS:	CORPORATIONS – CONSTITUTION AND REPLACEABLE RULES – MEMORANDUM AND ARTICLES OF ASSOCIATION – ARTICLES OF ASSOCIATION – PARTICULAR ARTICLES – VALIDITY – articles of association allow forfeiture of shares other than for non-payment of call or instalment and without compensation – whether power conferred by articles of association on company directors to forfeit shares would effect an illegal reduction of share capital – whether *Gambotto v WCP Ltd* principle invalidates the articles – whether articles are void as a penalty *Corporations Act* 2001 (Cth), s 254C, s 258C *Arakella Pty Ltd v Paton* (2004) 60 NSWLR 334, cited *Bellerby v Roland & Marwood's Steamship Co Ltd* [1902] 2 Ch 14, cited

Re Chas Jeffries & Sons Pty Ltd [1949] VLR 190, considered
In re Dronfield Silkstone Coal Company (1880) 17 Ch D 76, considered
Farr v Cash Orders (Amalgamated) Limited (1935) 35 SR (NSW) 380, not followed
Gambotto v WCP Ltd (1995) 182 CLR 432, followed
Heydon v NRMA Ltd (2000) 51 NSWLR 1, distinguished
Hopkinson v Mortimer, Harley & Co Ltd [1917] 1 Ch 646, discussed
Lion Nathan Australia Pty Ltd v Coopers Brewery Ltd [2006] FCAFC 144, considered
Rowell v John Rowell & Sons Ltd [1912] 2 Ch 609, considered
Trevor v Whitworth (1887) 12 App Cas 409, distinguished
Wellington Bowling Club v Sievwright [1925] GLR 227, not followed
Young v Owners – Strata Plan No 3529 (2001) 54 NSWLR 60, considered

COUNSEL: Mr D F Jackson QC with him Ms S Brown for the plaintiffs
Mr J C Bell QC with him Mr D A Kelly for the defendant

SOLICITORS: Minter Ellison for the plaintiffs
Corrs Chambers Westgarth for the defendant

[1] The defendant is a company limited by shares. Since it was incorporated in 1894 it has carried on the business of crushing sugar cane to produce raw sugar for sale. It also produces molasses and ethanol as by-products. The defendant's mill is located near Childers. It buys sugar cane from growers in the surrounding district. It owns and operates a light rail system which is used to transport cane from the farms to the mill.

[2] The defendant has more than 250 members, all of whom own shares of the same class. Nearly all of them supply sugar cane to the defendant's mill.

[3] The *Sugar Industry Act* 1999 (Qld) deregulated the production and sale of sugar cane. There is now a free market and the defendant may buy sugar cane from whom it pleases and sell raw sugar to whom it pleases at the best price it can negotiate.

[4] The second plaintiff is a member of the defendant. It holds 16,435 shares. It has been a member since 1996. Until 2003 it supplied sugar cane to the defendant's mill from a plantation owned by its directors, Mr and Mrs Sellers.

[5] The first plaintiff is an unlisted public company incorporated in Queensland. It has several businesses, one of which is the operation of sugar mills, some of which are not far from the defendant's premises. It also grows sugar cane and owns and leases sugar cane farms. Prior to 1989 the first plaintiff was a member of the defendant but ceased to be a member when it sold its farms in the defendant's 'district', a concept which had importance when the sugar industry was regulated. Between 2002 and 2004 the first plaintiff supplied sugar cane to the defendant's mill from farms it leased. In the years 2003 and 2004 the first plaintiff supplied sugar cane to the defendant grown on land owned by the second plaintiff and from which that

plaintiff had supplied sugar cane to the defendant. Since deregulation, which took effect in January 2005, the defendant has refused to accept sugar cane from the first plaintiff and has refused to make any contract for the supply of sugar cane from the first plaintiff.

[6] In 2003 and 2004 the first plaintiff bought sugar cane farms in the defendant's district. As part of the contracts of purchase the first plaintiff agreed to buy the vendors' shares in the defendant, but the defendant refused to give its consent to the transfer of the shares.

[7] The first plaintiff brought proceedings in which it challenged the defendant's refusal but did not proceed after the defendant revealed the basis for its refusal in its defence.

[8] In 2003 the first plaintiff agreed with the second plaintiff that it would buy its shares in the defendant. The contract of purchase was connected or incidental to the purchase by the first plaintiff of the second plaintiff's sugar cane farm and business. In December 2003 the first plaintiff sought to register a transfer of the shares it had acquired from the second plaintiff. The defendant refused to register the transfer on the ground that the second plaintiff was not a shareholder. The defendant contended that it had forfeited the shares held by the second plaintiff on 22 July 2003.

[9] The ground of the forfeiture was said to be that the second plaintiff was in breach of article 5 of the defendant's constitution because it had ceased to be a supplier of sugar cane to the defendant and had thereafter failed to comply with a notice given under article 29(2) requiring the second plaintiff to transfer its shares or again become a supplier.

[10] The plaintiffs disputed receipt of the notice. On 7 April 2006 the defendant resolved to annul the alleged forfeiture of the second plaintiff's 16,435 shares and directed its secretary to rectify the share register so as to restore the second plaintiff's shareholding.

[11] The plaintiffs requested the defendant to undertake that it would not again proceed to forfeit the second plaintiff's shares pursuant to articles 29(2) and 31(1) of its constitution. The defendant refused to provide the undertaking. It asserts that it may lawfully forfeit the shares of members who cease to be suppliers of sugar cane and who therefore are in breach of article 5.

[12] By a second further amended claim of 21 April 2006 the plaintiffs seek three alternative declarations:

> (1) That article 31(1) does not on its proper construction provide for the forfeiture of shares other than for non-payment of a call or instalment.
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> (2) That article 31(1) is invalid as authorising an unlawful reduction of capital to the extent that it authorises or empowers the directors to forfeit shares for non-compliance with a notice given under article 29(2) where the ground of notice is that a member has ceased to be a supplier.

(3) That article 31(1) is invalid to the extent that it provides for forfeiture of shares for non-compliance with article 29(2).

[13] The defendant does not resist the claim on the basis that it is premature or that there is no dispute between the parties which the declarations would resolve.

[14] The declarations raise two issues; the first concerns the proper construction of article 31(1). The second concerns its validity.

Construction of article 31 of the defendant's articles of association

[15] I turn to the construction of article 31 of the defendant's articles of association.

[16] Article 5 provided:

> 'Shares in the capital of the Company may only be held by bona fide Suppliers who have entered into such agreement or agreements as the Directors shall from time to time require:-
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> (a) granting or otherwise assuring to the Company free access to over and through the land owned or occupied by the Supplier for the purpose of transporting sugar cane to the Company's Mill from Assigned Lands or other lands;
>
> (b) granting or assuring to the Company full and free right to lay use and maintain tramways or railways upon or over such land;
>
> (c) whereby each such Supplier agreed to be bound by the Memorandum and Articles of Association; and
>
> (d) containing such other provisions as the Directors may from time to time in their absolute discretion require.'

[17] Article 1 defines 'Supplier' to mean a person or corporation who or which is:

> '(a) the registered proprietor, owner or lessee of Assigned Land; and
>
> (b) the holder of either an Assignment or a Peak to the Mill and who … actually supplies sugar cane to the … Mill …; and
>
> (c) who otherwise satisfies the Directors that he supplies or agrees to supply sugar cane to the … Mill.'

'Assignment' and 'Peak' were terms taken from the *Sugar Cane Prices Act* when that legislation regulated the production and sale of sugar cane.

[18] Articles 29 to 40 appear in a part of the articles under the heading 'Liens and Forfeiture'. Articles 29 and 30 provide:

‘29. (1) If any member fails to pay any call or instalment on or before the day appointed for payment of the same, the Directors may at any time thereafter during such time as the call or instalment remains unpaid give a notice to such member requiring him to pay the same together with any interest that may have accrued and all expenses that may have been incurred by the Company by reason of such non-payment.

(2) If any member shall cease to be a Supplier or shall be in breach of any agreement pursuant to article 5 hereof, the Directors may at any time give a notice in writing to such member requiring him to dispose of all shares registered in the name of such member or remedy such breach.

30. (1) Any notice under article 29(1) shall name a day (not being less than fourteen days from the date of the notice) and a place or places on and at which such call or instalment and such interest and expenses as aforesaid are to be paid.

(2) Any notice under article 29(2) shall name a day not being less than fourteen (14) days from the date of the notice) by which the member to whom the same is addressed shall either dispose of his shares or remedy the breach.

(3) The notice shall also state that, in the event of non-payment at or before the time and at the place appointed, the shares in respect of which the call was made or instalment is payable will be liable to be forfeited.’

[19] The present dispute is concerned with the meaning of article 31(1). It is in these terms:

‘31. (1) If the requirements of any such notice as aforesaid are not complied with, any shares in respect of which such notice has been given may at any time thereafter before payment of all calls or instalments interest and expenses due in respect thereof be forfeited by a resolution of the Directors to that effect.’

[20] Article 29 contemplates three circumstances in which the directors may resolve to take action against a member of the company who is in breach of his obligations *qua* member. They are:

1. Where a member has not paid a call or instalment on the due date.

2. Where the member ceases to be a supplier to the plaintiff as defined in the articles.

3. Where the member is in breach of the agreement described in article 5.

In any of these three cases the directors may give a notice to the defaulting member requiring him to make good the default: by paying the call or instalment; or by selling his shares in the case where he has ceased to be a supplier; or by remedying the breach of the agreement made under article 5.

[21] By article 30(1) and (2) respectively the notices given under the preceding article must identify a date by which the default is to be remedied, by payment of the call, sale of the shares or repair of the breach.

[22] Article 30(3) requires the directors to specify, in a notice, the consequence of non-compliance, but only in the first case, non-payment of a call or instalment. No such specification is required with respect to the other cases of default.

[23] Article 31(1) is problematic. The plaintiffs' submission is that it applies only to a default of the first case and that it is only where a member has failed to comply with a notice requiring it to pay a call or instalment that the directors may resolve to forfeit the member's shares. This is said to follow from the inclusion of the phrase 'before payment of all calls or instalments … due in respect thereof'. The phrase is said to limit the otherwise general application of the article which would follow from the introductory words 'If the requirements of any such notice … are not complied with …'.

[24] The plaintiffs point out that article 30(3) requires a notice to state that in the event on non-payment at or before the specified time the shares will be liable to forfeiture, but there is no such requirement with respect to notices given on the grounds found in article 29(2). From this and the limitation apparent in article 31(1) that shares may be forfeited 'before payment of … calls or instalments, interest and expenses due in respect thereof' it is said that the power may be exercised in that case only.

[25] The literal meaning of article 31(1) supports the plaintiffs. On its face the power to forfeit shares is limited to the circumstance described in article 29(1). But I do not think this meaning should be ascribed to article 31(1). It would make little sense. It is, I think, clear enough that the intention of these articles, which appear under the heading 'Liens and Forfeiture', were meant to specify three circumstances in which a default might lead to the giving of a notice which, if not complied with, might lead to forfeiture. The draftsman attended to specifying the power with respect to one only of those three categories but I think that is an oversight.

[26] There is an ambiguity in article 31(1). The 'requirements of any such notice as aforesaid' is a phrase general in its terms, and appropriate to refer to any notice which may be given pursuant to article 29. It is not, by its terms, limited to notices given under article 29(1). I do not think the reference to the directors having to act before overdue calls were actually made should detract from the generality of the earlier part of the article. I think the temporal limitation should be read as extending only to the proposed action of the directors to forfeit shares in the case of non-payment of calls. It should not be read as limiting the circumstances in which the directors might resolve to forfeit shares.

[27] Article 31(1) should thus be understood as though it read:

> 'If the requirements of any such notice as aforesaid are not complied with, any shares in respect of which such notice has been given may at any time thereafter be forfeited by resolution of the directors to that effect but, in the case of non-compliance with a notice given pursuant to article 29(1), before payment of all calls or instalments, interest and expenses due in respect thereof.'

[28] The cases and principles explaining the approach which a court should take to the construction of companies' constitutions were collected by Lander J in *Lion Nathan Australia Pty Ltd v Coopers Brewery Ltd* [2006] FCAFC 144 at paras 232-238. His Honour said:

> '[232] The constitution should be construed so as to give the document business efficacy. A construction which would make the constitution unworkable should be avoided if possible: *Rayfield v Hands* [1960] 1 Ch 1. In *Holmes v Keys* [1959] 1 Ch 199, Jenkins LJ said (at 215):
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> > I think that the as of association of the company should be regarded as a business document and should be construed so as to give them reasonable business efficacy, where a construction tending to that result is admissible on the language of the articles, in preference to a result which would or might prove unworkable.
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> [233] That decision has been followed in Australia in *Stillwell Trucks Pty Ltd v Nectar Brook Investments Pty Ltd* (1993) 10 ACSR 615 at 621 per O'Loughlin J; *Tosich v Tosich Construction Pty Ltd* (1993) 10 ACSR 590 at 596 per Lockhart J and *Parkin* at 235 per Ipp JA.
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> [234] In *Egyptian Salt and Soda Co Ltd v Port Said Salt Association Ltd* [1931] AC 677, Lord MacMillan said (at 682):
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> > If by this he meant merely that the memorandum must be construed in accordance with the accepted principles applicable to the interpretation of all legal documents no exception need be taken to his statement, but if he meant that a specially rigid canon of construction is to be applied to the memoranda of association of limited companies their Lordships do not agree. A memorandum of association like any other document must be read fairly and its import derived from a reasonable interpretation of the language which it employs.
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> [235] In HAJ Ford, RP Austin and IM Ramsay, *Ford's Principles of Corporations Law*, 12th ed, Butterworths, 2005, the learned authors write (at 190):

> Because courts have considered the constitution to be a contract they have been construed according to the rules of construction of terms applicable to contracts generally.
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> In the interpretation of constitution courts approached them as business documents. They sought to give them business efficacy: *Rayfield v Hands* [1960] Ch 1. Where provisions were ambiguous a construction which produced reasonable business efficacy was preferred over one which produced an unreasonable result: *Holmes v Keyes* [1959] Ch 199 at 215; *Stillwell Trucks Pty Ltd v Nectar Brook Investments Pty Ltd* (1993) 115 ALR 294; *Norths Ltd v McCaughan Dyson Capel Court Cure Ltd* (1988) ACLR 739 at 746; *Tosich v Tosich Construction Pty Ltd* (1993) 10 ACSR 590 at 596.
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> …
>
> [238] … The need for an ambiguity before recourse can be had to previous negotiations is no longer the law: *Pacific Carriers Ltd v BNP Paribas* (2004) 218 CLR 451 …; *Toll (FGCT) Pty Ltd v Alphapharm Pty Ltd* (2004) 219 CLR 165 … Rectification of a company's constitution is not available even if the constitution does not accord with the intention of all the signatories at the moment of signature: *Scott v Frank F Scott (London) Ltd* [1940] Ch 794 …; *Bratton Seymour Service Co Ltd v Oxborough* [1992] BCLC 693 …; *Bailey v New South Wales Medical Defence Union.*'

[29] The plaintiffs' construction of article 31(1) would deprive the article, and the two preceding articles, of business efficacy and, indeed, sense. Articles 29(2) and 30(2) would serve no purpose at all if the plaintiffs are right and the only power in the directors to resolve to forfeit shares pursuant to article 31(1) is limited to the circumstance provided for by article 29(1). The notice which the directors are empowered to give pursuant to article 29(2) would lead to nothing. Non-compliance with it would have no effect. No sanction would apply to non-compliance with its terms. The defendant would be powerless in the case of breach of article 5 by a member. Despite losing the eligibility for membership of the company the defaulting shareholder could remain a member.

[30] This cannot have been the intention of the draftsman.

[31] There is a logical progression in the articles from (i) breach, of one of the three kinds specified; to (ii) the giving of a notice specifying that the defaulting member is to make good his default; to (iii) forfeiture where the notice is not complied with. Two thirds of the progression is destroyed if article 31(1) does not also apply to non-compliance with notices given pursuant to article 29(2).

[32] It is to be remembered that the articles appear in that section of the constitution headed '… Forfeitures'. The draftsman clearly intended that the giving of a notice pursuant to article 29(2) be connected with the forfeiture of shares.

[33] For these reasons article 31(1) should be construed as I have indicated in para 27.

[34] The defendant sought to tender extrinsic evidence in the form of an Explanatory Memorandum which was delivered to the defendant's shareholders in 1987 when the articles were amended, and articles 29 to 32 were inserted. The plaintiffs objected to the tender submitting that the evidence was inadmissible and could not be used to aid in the construction of the articles. It is not necessary to resolve the objection. In my opinion the meaning of the article is clear enough from the document itself and resort to extrinsic materials is unnecessary.

Validity of article 31: the power to forfeit shares

[35] The plaintiff submits that should the articles be construed so as to confer a right on the directors to forfeit shares in the case of a member ceasing to be a supplier the article is invalid. I have so construed the articles and must now consider the submission that the article is invalid. The ground of invalidity advanced is that a power conferred on the directors of a company to forfeit shares for any circumstance other than the failure of the shareholder to pay a call on the shares is beyond power. It is said to infringe the rule that a company limited by shares must maintain, and cannot reduce, its share capital. The principle is well established. It is said that to allow the directors to forfeit the shares would be to effect a reduction of the capital of the company which may occur only in the circumstances admitted by the *Corporations Act* and/or with the approval of the Court. The only exception is that there may be a forfeiture where the shareholder has not paid calls due in respect of the shares.

[36] The plaintiffs' submission continues:-

> '51. Forfeiture for any reason other than non-payment of calls or instalments does not fall within the exception. That is true even where the shares concerned are fully paid shares. In *Hopkinson v Mortimer, Harley & Co Limited* a company sought to amend its articles so that it could forfeit fully paid shares on the basis of an unpaid debt due by a shareholder to the company, which was not for a call or instalment of money due on the shares. Before the amendment, the articles had made provision for forfeiture of shares other than fully paid shares. Eve J held that the forfeiture would constitute an illegal reduction of capital and the article was invalid. His Honour stated at 654:
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> > *"But as the article stands, I am of opinion it is invalid in this respect, and that the board cannot forfeit shares for non-payment of the debts and liabilities therein referred to without bringing about an illegal reduction of the company's capital in any event and a purchase by the company of its own shares in some events. It may be that a reduction in capital brought about by the forfeiture of fully-paid shares inflicts no injury on the creditors or contributors, but this consideration cannot legalize a procedure which for other reasons is illegal, and it does not exist if in fact the value of the shares – which may be greatly in excess of the amount paid up on them – has to be brought into account with the defaulting member."*

> 52. There was thus a reduction of capital notwithstanding that the shares forfeited were fully paid shares. The decision has been treated since as establishing that forfeiture is only permitted for unpaid calls or instalments.'

[37] The article in question in *Hopkinson* provided that the company should have a lien upon all the shares registered in the name of each member for the debts of the member. Another article gave the board power to sell the shares for the purpose of enforcing the lien. Another article gave the board power to sell the shares for the purpose of enforcing the lien and to forfeit the shares. Eve J held the articles invalid for a number of reasons. One was that the lien was an interest in property to secure the repayment of a debt, and the articles operated as a clog on the equity of redemption. They were therefore inequitable, and invalid. That point has no importance for present purposes. Another ground was that the power of forfeiture, to be valid, had to vest in the company rather than the directors. That point also has no present importance. The third ground, which is relevant, was that the forfeiture would effect a reduction in capital. Eve J was concerned that if the value of the shares forfeited, whether the par value or market value, were credited against the debt owed by the shareholder the company would be, in effect, purchasing its own shares in contravention of the principle enunciated by the House of Lords in *Trevor v Whitworth* (1887) 12 App Cas 409. The articles in fact did not make it clear whether the shareholder whose shares were forfeited got the benefit of a reduction in the debt equivalent to the value of the shares.

[38] Eve J said (at 653-654):

> 'Even if the forfeiture is made without any part of the value of the shares being set off against the debt, the capital is reduced by the amount paid up on the forfeited shares, and if on the other hand the debt is partially or wholly satisfied the transaction involves not only the same reduction, but what is equivalent to an actual payment by the company; and how can this … be … anything but a purchase by the company of its own shares? I think, further, when one appreciates the narrow limits within which the Court has decided that a surrender of shares may properly be regarded as not infringing the principles established by *Trevor* … it is impossible to believe that a power to forfeit vested in the board, and bringing about … one or both of the consequences I have just indicated, ought to be held valid … It may be that a reduction in capital brought about by the forfeiture of fully-paid shares inflicts no injury on the creditors or contributories, but this consideration cannot legalize a procedure which for other reasons is illegal, and it does not exist if in fact the value of the shares … has to be brought into account with the defaulting member.'

[39] The point under consideration in *Trevor* was whether it was lawful for a company to buy back own shares which it had issued to its shareholders. The House of Lords held it was not. Some passages in the judgments contain remarks which are of value to the present problem. *Trevor* was not a forfeiture case.

[40] Lord Herschell said (at 417):

> 'It is urged that the views I have expressed are inconsistent with the forfeiture and surrender of shares in a company. I do not think so. The forfeiture of shares is distinctly recognised by the Companies Act, and by the articles … It does not involve any payment by the company …'

and (at 419-420):

> 'Again, in the case of *Guinness v Land Corporation of Ireland* … Lord Justice Cotton … said: "From that it follows that whatever has been paid by a member cannot be returned to him. In my opinion, it also follows that what is described in the memorandum as the capital cannot be diverted from the objects of the society…".'

[41] Lord Watson said (at 423-424):

> 'One of the main objects contemplated by the legislature, in restricting the power of limited companies to reduce the amount of their capital as set forth in the memorandum, is to protect the interests of the outside public who may become their creditors. In my opinion the effect of these statutory restrictions is to prohibit every transaction between a company and a shareholder, by means of which the money already paid to the company in respect of his shares is returned to him, unless the Court has sanctioned the transaction. Paid-up capital may be diminished or lost in the course of the company's trading; that is a result which no legislation can prevent; but persons who deal with, and give credit to a limited company, naturally rely upon the fact that the company is trading with a certain amount of capital already paid … and they are entitled to assume that no part of the capital which has been paid … has been subsequently paid out, except in the legitimate course of its business.
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> When a share is forfeited or surrendered, the amount which has been paid upon it remains with the company, the shareholder being relieved of liability for future calls, whilst the share itself reverts to the company, bears no dividend, and may be re-issued. When shares are purchased at par, and transferred to the company, the result is very different. The amount paid up on the shares is returned to the shareholder … and … is … withdrawn from its trading capital.'

[42] Lord Macnaghten said (at 432-433):

> 'The third point … raises the question whether it is competent for a company … to purchase its own shares … that question … necessarily involves the broader question whether it is competent for a limited company under any circumstances to invest any portion of its capital in the purchase of a share of its own capital stock, or to return any portion of its capital to any shareholder without following the course which Parliament has prescribed.'

[43] The House ruled that the article empowering the company to buy its own shares was invalid. It is apparent from the passages I have quoted that the reason was the need to preserve the company's capital and to ensure that it was expended on its business objectives. The purchase by the company of its own shares would infringe the rule and diminish its stock of capital. The same result would occur in the eventuality considered by Eve J in *Hopkinson*: where upon forfeiture of the shares the company credited the shareholder/debtor with their value thereby reducing the value of the chose in action, the debt, owed by the shareholder to the company. In such a case the shares would be acquired by the company for valuable consideration, the payment of which would diminish the value of the company's assets, and therefore its capital.

[44] I stress these points which are obvious, because the problem with which I am concerned is of a forfeiture of fully paid shares for no consideration. Once the shares are forfeited the defendant company will lose nothing. The defendant has received the full value of the shares issued and held by the plaintiffs. Moreover the defendant will pay nothing for the forfeited shares. There will be no reduction in the value of its assets and therefore no reduction in capital.

[45] Eve J appreciated the point: that emerges from his judgment in the passage I have quoted, but it was not necessary for him to consider the point further because the article empowering the forfeiture of shares was illegal for other reasons. Eve J did not consider, and did not decide, that an article allowing directors to forfeit shares which were fully paid and for no consideration would be invalid.

[46] He did, however, say that the forfeiture, even if made without any part of the value of the shares being set off against the shareholder's debt, would reduce the capital of the company 'by the amount paid up on the forfeited shares …'. I presume his Lordship meant that the issued capital of the company would be reduced, by the amount of the forfeited shares, from its stock of capital though its actual, paid-up capital would not be reduced in the circumstances under discussion. Nor would the company's nominal capital be reduced because the forfeited shares could be re-issued.

[47] The plaintiffs submit that *Hopkinson* stands as authority for a wider principle than the proposition that an article permitting a company to forfeit a member's shares on the ground that the shareholder is indebted to the company, for an amount not due in respect of the shares, is invalid. The plaintiffs cite the (New Zealand) Court of Appeal in *Wellington Bowling Club v Sievwright* [1925] GLR 227, but that case does not support their contention. The company in question was a bowling club 'with a capital of £1,050 divided into 350 shares of £3 each, none of which (had) been called up.' The company purported to forfeit the shares of a member who had misbehaved. The articles permitted such a forfeiture. The respondent contended that his share had been wrongly forfeited and that he remained a member of the club. Sim J said (at 229):

> 'If a forfeiture took place under any of these articles an existing liability to contribute to the capital of the company would be extinguished, and a reduction made thereby in the capital of the company. Such a reduction is unlawful, unless it is effected with the sanction of the Supreme Court, and in the manner prescribed by the Companies Act: *Trevor v Whitworth* … In the case of *Hopkinson* … it was held … that an article which provided for the forfeiture of

> shares for non-payment of liabilities of a member other than debts due by him as a contributory was *ultra vires*, and it seems that a company is not entitled to take power in its articles to forfeit shares for any cause other than that specified in … the Companies Act 1908, namely, the non-payment of calls or instalments …'.

[48] Adams J said (at 231):

> 'Moreover, the power of a company to forfeit shares is limited to cases of non-payment of calls or instalments due on the shares, and … the power is exerciseable (sic) only when it is for the benefit of the company.'

His Honour cited no authority but no doubt had *Hopkinson* in mind.

[49] Two things may be said about *Wellington Bowling Club*. The first is that it was a case in which the forfeiture did effect a reduction in capital. The share forfeited was not paid up and the forfeiture meant that the company had lost its right to call up the £3. The second point to make is that the case expands the effect of the decision in *Hopkinson* beyond its *ratio decidendi*.

[50] The plaintiff refers also to *Farr v Cash Orders (Amalgamated) Limited* (1935) 35 SR (NSW) 380, a case of a demurrer heard by the Full Court. The decision turned entirely upon the construction of the articles in question which allowed forfeiture for non-payment of calls. Davidson J, who gave the judgment of the court, said (at 382-383):

> 'It may be mentioned in passing that any claim on the part of the company … to forfeit shares otherwise than for the payment of calls would be invalid. That proposition is stated, and I think correctly, in the case of *Hopkinson* … it was held:-
>
> > "That under this power the forfeiture for debts due from a member generally, as distinct from those due from him as contributory, would amount an illegal reduction of capital."
>
> The decision appears to have been based on the fact that the statute recognises a forfeiture of shares for non-payment of calls, and for that reason the company is allowed … to become the proprietor of shares, notwithstanding that, in other circumstances, such an action might result in a reduction of capital.'

[51] It will at once be appreciated that the remarks relied upon by the plaintiff were *obiter* and, again, the effect of the decision in *Hopkinson* is extended.

[52] Moreover there is, I think, a misconception involved in the expression of the rationale for the supposed rule established by *Hopkinson*. It is that the forfeiture of shares constitutes the company the owner of the shares in itself and this is an anomaly permitted by company legislation only in the case of forfeiture for the non-payment of calls.

[53] It is true that this consideration formed a basis for the opinions in *Trevor*. But to say that a company may not be a member of itself and may not therefore own shares in itself, which a point made in *Trevor*, is to overlook what was said by Lord Watson (at 424):

> 'When a share is forfeited or surrendered, the amount which has been paid upon it remains with the company … whilst the share itself reverts to the company, bears no dividend, and may be re-issued.'

This description of the effect of forfeiture is not apt to describe a conventional shareholding. Whilst the word 'reverts' may be ambiguous the fact that the share bears no dividend and may be reissued rather than transferred suggests that the capacity in which the company may deal with the share is not that of owner.

[54] The plaintiff also points to the fact that a number of text writers have taken the same view of the effect of *Hopkinson*, particularly the authors of *Ford's Principles of Corporations Law* (7th ed, 1995). They say (at 17.480):

> 'Forfeiture amounts to a reduction of capital and could not be authorised by articles in respect of anything other than anything other than non-payment of calls or instalments'

citing *Hopkinson* and *Wellington Bowling Club*.

[55] The situation is, I think, accurately summarised by the defendant in its submission:

> '52. It is cited by some of the texts as authority for the proposition that a provision in a corporate constitution which purports to confer a power of forfeiture for reasons not involving the non-payment of calls is void: Ford and Austin's *Principles of Corporations Law*, 7th ed at 638; Tomasic, Bottomley, McQueen, *Corporations Law in Australia*, 2nd ed at 299-300; Estrin and Magnus, *Companies Law and Practice*, 5th ed at 427. However it is submitted that a statement in these broad terms is unwarranted and inaccurate. The better view is to limit *Hopkinson* to its facts and to regard it as authority for the narrow proposition that a power to forfeit shares for enforcing a lien in respect of debts due from the holder generally and not in respect of calls on shares is invalid as involving an illegal reduction of capital and as being a clog on the equity of redemption: *Buckley on the Companies Act*, 14th ed, vol 1 at p 946; *Farrar's Company Law*, 2nd ed, at p 214; *Gore-Browne on Companies*, 44th ed, at [15.4]; *Palmer's Company Law*, Vol 1, [6.901].
>
> 53. It would be a mistake to regard forfeiture not involving the forgiveness of a debt owed to the company, as necessarily involving a reduction of capital. Such a contention is quite inconsistent with orthodox notions of forfeiture as exemplified by the comments of Lord Watson in *Whitworth* at 424 (set out above). The point is taken up in *Pennington's*

Company Law, 6th Edition at 173-174, where the learned author comments:

> "It is questionable whether a forfeiture or surrender of shares does really reduce the company's capital. At first sight it appears to do so, because the company cannot be treated as having taken a transfer of the shares, and it therefore looks as though the shares are extinguished. But this is not necessarily the result. The cases show that shares are not cancelled by being forfeited or surrendered, but are merely in abeyance until they are re-issued. No dividend is paid in respect of forfeited or surrendered shares, and no votes can be case in respect of them at shareholders' meetings if the company is a public one or, presumably, if it is a private company, but that does not mean that the shares cease to exist. When forfeited or surrendered shares are re-issued the full rights attached to them revive. The re-issued shares are the same shares that were forfeited or surrendered, and not new shares issued in place of the forfeited or surrendered ones. Consequently, the company may reissue them at whatever price it can obtain, whether more or less than their nominal or paid up value, and they are paid up in the hands of the person who takes them on re-issue to the same extent as they were paid up immediately before they were forfeited or surrendered. The amount received by a company on the re-issue of forfeited or surrendered shares is not paid up capital of the company, except in so far as it is appropriated by agreement to pay calls or instalments of the issue price which is owing but unpaid."'

[56] I respectfully agree with the analysis found in *Pennington*.

[57] There is a surprising dearth of authority on the power of a company to forfeit shares for reasons other than the non-payment of calls. Each side seeks to turn the lacuna to its own advantage. The plaintiffs submit that the lack of any decided case endorsing such a forfeiture indicates that the wider view of *Hopkinson* has been accepted without challenge. The defendant, on the contrary, contends that it is significant that the plaintiff cannot point to any case in which such a forfeiture has been struck down. The position, it seems to me, is that, there being no authority, one must approach the question as a matter of legal principle.

[58] Two reasons are advanced for contending that an article permitting the forfeiture of shares on grounds other than non-payment of calls is invalid. The first is that as a result of the forfeiture the company owns shares in itself, and the second is that the forfeiture operates as a reduction of capital.

[59] The first ground is, I think, misconceived. Forfeited shares are 'in abeyance' until they are reissued, sold or cancelled. No dividend is paid on the forfeited shares and no votes are cast in respect of them. The company is not the proprietor of them; it is not a member in itself and does not hold the shares in itself. The defendant's

articles provide that forfeited shares are held by the directors on trust for the company, which is not a member of itself.

[60] The second point does have some substance. A forfeiture of shares may operate to reduce the company's capital, but it will not operate to reduce paid up capital when the shares have been fully paid. This point is recognised in the cases. Nevertheless a forfeiture may still serve to reduce the company's issued capital, at least if the shares are cancelled consequent upon the forfeiture. This may be the point Eve J had in mind when he said that, on a forfeiture, 'the capital is reduced by the amount paid up on the forfeited shares.'

[61] This point is now without substance. Section 254C of the *Corporations Act* provides that a company's shares 'have no par value'. There is now no requirement that companies have a specified nominal capital. See ss 117 and 118 which set out the criteria for the registration of a company. They do not include nomination of the company's capital. A forfeiture of shares cannot therefore reduce a company's nominal capital, the shares having no par value and the company having no such nominal value. Nor can it reduce the issued capital since the shares have no par value and the forfeiture and subsequent cancellation of shares will not affect the value of issued share capital, because the shares have no fixed, par, value. To the extent that the cancellation of forfeited shares may somehow effect reduction in share capital that result is expressly permitted by s 258D which provides that a company may, by ordinary resolution, cancel shares 'that have been forfeited under the terms on which the shares are on issue.'

[62] As the discussion in the cases reveals, in earlier times the model articles of association for a company permitted the forfeiture of shares for non-payment of calls or instalments. To the extent that *expressio unius exclusio alterius* applied so the specification of that ground of forfeiture gave rise to an implication that there were no other grounds the argument ceases to have effect since the enactment of the *Corporations Act*. A company may adopt a constitution which displaces or modifies the replaceable rules. To the extent that it does not the replaceable rules apply. There is nothing in those rules concerning the forfeiture of shares. There is, in particular, no rule limiting the circumstances in which forfeiture may occur. A company is free to provide for that eventuality in its own constitution, as the defendant has done. See ss 134 to 136 of the *Corporations Act*.

[63] Because of the dearth of authority on the validity of forfeitures counsel referred me to some cases which examined the surrender of shares, a process which, in some circumstances, has a similarity to forfeiture. I do not think that an examination of the surrender cases will be fruitful. One does well to remember the advice of Jessel MR in *In re Dronfield Silkstone Coal Company* (1880) 17 Ch D 76, cited by Herschell LJ in *Trevor* (at 418):

> 'It is not for me to say what the limits of surrender are which are allowable under the Act, because each case as it arises must be decided upon its own merits'.

In this area of the law, too, the cases are few and conflicting. I think one cannot go beyond what was said by Fullagar J in *Re Chas Jeffries & Sons Pty Ltd* [1949] VLR 190 at 196:

> 'It has never been denied, I think, that the authorities are in an unsatisfactory state both as to what constitutes such a reduction of capital as requires confirmation by the court and as to the extent to which … it is *intra vires* a company to accept a surrender of shares.'

His Honour was dealing with a case in which 'there was no reduction of nominal capital, but there was a reduction of issued capital.' He followed the dictum of Cozens-Hardy LJ in *Bellerby v Roland & Marwood's Steamship Co Ltd* [1902] 2 Ch 14 at 32 where the surrender of shares 'involved a release of a liability of £1 per share …'. His Honour referred also to *Rowell v John Rowell & Sons Ltd* [1912] 2 Ch 609 in which a surrender involved no release of liability and Warrington J held the surrender lawful. This case has been criticised but I find it hard not to agree with Warrington J's emphasis on the question of whether or not the surrender in fact operated to reduce the company's capital. In that case it did not and his Lordship held the surrender lawful.

[64] The analysis comes to this. There is no reason in principle why a forfeiture which does not in fact operate to reduce the capital of the company should be invalid. Indeed under the present *Corporations Act* a forfeiture of fully paid shares cannot reduce a company's nominal or issued capital. Secondly there is no clear authority for the proposition that the forfeiture of shares except for non-payment of calls or instalments is invalid, whether or not it effects a reduction in capital. There are *dicta* to that effect but they depend upon *Hopkinson* which is an unsatisfactory base for them. The *ratio* of that case is properly recognised by the authors of *Gore-Browne on Companies*, 44th ed, at [15.4]: 'a forfeiture of shares for the non-payment of debts other than calls is invalid … [if] the articles purport to give a lien on shares for such a debt, the rule forbidding a clog on the equity of redemption will be infringed by an attempted forfeiture.'

[65] If *Hopkinson* is to be taken as deciding that forfeiture in all events, save the non-payment of calls, is invalid the decision goes beyond its rationale which is the preservation of the company's capital.

[66] Article 32(1) of the defendant's articles deems a forfeited share to be held on trust by the directors on behalf of the defendant and further provides that the forfeited shares may be sold, realloted or otherwise disposed of by the directors in such a manner as they think fit. If the shares are re-allotted the re-allotment may occur with or without any money paid on the re-allotment being credited as monies paid up by the former shareholder. If the forfeited shares are sold the net proceeds of sale are to be applied in satisfaction of any monies due in respect of the shares, or for their sale. Any surplus goes to the former shareholder.

[67] By article 35 a member whose shares have been forfeited remains liable to pay all calls, interest and expenses owing in respect of the shares at the time of the forfeiture.

[68] It is apparent from these provisions that a forfeiture does not operate to reduce the defendant's capital. The shares are not cancelled but are held on trust, or in abeyance, pending sale or re-allotment. There is no return of subscribed capital because the former shareholder remains liable to pay outstanding calls and does not become entitled to receive any monies previously paid in respect of the shares.

[69] In these circumstances there is no reason in principle why the articles permitting forfeiture should be held invalid. There is no compelling persuasive authority which requires that course. Accordingly I refuse the plaintiffs' invitation to strike down the articles.

Validity of articles 2992), 30(2) and 31(1): forfeiture of shares and the *Gambotto* principles

[70] The next point taken by the plaintiffs is that the amendments to the articles which occurred in 1987 were invalid because articles 29(2), 30(2) and 31(1) operate to authorise the forfeiture of the shares of a member who ceases to be a supplier to the defendant and the forfeiture so authorised is an expropriation of the shares without compensation. The principles discussed by the High Court in *Gambotto v WCP Ltd* (1995) 182 CLR 432 are said to invalidate those articles.

[71] It is pointed out that upon forfeiture the former member loses all ordinary rights and entitlements. Its name is removed from the register of members and it may not receive dividends, or attend or vote at general meetings, or participate in the proceeds of a voluntary winding up. The plaintiffs stress the point that article 32(1) confers on the directors a wide discretion as to the manner in which forfeited shares may be dealt with. They may be sold, re-allotted or 'otherwise disposed of in such manner as the directors think fit'. Unless shares are resold no money is payable for the former member whose shares had been forfeited.

[72] In *Gambotto* the High Court was concerned with amendments to an article which, when amended, enabled a shareholder holding 90 per cent of the issued shares to compulsorily acquire shares held by minority shareholders. In their joint judgment Mason CJ, Brennan, Deane and Dawson JJ said (at 444-5):

> '… in … a case [giving rise to a conflict of interests and advantages] not involving an actual or effective expropriation of shares or of valuable proprietary rights attaching to shares, an alteration of the articles by special resolution regularly passed will be valid unless it is ultra vires … or oppressive … Somewhat different considerations apply, however, in a case such as the present where what is involved is an alteration of the articles to allow expropriation by the majority of the shares … of a minority …
>
> …
>
> The exercise of a power conferred by a company's constitution enabling the majority shareholders to expropriate the minority's shareholding for the purpose of aggrandizing the majority is valid if and only to the extent that the relevant provisions of the company's constitution so provide … But it is another thing when a company's constitution is sought to be amended by an alteration of articles of association so as to confer upon the majority power to expropriate the shares of a minority … In our view, such a power can be taken only if (i) it is exercisable for a proper purpose and (ii) its exercise will not operate oppressively in relation to minority shareholders. In other words, an expropriation may be justified where it is reasonably apprehended that the continued shareholding of the minority is

> detrimental to the company, its undertaking or the conduct of its affairs – resulting in detriment to the interests of the existing shareholders generally – and expropriation is a reasonable means of eliminating or mitigating that detriment.'

[73] The full extent of what has been described as the '*Gambotto* principles' is yet to be determined as is the precise definition of the circumstances to which they will apply. See eg the remarks of Austin J in *Arakella Pty Ltd v Paton* (2004) 60 NSWLR 334 at 369.

[74] The defendant submits that the principles have no application in this case. It is said that:

> (a) The amendments to the articles which occurred in 1987 were adopted by a unanimous resolution.
>
> (b) The particular articles under attack were not the subject of a particular amendment but were adopted as part of a complete new set of articles which replaced, in their entirety, the previous articles of association.
>
> (c) The articles cannot be said to work an expropriation because the defendant's power to forfeit shares pursuant to article 31(1) only arises after
>
> (i) the member has ceased to be a supplier of sugar to the mill
>
> (ii) the company gave notice to the member requiring it to dispose of its shares or become a supplier; or
>
> (iii) the member failed to do either.

[75] Consequently, the submission runs:

> '… this is not a case which falls within the scope of *Gambotto*. In particular this was not a case …
>
> (a) [Where] [t]he majority "secured some personal gain";
>
> (b) Where the amendment allowed "an expropriation by the majority of the shares … of a minority", such that the majority had conferred on them "power to acquire compulsorily the property of the minority"; or
>
> (c) Where the purpose of the amendment was "aggrandizing the majority".'

[76] The defendant's essential point is that the resolution by which the new articles were adopted brought about a regime which treats all members of the company equally in the sense that any member who ceases to be a supplier of sugar to the mill is liable

to have its shares forfeited. The articles in question do not operate to allow a majority of shareholders to acquire the shares of a minority.

[77] The plaintiffs' arguments in reply submit that *Gambotto* is not confined to the acts of a particular majority of shareholders against a particular minority and that in *Gambotto* the majority judgment spoke of a 'case involving actual or effective expropriation of shares', and of an 'alteration of the articles to allow expropriation by the majority of the shares'. The plaintiffs submit that the 'critical feature' of *Gambotto* was 'the taking by amendment of a power whereby a majority is able to effectively expropriate the shares … of a minority. Providing for forfeiture of shares on the ex-supplier ground is such a provision. … The power is directed to a minority (the ex-supplier) and for the benefit of a majority (the other shareholders who accrued the benefit of the forfeited shares by their being forfeited) when it is engaged.'

[78] Support for this submission may be found in the judgment of McPherson A-JA in *Heydon v NRMA Ltd* (2000) 51 NSWLR 1 at 125 (para 381). Dealing with an attempt to distinguish *Gambotto* his Honour said:

> 'Nor is it … sufficient to say that *Gambotto* involved expropriation by the majority of a minority whereas here the rights of all members of … NRMA Insurance Pty Ltd were to be extinguished and replaced by something of equal or greater value. Although at various points the majority in *Gambotto* speak of an "aggrandisement" of a "majority", the reasoning is in terms applicable to an expropriatory amendment as such, whether or not the specific target is a minority of members.'

[79] Ormiston A-JA may have taken a different view. His Honour said (at 206):

> '… where transferor destruction of the minority's rights is not in issue, I would not see the ratio of the case, insofar as it relates to expropriation, as extending to amendments which extinguish all of a company's shares or all membership rights but which provide in their place rights or options available to all members equally, whether or not they choose to exercise them.'

Malcolm A-JA (at 63) appears to have taken a similar approach.

[80] It is not necessary to choose between this conflict of opinion, whether real or apparent. *Heydon* was concerned with circumstances very different from those relevant in this case. The circumstances there were that by the reconstruction of a company the rights of the members in the company which was limited by guarantee were to be replaced by shares in the company which was to become one limited by share capital. All members were to be treated equally. The remarks of their Honours on appeal must be understood in that context, and as addressing that question.

[81] In my opinion the plaintiffs' analysis of the amendments to the articles of the defendant's constitution is correct. This is not a case where the articles affect all shareholders equally. They operate differentially, or allow the directors to act differentially, with respect to different classes of members: those who supply sugar

and those who do not. The shares of members in the second class may be taken from them, compulsorily, and either destroyed by cancellation or sold or re-allotted to an existing member or members who will, by definition, be one of the majority class of shareholders; those who supply sugar.

[82] This case falls squarely within what the majority said in *Gambotto*: '… a case … where what is involved is an alteration of the articles to allow an expropriation by the majority of the shares … of a minority. … The immediate purpose of the resolution is to confer upon the majority shareholder … power to acquire compulsorily the property of the minority …'. There was here an amendment to the articles allowing for the forfeiture of the shares and their transfer to another shareholder, who constitutes part of the majority of shareholders, or the extinction of the shares which will confer benefits on the other shareholders. Should a dividend be declared the other shareholders' entitlement will be proportionately increased. The same is true for the return of capital on a winding up.

[83] The fact that the shares may be cancelled following forfeiture rather than transferred to another shareholder, or re-allotted to another shareholder, does not mean that the act of forfeiture is not an expropriation. Santow J in *Young v Owners – Stata Plan No. 3529* (2001) 54 NSWLR 60 at 74-5 concluded that the '*Gambotto* principles' applied to the extinction of rights as well as to their compulsory acquisition. His Honour referred with approval to what Ormiston A-JA had said in *Heydon* at 206 para 577:

> 'Thus I would conclude that, although the word "expropriation" is ordinarily wide enough to comprehend not merely compulsory acquisition but also compulsory destruction of rights, the High Court in *Gambotto* was concerned primarily with amendments to articles which have the effect of destroying the minority's shareholding … or of placing those rights in the hands of the majority shareholders … In other words where transferor destruction of the minority's rights is not in issue …'.

Santow J said (at 74-75 para 52-53):

> 'I prefer the reasoning of Ormiston A-JA who rejected the submission that *Gambotto* does not apply to the mere removal of rights by way of their compulsory destruction … The limited view of expropriation suffers from its preference for form (legitimate compulsory extinction artificially distinguished from illegitimate compulsory transfer) over substance. To work a compulsory extinction is just as much a deprivation or expropriation as a compulsory transfer. Extinction leaves the remainder to "inherit the earth" just as they would if beneficiaries of a compulsory transfer.'

[84] I conclude that this case is governed by the principle enunciated in *Gambotto*. The power to amend the defendant's articles was validly exercised only if the resolution by which they were amended was passed for a proper purpose, and the article will not operate oppressively in relation to the members whose shares are forfeited. The power of amendment will have been exercised for a proper purpose if the company reasonably apprehended that the continued shareholding of the minority ie those

members who ceased to be suppliers of sugar, would be detrimental to the interests of the other shareholders generally.

[85] Although this point was argued the plaintiffs did not, as I understood it, in the end vigorously oppose the defendant's contention that the amendment to insert the new articles was for a proper purpose.

[86] The defendant has for many years enjoyed substantial taxation benefits by reason of its being a co-operative company for the purposes of the *Income Tax Assessment Act* 1936.

[87] Section 117 of that Act provides:

> '(1) In this Division, a ***co-operative company*** means a company … the rules of which limit the number of shares which may be held by … any one shareholder … and prohibit the quotation of the shares for sale or purchase at any stock exchange or in any other public manner whatever … and which … is established the purpose of carrying on any business having as its primary object or objects one or more of the following:
>
> …
>
> (b) the acquisition of commodities … from its shareholders for disposal …;
>
> (c) the storage, marketing, packing or processing of commodities of its shareholders;
>
> (d) the rendering of services to its shareholders …'

[88] Section 118 provides:

> 'If, in the ordinary course of business of a company in the year of income, the value of commodities … acquired from, its shareholders … or the amount of its receipts from the storage, marketing, packing and processing of commodities of its shareholders, or from the rendering of services to them, or the amount lent by it to them, is less respectively than 90% of the total value of commodities … acquired by the company, or of its receipts from the storage, marketing, packing and processing of commodities, or from the rendering of services, or of the total amount lent by it, that company shall in respect of that year be deemed not to be a co-operative company.'

[89] Section 120 allows as deductions against the assessable income of a co-operative company the rebates or bonuses it pays to its shareholders 'on business done by shareholders with the company', and repayments by the company of moneys loaned to it by a government of the Commonwealth or a state.

[90] The defendant has for many years taken advantage of deductions allowed by s 120 to such good effect that despite making substantial annual profits it has paid no

income tax. It is to maintain its status as a co-operative company that the defendant has utilised the provisions of articles 29, 30, 31 and 32 to forfeit the shares of members who have ceased to be suppliers. It is not just the plaintiffs who have been subjected to the operation, or threatened with the operation, of those articles.

[91] The continued shareholding by persons who do not supply sugar to the defendant would be detrimental to the company and the conduct of its affairs (the loss of the valuable tax deductions) if it were to lose its co-operative status. It is reasonable for it to preserve that status by doing business only with its members. To that end it forfeits the shares of members who cease to supply it with sugar cane.

[92] The plaintiffs' real complaint was that the articles allowed the majority shareholders to oppress the minority by expropriating their shares without any corresponding obligation to compensate them for the loss. As I have pointed out, unless the forfeited shares are resold the member whose shares are forfeited goes completely without recompense. This is, I think, an infringement of the *Gambotto* principle.

[93] The consequence is not, in my opinion, that articles 29(2), 30(2) or 31(1) are invalid. These operate to allow a forfeiture, but there is no complaint about that. The complaint is about forfeiture without compensation. That can occur by operation of article 32(1). The articles are capable of working fairly and without oppression to a member who ceases to be a supplier and whose shares are forfeited. If the shares are sold, as they may be pursuant to article 32(1) then the proceeds of sale are paid to the former member who thus receives fair recompense for their loss. This last statement may require one qualification. The recompense will be fair only if the shares are sold for their market value but article 32(1) is clearly subject to an implication that any sale of forfeited shares must be honest and the result of a reasonable attempt by the directors to obtain market value. It is only if the forfeited shares are disposed of other than by sale that there can be oppression to the expropriated shareholder.

[94] Accordingly article 32(1) is invalid only when the power it confers is invoked with respect to shares forfeited for non-compliance with a notice given pursuant to article 29(2) and to the extent that it permits the directors to dispose of the forfeited shares except by sale.

Validity of articles 29(2), 30(2) and 31(1): operation as a penalty

[95] The next point taken by the plaintiffs is that the articles in question operate as a penalty and are void for that reason. This argument is really an alternative to the one I have just considered, that the articles are invalid for contravention of the '*Gambotto* principles'. It is not necessary to consider the argument because of the success of the primary complaint. The invalidating of the article to the extent that they purport to allow the directors to dispose of forfeited shares other than by sale would be sufficient to overcome any concern that it operated as a penalty.

[96] The parties each adduced evidence touching the value of shares in the defendant. The question was said to be relevant to the argument that article 31(1) operated as a penalty by forfeiting shares without recompense. The plaintiffs called evidence from an accountant, Mr Sorbello in an endeavour to show that the shares had substantial value. It is not necessary to address this question, which the defendant

contested, asserting in turn that the shares were effectively worthless, or worth a nominal value.

[97] As I have mentioned it is not necessary to consider the arguments as to penalty. It is therefore unnecessary to say anything of the evidence about the value of the shares. In any event the evidence did not allow a conclusion as to the value of the shares. As the evidence unfolded it seemed clear that the shares had some value though it was quite impossible to express it in money terms. The only value comes from the fact that shareholders would have a right to participate in a return of capital should the defendant be wound up by its members, or be the target of a successful takeover.

[98] There is no evidence of the value of the defendant's assets, save for the director's opinion expressed in the accounts which have never been verified by independent valuation. The value of the shares would depend not only on the value of the company's assets but on the chance that it may be wound up or taken over. The first prospect seems remote indeed: the company has traded successfully since 1894 and provides a necessary service to its members who sell their sugar cane to it. No-one in evidence identified any possible reason why its members should wind it up. A takeover is always possible but the only evidence on the point, perhaps biased, is that no takeover offer is in prospect and the defendant is not an attractive target.

[99] It is impossible to know how these factors would reflect in a money value for the defendant's shares but, as I said, it does not matter for the outcome of the action.

Orders

[100] Accordingly I declare that article 32(1) of the defendant's constitution is invalid when the power it confers is invoked with respect to shares forfeited for non-compliance with a notice given pursuant to article 29(2) to the extent that it permits the defendant to dispose of the forfeited shares except by sale.

[101] I otherwise dismiss the plaintiff's claims. The parties should make submissions on costs. The plaintiffs succeeded only to a limited extent. The appropriate order may well be that the plaintiffs recover a small fraction of their costs, or that there be no order as to costs.