CORPORATIONS LEGISLATION - SHARE BUY BACKS AND SECTION 129

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It does us good occasionally to recollect that the concept of limited liability shocked some of our forebears. The recollection assists a realisation of the distance we have travelled in the companies firmament over a comparatively short time. On 22 February 1862 the *Law Times* imperiously denounced the Joint-Stock Companies Bill, then about to be re-introduced into the House of Commons, as one exhibiting "manifold imperfections" and asseverated that one of the improvements it required was "that shares should not be permitted to be paid up in full". "A margin should be left", so the *Law Times* thundered, "to meet ... cases ... where debts have been incurred beyond the moneys received. If all is permitted to be paid up, there is no fund for creditors, nor even for the costs of winding up the concern. The obvious remedy for this great defect of limited liability is to reserve a margin of uncalled capital to meet claims and contingencies".

How very odd that sounds to modern ears - as a cry in the wilderness.

There is a canny dictum to be found in what I will call *In Re Utopia Limited* in this vein -

> "Some seven men form an Association
> (If possible, all Peers and Baronets),
> They start off with a public declaration
> To what extent they mean to pay their debts.
> That's called their Capital : if they are wary
> They will not quote it at a sum immense.
> The figure's immaterial - it may vary
> From eighteen million down to eighteen pence.
> *I* should put it rather low;
> The good sense of doing so
> Will be evident at once to any debtor.
> When it's left to you to say
> What amount you mean to pay,
> Why, the lower you can put it at, the better."

You will be unlikely to find the authorised Law Reports expressing the law quite so vividly as that, but W.S. Gilbert, whose dictum it is, did found and bottom his operetta upon the *Joint-Stock Companies Act* 1862, and he uncovered a happy subject of lampoonery. It is not impossible that some enterprising Victorian judge - using the last adjective in any sense you please - might have adopted or adapted Gilbert's limpid wisdom, or might have liked to do so. Now, if Gilbert was not thoroughly familiar with the doctrine of *Trevor v Whitworth* (1887) 12 App Cas 409, he may at least be supposed to have been aware of it. Was not that decision a tap-root of our notions of company law? And was its precept not naturally upon the lips of most gentlemen of the City when Utopia Limited had its premiere at the Savoy Theatre in October 1893? But the sub-title of Utopia Limited was "The Flowers of Progress". Progress was foreseen and, rightly or wrongly, progress has been had - with what effect on the souls of Sir George Jessel and Lord Macnaghten one can but speculate. Those very learned judges, pre-eminently perhaps, were responsible for articulating what they took to be inherent in the doctrine of limited liability, as sanctioned by the 1862 Act, namely a prohibition against the purchase or acquisition by a limited company of shares in its own capital. One may argue that it was not absolutely inevitable that the statute should have been construed as it was to produce the result in *Trevor v Whitworth*: there was quite a respectable argument the other way and indeed the law did develop differently in the United States, as well we know. The statute was construed as it was, and the law develop as it did, in England and in Australia largely, no doubt, because of the kind of apprehension or fear that is inherent in Gilbert's satire.

Insofar as the rule in *Trevor v Whitworth* was a creature or a corollary of statute it was of course vulnerable to statutory modification. So for 120 years the court has been empowered to sanction a reduction of capital, thus countenancing in accordance with strict forms a departure from one of the concepts that buttressed the general rule. Again, for over 50 years a limited company has been entitled to issue preference shares that are liable to be redeemed. *Trevor v Whitworth*, now enshrined in statute as s 129 of the *Companies Code*, still nominally reigns but it cannot now be said to reign supreme. The most recent statutory modification of it, which took effect in November last year, has provoked this paper.

I shall treat as the relevant modifying legislation the provisions of the *Co-Operative Scheme Legislation Amendment Act* 1989 of the Commonwealth which, among other things, amends the *Companies Act* 1981 by inserting a new Division 3A of Part IV. By virtue of the scheme the *Companies Codes* of the States are of course each correspondingly amended. The *Corporations Act* 1989 of the Commonwealth does not contain the provisions: there is a forecast that it will be amended to do so but I am not privy to information reflecting the accuracy of the forecast in the light of that Act's recent vicissitudes.

The *Amendment Act* of 1989 is concerned with direct and indirect acquisitions by a company of its shares, the latter through a mechanism of cross-shareholding arrangements of a kind exemplified in *August Investments Pty Ltd v Poseidon Limited* (1971) 2 SASR 71. I shall, however, confine myself to direct acquisitions, called "buy-backs", which are covered by the new Division 3A (ss 133AA - 133VF). The essence of the Division is that, subject to the many conditions it imposes, it permits a public or a proprietary company to buy from one or more of its members ordinary shares in its capital, whether fully or partly paid. I invite you to note that the company may pay in cash or kind, although what the legislation provides for is that the company may buy, not barter. Also central to the legislation is the contemplation that shares bought back by a company from its shareholders should be cancelled. When there is a buying back all rights attached to the shares are suspended and, immediately after the transfer to the company is registered, the shares are cancelled by force of s 133PC and all rights attached to the shares are extinguished. Curiously, there seems to be no positive obligation imposed on the company to effect a registration but, if it is effected, the company's issued capital, but not its nominal capital, is thereupon reduced by the nominal value of the shares bought back.

Much already has been written about the new legislation describing the way in which it is intended to work and suggesting circumstances in which it might be expected to be put to use. I should not perform any useful purpose to canvass or even to try to summarise these kinds of things here: the technicalities are best gathered from a thorough perusal of the legislation itself (which is, if not user-friendly, then apparently user-sympathetic) and from textbooks and other expositions of it. Rather, I should like to attempt in a very selective way to examine what I take to be a couple of the possible consequences of the exercise of the power, and what I take to be some of the dangers of it to a company's creditors and to its directors.

First there are a few basic features of the new legislation that I cannot avoid labouring.

What the legislation in truth allows is the redemption by a company of shares that were not issued on terms that they were redeemable. A redemption really means a buying back. Use of the verb "redeem" is avoided, however, in the new legislation, presumably in order to distinguish a buy-back which is essentially voluntary and consensual from a buying back by way of redemption of preference shares that were issued on terms that they might be redeemed compulsorily and on the company's unilateral motion. So it is that fundamental to the new legislation are the terms "buy back" (without a hyphen) - a verb - and "buy-back" - a hyphenated noun. Each is a term of art. The noun is defined by s 133BB to mean an acquisition by a company constituted by the company's buying back shares. A company buys back shares when (as it is said) it buys shares in itself, so that when a company actually does that there is a "buy-back". The point of time when a buy-back is constituted is not expressly spelled out but there are in the legislation several references to "an agreement constituting a buy-back": eg. ss 133BH(1)(e), 133BK, 133JA(c), 133LG, 133RA, 133RB and 133RC. The concept therefore seems to be entirely contractual. Before a buy-back can be said to exist there must be an enforceable agreement which involves a buying by a company from one or more of its shareholders of ordinary shares in its own capital; and when such an agreement is made the buy-back exists. This conclusion is reinforced by s 133FB(1), which provides that -

> "A buy-back is made under a buy-back scheme if, and only if, it results from the acceptance of an offer made under the buy-back scheme".

It seems to follow that each enforceable agreement made by a company to purchase its shares is an individual and distinct buy-back which is complete when the agreement is made, and whether executory or not.

Another point to note is that an agreement constituting a buy-back may be enforced by an order for specific performance (s 133RA) unless the company proves that it is unenforceable by virtue of s 133RB - ie. broadly, because the company is in financial difficulty. Presumably any other defence to a claim for specific performance would be available, too, whether the plaintiff were the seller-shareholder or the buyer-company.

Buy-backs may be selective or made pari passu with all shareholders or all of a particular class. If selective they may be made by private treaty and, by provisions not yet in operation, it is intended that they may be made by transactions on the Stock Exchange. If a public company does not buy back on the market, and does not make a selective purchase off market approved by special resolution, or make an employee shares purchase or an odd-lot purchase, it can buy back only in accordance with a buy-back scheme. A buy-back scheme involves the company's making written offers in uniform terms to buy back to all persons who held ordinary shares (or, it seems, a class or ordinary shares) as at the time when the first of the offers is sent for a fixed proportion of each holding. The similarity in some features to a take-over scheme is evident.

The buy back power is conferred on the company but is exercisable only by the directors. The power has in general been welcomed by commentators and vaunted as heralding a new era in company law in Australia, essentially because it is said to afford greater flexibility to companies than previously existed for the deployment of capital. Australian companies are now, in this respect, in a substantially similar position to those in senior commercial nations - notably the United States, the United Kingdom, Canada and many in the European Community. I do not want to disagree with that assessment. It may very well be that share buy-backs will become routine here, just as court-sanctioned reductions of capital have long-since been routine - perhaps more so, though that I do not predict.

I do want to advance the thesis, however, that the share buy-back power, though useful, is a dangerous power. That is not to deny that it may be put to good use in the same way as any other useful power - be it steam, electric, nuclear or fiduciary - but, like all those, it needs to be handled with care and with a full knowledge of the perils that can attend its abuse. The danger is posed, as it seems to me, to creditors, to directors and perhaps to the company itself and its members, and it is no mere illusion.

I refer first and with some emphasis to creditors, whom the new legislation has striven hard to protect from potential depredation of buy-backs. Partlett and Burton, in a stimulating article recently published in the Australian Law Journal ("The Share Re-purchase Albatross and Corporation Law Theory" (1988) 62 *ALJ* 139) have submitted that proposed reforms to enable a company to buy back shares in its own capital had been "unduly timid". They advanced the view that it is a "gross fiction" that creditors deal with companies in the real world on the strength of the issued capital. That is a view I consider to be altogether too sweeping. Whether or not all trade creditors do advance credit to a company by reference to its issued capital the fact is that they are entitled to do so, and the principle of limited liability has been practised in this country upon the footing that they are so entitled. If we are now to adopt a philosophy the reverse of what used to be accepted as axiomatic, and say that no creditor should be entitled to look with confidence to the company's issued capital, we shall have to re-learn a great deal of what we used to think was not only right but necessary. It has also to be remembered that not every creditor of a company assumes that status voluntarily as a result of extending credit which he can equally choose to withhold. Some people are driven to seek monetary redress from a company for a wrong done to them and they are obliged to take their chances in finding the company worth a claim.

Certainly many possible disadvantages to creditors will be avoided by the stringency of the conditions imposed as pre-requisites to the exercise of the buy-back power. I shall not dwell on these conditions but they include authorisation in the company's articles (which lasts only three years at a time), solvency declarations by all directors, shareholders' approval by special or sometimes by ordinary resolution, the requirements of objective expert opinion as to the fairness of consideration to be paid for a buy-back and public advertisement and the imposition of potential personal liability upon directors. Given all this, there is comparatively little said in the legislation about the precise way in which the courts may assist creditors to defeat a proposed exercise of the buy-back power that is inimical to their interests. A company proposing to buy back any of its shares (unless for practical purposes the contract is for an employee shares purchase or an odd-lot purchase) is required to advertise its proposal by notice in a newspaper: s 133LA. If such a notice is published a creditor is entitled to apply to the court for an order "prohibiting the making of the offers or the entering into of the agreement": s 133LD. This section was presumably intended to allow a creditor to apply to nip an incipient buy-back in the bud, but the powers of the court upon such an application appear to be curiously limited. Section 133LE requires the court, if satisfied that the company is insolvent, or that a declaration of solvency is no longer in force, or that the company is unlikely to remain solvent as specified in the relevant notice of solvency, to make a prohibitory order, presumably in the nature of an injunction. It is unclear from the section whether the respondent to the creditor's application should be anyone other than the company. The fact is, however, that the section does not enable the court to enjoin any potential party to a proposed buy-back other than the company. All that the court can do under the s 133LE(1) is to "prohibit *the company*, except on such conditions (if any) as the order specifies, from making the offers or entering into the agreement, as the case may be ...". Otherwise, the court is *required* to refuse the creditor's application. It follows that if the company has made its offers to shareholders at the time the creditor's application is made - and it should be remembered that offers under a buy-back scheme must, unless withdrawn with the Commission's consent, remain open for at least one month - the court cannot under this section enjoin an offeree from accepting the company's offer to buy. Any acceptance of such an offer would, it seems, result in a buy-back, the agreement constituting which (if s 133RA is to be taken at face value) would be specifically enforceable at the instance of the shareholder.

Let it be supposed that a company's creditor, claiming to be at risk from a proposed buy-back or buy-back scheme, did manage to approach the court for protection before any buy-back sprang into being. The jurisdiction that the court can exercise under s 133LE is strictly limited, depending in effect upon proof of the company's present or likely future insolvency. Unless such proof is provided the court is required to refuse the creditor's application.

The legislation appears to assume that the only legitimate interest that a creditor should be entitled to protect by force of the legislation is one consisting in the company's continuing solvency. Solvency, for the purposes of the legislation, means the company's ability to pay all its debts as and when they become due and payable. In reality one knows that a creditor's interest may well be much wider and more sensitive than that. Take the relatively simple case of a creditor who holds a first-ranking debenture charge over certain of the debtor company's assets or even a floating charge over the undertaking of a subsidiary of the debtor. It is entirely possible, as it seems to me, that a reduction of the debtor company's capital achieved by a buy-back of its shares in consideration of assets, especially assets other than money, could result in an undermining, or a demotion in priority, or even a loss, of the security. All this may happen without the debtor company's necessarily becoming insolvent but not without discomfort to a secured creditor.

Were such a reduction of capital to require the sanction of the court under s 123 of the Code the secured creditor would no doubt have immediate standing to object because his security might be imperilled. In practice it might be doubted whether the reduction would stand a practical chance of being sanctioned without his consent, or at least without the court's being satisfied that he was not disadvantaged by the proposed reduction. The position of such a secured creditor in the context of the buy-back legislation is much less clear. I should not suppose that he is without a remedy but what it is, and the way it may be sought, are not conspicuously clear. If the creditor learns from a newspaper advertisement, or on the grapevine, facts which cause him to fear for his security, it is he who is left to take the initiative to induce the court to protect it. On the other hand, when the debtor company is obliged to justify its reduction of capital by seeking the court's sanction under s 123, it is the company that runs the risk of non-persuasion. Under the new legislation the debtor company has what looks very much like an absolute legislative entitlement to buy back its shares, with all the consequences that that entails, if the prescribed statutory conditions are satisfied. Whether the statutory conditions will prove sufficient to afford reasonable protection to creditors only time will tell.

The Companies and Securities Law Review Committee (to which the Australian commercial community owes a handsome debt for its work on this topic) recognised in its report that a buy-back power, necessarily involving the distribution of corporate assets to shareholders, poses an increased financial risk to creditors and remaining shareholders. The Committee suggested that the imposition of strict solvency requirements would best protect the rights of creditors and remaining shareholders, and pointed out that creditors might also protect themselves by imposing restrictions in debt covenants. The Committee's supposition was that debenture trust deeds and other financing instruments might be employed to restrain the company from buy-backs detrimental to creditors (paragraph 27 of its report). I have already submitted that the satisfaction of solvency requirements alone may not achieve all that a secured creditor might desire. As to the imposition of restrictions in debt covenants, it needs to be understood that the buy-back provisions have statutory effect by virtue of s 133CC(1) despite the constituent documents or a resolution of a company or "*any agreement*".

The notion that the new Division 3A should have effect despite "any agreement" (whatever that expression may mean) does not seem to have derived from any recommendation of the Companies and Securities Law Review Committee and, indeed, on one view, may not square with the Committee's expectations. There seems to be scope for argument as to what s 133CC(1)(e) means to say when it lays it down that "Division 3A has effect despite ... any agreement". Does the sub-section refer to any agreement made by the company? If so, does it mean that no agreement made by the company with a creditor could affect the company's right to buy back its shares in accordance with the Division? If it does mean that, then the limited right given to a creditor under the Division to apply to the court only in the case of, or in anticipation of, the company's insolvency (as defined) has the potential to constitute a severe privation of secured creditors.

The point has a particular significance with reference to proprietary companies and it is brought into high relief when one notes that the company's consideration for a selective off-market purchase of its own shares may be its assets other than cash. A public company's buy-back cannot exceed what is called, in rather shirt-sleeved language, "the 10 per cent in 12 months limit", apart from employee shares purchases or odd-lot purchases: s 133BE. That puts a brake on a public company as to the proportion of its issued shares that it can buy back within a period of 12 months. It does not affect a proprietary company if a proposed selective buy-back is approved by a special resolution of the company on which vendor shareholders or persons associated with them do not vote. Subject to that there is no limit on the number or proportion of its shares that a proprietary company can buy back in any period so long as its membership does not fall below the minimum requirements of s 82 of the Code.

Let the potential of that be illustrated by the old Irish case of *In Re The Balgooley Distillery Company Ltd* (1886) 17 LR(I) 239, the decision in which was cited with evident admiration by Lord Fitz Gerald in *Trevor v Whitworth*. The company, a whiskey distiller, had accumulated a large stock of its product in bond and for which, for a reason unexplained in the report, it was unable to find a market. The directors determined to sell 20,000 gallons of it to one of their number at two shillings and nine pence the gallon. It was not for his own use but so that he might personally undertake the bottling and sale of it, as he said, "in order to relieve the company". The price for the sale was not suspect but the means of payment was. The purchase by the director, involving a consideration of just over 2,500 pounds, was financed by his surrendering to the company his 500 fully-paid shares of 10 pounds each in its capital, for which the company credited him with four pounds per share, thus yielding him 2,000 pounds. The balance he paid in cash. The 500 shares were assigned to the company and cancelled and subsequently the transaction was ratified by the company in general meeting. Some two-and-a-half years later the company was ordered to be wound up. The liquidator sought payment from the director of 2,000 pounds on the footing that the transaction had been void because it had involved a purchase by the company of its own shares and also an impermissible reduction of its capital. With some regret the Irish Court of Appeal disallowed the liquidator's claim, although the reasoning could scarcely have survived *Trevor v Whitworth*. In the course of an elaborate judgment, which was presumably the point of Lord Fitz Gerald's admiration expressed in the House of Lords, Fitz Gibbon, LJ said -

> "I see danger in permitting a company to deal at all, by way of purchase or sale, with that limited capital which is the essential condition of its existence, and I fail to see any satisfactory distinction between trafficking in shares, as it is called (which is admittedly illegal), that is, buying them with the intention of trying to sell them again at a profit, and acquiring them for valuable consideration for other motives."

The modern legislation would presumably accommodate a scheme of the kind effected in the *Balgooley Distillery Case*. The winding up of the company had begun so long after the occurrence of the transaction in question that it seems unlikely that provisions such as those in sub-div Q of the new legislation, providing for directors' indemnity, would have given creditors much comfort. The scheme was one such as James, LJ described in *Hope v International Financial Society* (1876) 4 Ch D 327, 355 to be "... however honestly it may have been intended by these parties who, I dare say, thought no harm would come of it - a scheme to divide the assets between the shareholders under the guise of the company's purchase of the shares - a device, in fact, to evade the provisions of the law regulating the reduction of capital".

It is a little ironic that nowadays such a scheme would not evade, but would presumably be encouraged by, the provisions of the law regulating the reduction of capital. Taken to its logical limit the scheme could work, if not a winding up, then an appreciable winding down of a proprietary company. Indeed it has been said to be one of the virtues of the new legislation that it gives companies the ability and flexibility to decline in size, but the cost to creditors must yet be counted. It might be answered that a debenture holder, for example, always runs the risk that his debtor will sell off its assets that are subject to a floating charge. Hitherto, however, the chargee has run that risk in the expectation that the company, if it does sell, will receive value for the sale other than the cancellation of paid up shares. The holder of an existing floating charge who has not given consideration to the effect of the new legislation upon his security might perhaps be wise now to do so.

Dwelling as I have on the important position of creditors has, I am afraid, squeezed out much of what I would otherwise have liked to say in the available time. I should like, however, to make some short and rather random observations about the likely or possible effect of the new legislation on the role played by directors. If the new buy-back power gives directors greater scope and flexibility in the management of capital, it will indubitably carry with it an increase of their responsibilities.

As I have already mentioned in passing, there can be no buy-back at all of any kind unless there is in force a declaration signed by every one of the directors individually to the effect that it is the opinion of the directors that (among other things) the company was solvent on the day the first of them signed the declaration and that the company will remain so during the next twelve months. Such a declaration must cast a troublesome obligation on any director signing it. A copy of the declaration must be filed with the Commission at the latest seven days after it is made. It therefore amounts to a public and easily provable representation by each director that he or she had, when signing it, the opinions described in it. That seems to mean not only that each director had the opinions that the company was solvent and would remain so but that each had the opinion that each other director had the same opinions. So to represent involves a stout undertaking which, to use a familiar formula, ought not by any to be enterprised nor taken in hand unadvisedly, lightly or wantonly. I do not labour the point beyond saying that civil liability in negligence of directors to creditors or shareholders who suffer loss when acting on the faith of such a representation would appear to be a distinct probability. Moreover, a director who signs a solvency declaration may become personally liable to the company, in the circumstances set out in sub-div Q of Division 3A, in effect to restore to the company an amount equal to the consideration provided by the company for a buy-back. If, for example, the company is wound up within the succeeding twelve months the directors may be liable to make up to the company any capital loss resulting from a capital reduction involved in the buy-back. The liability appears to be absolute save that a dispensing power is conferred on the court in terms similar to those of s 535 of the Code.

It is worth comparing the position of directors when a reduction of capital is sought to be made in what I may call the conventional way, involving an application for the court's sanction. In such a case the directors undertake no obligation to represent to anyone the state of the company's solvency. They can with propriety leave it to the court to be satisfied, upon appropriate evidence and argument, that the terms of the proposed reduction are fair to creditors and to all shareholders and are in the public interest and that the reduction ought to be approved. The court has a wide discretion and is bound to go into all the circumstances, considering what equity the company has to call for the court's interposition. The potency of that discretion was recently illustrated by the decision of the New South Wales Court of Appeal in *Catto v Ampol Ltd* (1989) 16 NSWLR 342. The onus of satisfying the court of the propriety of the reduction is real and substantial but the point to be made here is that the onus is the company's and not that of the directors; and they are protected, if they have acted in good faith, by the court's decision in advance from any claim against them if the reduction of capital should prove disastrous for creditors or shareholders. This is an advantage of the procedure under s 123 of the Code that is perhaps often overlooked. No such advance protection can, however, be afforded to directors acting under the new legislation to achieve a reduction of capital by means of a buy-back.

As I have noted also in passing a buy-back power has long existed in the United States and it has generated, or at least allowed, the development of a range of principles and attitudes which have enormously increased directors' powers but also their responsibilities. Many of the individual States have now confirmed the power by statute in a very broad way. Thus in Delaware the relevant Code provides, with a remarkable conciseness and (by our standards) an amazing breadth, that -

> "Every corporation may purchase, redeem, receive, take or otherwise acquire, own and hold, sell, lend, exchange, transfer or otherwise dispose of, pledge, use and otherwise in and deal with its own shares ..." : 8 Del C s 160(a).

Certainly there are statutory conditions to be observed in the exercise of the power and they are, I gather, proliferating in State and notably in Federal legislation. Mr David Huggin will no doubt refer to these in a way which is beyond my capability.

One purpose for which the buy-back power has been used in the United States is to deal with a hostile take-over bid. An example is provided by the decision of the Delaware Supreme Court in *Unocal Corporation v Mesa Petroleum Co* (1985) 493 Atlantic Rep 946. I understand that Mr Huggin will refer to this and I shall not go into any detail about it. The directors of the target company arranged that the company should make a tender for its own issued stock, including that of the directors, in exchange for debt securities, but excluding the raider from the tender. The Supreme Court dismissed the raider's protest on the essential basis that the board of the target had not only a power to make the self-tender but, in the circumstances, a positive duty to take steps to thwart the take-over bid. The take-over bidder, Mesa, was controlled by the disingenuous T. Boone Pickens Junior, who was seen as having an established reputation as a greenmailer. "Greenmail" I take to refer to the technique of taking a large position in a company's stock, threatening a take-over and then selling the shares back to the company at above-market prices - a form of corporate blackmail. The two-tiered "front loaded" bid by Mesa involved, as the second tier, an offer of so-called junk bonds designed to be irresistible, and was perceived by the board of Unocal to be inimical to the interests of shareholders as a whole. The court said, notably that "... in the face of the destructive threat Mesa's tender offer was perceived to pose, the board [*scil.* of the target] had a supervening duty to protect the corporate enterprise, which includes the other shareholders, from threatened harm". In applying the business judgment rule, given the directors' duty, the court concluded that -

> "... unless it is shown by a preponderance of the evidence that the directors' decisions were primarily based on perpetuating themselves in office, or some other breach of fiduciary duty such as fraud, overreaching, lack of good faith, or being uninformed, a Court will not substitute its judgment for that of the Board".

Now that Australian companies have the buy-back power, an interesting question is whether the law will develop in this country to the extent that it has in, for example, Delaware, so that directors have not only the right but the duty to exercise it in an appropriate case; and if the directors have such a duty what will the consequences be if they do not exercise it?

We have a well-established business judgment rule of our own. So, in *Harlowe's Nominees v Woodside (Lakes Entrance) Oil Co NL* (1968) 121 CLR 483 the High Court observed, at page 493, in a celebrated passage that -

> "Directors in whom are vested the right and the duty of deciding where the company's interests lie and how they are to be served may be concerned with a wide range of practical considerations, and their judgment, if exercised in good faith and not for irrelevant purposes, is not open to review in the courts".

If, on the other hand, the directors use their power for an impermissible purpose, whether it is dominant or not, it seems likely that the purported exercise will be interfered with by the courts "if the impermissible purpose was causative in the sense that, but for its presence, 'the power would not have been exercised'": *Whitehouse v Carlton Hotel Pty Ltd* (1987) 162 CLR 285, 294.

Much of the discussion in Australian courts of the business judgment rule has been generated in the context of increases in capital by the issue of new shares. *McGuire v Ralph McKay Ltd* (1987) 12 ACLR 107 is a recent example. Now it can be expected, perhaps, that the rule will call for consideration in the new context of reduction of capital by the cancellation of shares the subject of buy-backs. The law will, it is to be hoped, develop slowly and carefully; but already it has been said, albeit rather tentatively, that it is within the functions of the directors of a company to ensure that where an unsatisfactory take-over has been made there is an alternative offer open at a better price. *Darvall v North Sydney Brick & Tile Co Ltd* (1987) 16 NSWLR 212, 324. The Americans' experience suggests that our self-purchase power, just as much as theirs, is quite capable of providing directors with a tantalising dilemma.

Speaking of dilemmas, I refer you in conclusion to the refined sort of mixed metaphor that the usually impeccable Sir Hugh Cairns employed, before he became Lord Chancellor, to advise the House of Commons that: "It is always dangerous to pin yourself to one horn of a dilemma until you have heard the other". I have endeavoured to expose part of one horn but I fear we may have to attend very carefully to the Australian development of the buy-back power before we hear the full extent of the other.