Beneficial interests in company shares: voting rights - II

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This is the final section of the article which began in the last issue of this Review at page 261. Of the four categories of fiduciary relationships giving rise to beneficial interests in company shares, one — the trust — was discussed earlier. Here the author completes his review of the law with a consideration of bankruptcy situations, mortages of shares, and unregistered share transfers.

II. THE NATURE OF THE RIGHTS UPHELD BY THE COURTS (Cont'd)

B. Bankruptcy

Unlike the cestui que trust, whose rights are very much a matter of Common Law, the rights in New Zealand of the assignee in bankruptcy as "beneficial owner" of shares are specifically prescribed by statute.

It appears that it is unnecessary for the assignee in New Zealand to be entered on the register of shareholders in order to deal with any shares forming part of the bankrupt's estate.[1] In these circumstances the rights of the assignee in respect of such shares, whilst they remain in the name of the bankrupt pending disposal, are protected by provisions in both the Insolvency Act 1967 and the Companies Act 1955.

Section 42(2)(b) of the Insolvency Act 1967 provides that subject to certain exceptions[2] the property and powers of the bankrupt to vest in the assignee and be divisible amongst his creditors include

> The capacity to exercise and to take proceedings for exercising all such powers in or over or in respect of any property whatsoever and wheresoever situated as might have been exercised by the bankrupt for his own benefit at the commencement of the bankruptcy or before his discharge.

In so far as company shares are concerned that section is supplemented by section 85 (2) of the Companies Act 1955 which provides that subject to pro-

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1 Section 74(1) of the Insolvency Act 1967. See also Article 29 Table A which is not mandatory in its requirements of transmission of a bankrupt's shares.

2 See ss. 47, 48, 49, 50 and 59 of that Act.

duction of satisfactory evidence of his status the assignee shall be entitled, inter alia, to the same voting rights as the registered holder would have been entitled had he not become bankrupt.

The combined effect of those two sections is to vest the actual voting rights on the shares in the assignee notwithstanding that the name of the bankrupt may remain on the register as the legal owner of the shares. Section 85(2) thus represents a statutory gloss on the long-standing principle of company law reflected in section 125 of the Companies Act 1955 for, whereas in the case of a deceased shareholder it does no more than establish the means for recording the vote of the representative of the legal owner, in the case of a bankrupt shareholder it establishes a direct link, for voting purposes, between the company and the person representing the totality of the beneficial interests in the shares.

Although section 85(2) of the Companies Act 1955 has no English counterpart it is nevertheless submitted that the English cases will apply as good authority in New Zealand to determine the respective rights of the asignee and the bankrupt in the interim period after adjudication until production to the company of the evidence as to the assignee's status which may from time to time be properly required by the directors. During that period the bankrupt shareholder's name will, in the absence of any provision in the articles to the contrary, remain on the register and it is with the register alone that the company will be concerned.

The headnote to the official report of the judgment in *Wise* v. *Lansdell*[3] states that it was held, by Astbury J. that, as between himself and the company, the bankrupt, so long as he remained on the register, was entitled to vote in respect of the shares. Unfortunately the judgment is neither as clear nor as forceful on this point as the headnote would seem to suggest. The bankrupt shareholder, who remained on the register, attended and voted at a meeting of the company called to deal with a resolution reappointing for another year a director who was due to retire. The Chairman of Directors refused to accept the bankrupt shareholder's vote and his subsequent demand for a poll, on the ground that the bankrupt was not a shareholder and not entitled to vote. Subsequently a resolution for voluntary winding up was passed in the same manner. The bankrupt shareholder then brought an action for a declaration that the resolutions were invalid and for an injunction to restrain the defendants from acting on them.

In argument counsel for the defendants maintained that on the bankruptcy the entire property in the shares and the right to vote passed to the trustees in bankruptcy whose subsequent disclaimer of the shares as onerous property determined the bankrupt's rights in the shares, including his right to vote in respect thereof. In short, it was argued that his membership of the company was thereby determined. Astbury J. refused to accept that argument finding that the disclaimer related only to the bankrupt's beneficial interest in the shares:[4]

> The voting power exercisable or obtainable in respect of these shares on behalf of those beneficially interested has not been destroyed by anything that has taken place in the bankruptcy.

3 [1921] 1 Ch. 420.
4 Ibid. 431.

However his opinion that[5]

> The bankrupt's interest, as far as it was a beneficial interest, in these shares had ceased to exist, but as between the real owners of the shares and the other shareholders in the company, he still had left in him a voting power by reason of being on the register.

cannot be propounded as conclusively determining the respective rights of the bankrupt and his assignee beyond all doubt because, since the shares were heavily encumbered, the assignee's disclaimer meant that the voting power was exercisable at the direction of the mortgagees for whom the shares were held.

That unsatisfactory feature of the judgment was noted by Dankwerts J. in *Morgan* v. *Gray*[6] where a similar refusal by a company to record the vote or proxies of a bankrupt shareholder was sought to be justified by the company on the ground that although he might remain for a time on the register a bankrupt shareholder ceases to be a member of the company. The refusal of the company to receive the bankrupt's vote was held to be invalid and orders were made restraining the defendants from acting upon the resolutions passed in disregard of that vote. Dankwerts J. commenced by commenting:[7]

> It is curious that apparently it has never been decided whether, in spite of bankruptcy, a member of a company who remains a registered proprietor of shares on the company's register can continue to vote.

He then proceeded to the conclusion in respect of a company still in operation that:[8]

> It seems to me that, unless there is some provision in the company's articles or in the Companies Act which empowers me to say that the bankrupt is no longer a member of the company, and is, therefore, unable to vote, expressly, I must come to the conclusion that the bankrupt still remains a member as long as he is on the register; notwithstanding that by taking appropriate steps under the appropriate provisions the trustee in bankruptcy may be able to secure registration of himself as the proprietor of the shares. Unless and until that is done, and as long as the bankrupt remains on the register of the company, he remains a member in respect of those shares and is entitled, as it seems to me, to exercise the votes which are attributable to that status, notwithstanding that he has no longer any beneficial interest in the shares and that the company is entitled to pay any dividends to his trustee in bankruptcy.

Having so determined that the bankrupt could still vote he had no doubt that he must exercise his vote in accordance with the direction of his trustee in bankruptcy because the full beneficial interest in the shares would have vested in the trustee.[9]

Two reservations only need be recorded in respect of Dankwerts J's formulation. First, those principles will only apply only in respect of shares in a company which is a going concern. The wording of section 215(a) of the Companies Act 1955 is very strong and makes it plain that the assignee is the contributory in any wind-

5 Ibid. 430.
6 [1953] 1 Ch. 83.
7 Ibid. 86.
8 Ibid. 87.
9 Ibid. 86.

ing up and that the bankrupt has absolutely no status in that regard. Secondly, provision in the articles to the effect that upon bankruptcy a shareholder shall cease to be a company member and thereafter shall not be entitled to vote will prevail over the Common Law rules.

To recapitulate, the assignee's rights in respect of the bankrupt's shares may be placed in their correct perspective thus:

(a) Pending production by the assignee of such evidence of his status as the company may require pursuant to section 85(2) of the Companies Act 1955, and subject to any contrary provision in the articles the bankrupt shareholder, who remains on the register retains the power to exercise the voting rights on the shares so long as the company is a going concern. During that time the assignee has the right to control the vote of the bankrupt shareholder.

(b) After production of that evidence the assignee may himself directly exercise the voting rights without becoming a registered member by transmission or transfer and notwithstanding that the bankrupt shareholder may remain on the register.

(c) Alternatively, if registered as owner, the assignee may vote in the usual manner.

C. Mortgages

1. *General*

It is appropriate at the outset to refer to the manner in which a mortgage of company shares may be effected. For this purpose a distinction must be drawn between a legal mortgage and an equitable mortgage.

A legal mortgage of shares is implemented by registration of a transfer of the shares to the mortgagee which usually will be accompanied by an agreement or deed made between the mortgagor and the mortgagee establishing that it is a transfer by way of security only and reserving to the mortgagor the right to redeem his property. Because of the provisions of section 125 of the Companies Act 1955 the transfer will operate from the company's point of view as an out-and-out transfer so that the register will show the mortgagee as absolute owner. Such a mortgage clearly offers the greatest protection to the mortgagee in whom all of the usual rights of share ownership vest upon registration. It may not however always be prudent[10] or even possible[11] for a legal mortgage to be created in which event the parties may resort to an equitable mortgage.

10 E.g. If the shares are not fully paid up the mortgagee would, by taking a complete transfer to himself, incur the liabilities of the shareholder — *Re Land Credit Company of Ireland, Weikersheim's Case* (1873) L.R. 8 Ch. App. 831.

11 E.g. Where there are pre-emptive provisions in the company's articles, an absolute discretion in the directors to refuse registration which it is reasonably anticipated may be adversely exercised, or perhaps where the existence of a debt due to the company which the company requires to be liquidated prior to registration.

An equitable mortgage of shares is created by the deposit with the mortgagee of the share certificate which is held as security for the advance.[12] Generally the parties will also execute an agreement or deed setting out the terms of the mortgage and their respective rights and obligations[13] which will accompany a share transfer in blank executed by the mortgagor. The equitable mortgage, although resolving the registration difficulties associated with the legal mortgage, is open to the criticism that the mortgagor remains the legal owner and is therefore free to enter into dealings which may be adverse to the interests of the mortgagee thereby creating a prior legal interest to which the equitable charge may be postponed.[14]

From the above brief explanation it will be observed that the position of the registered shareholder under both the legal and equitable mortgage is not strictly analagous to that of the trustee. The trustee has no beneficial interest in the shareholding, whereas the registered shareholder in the mortgage transaction, whether he be the mortgagor or mortgagee, maintains some interest in the mortgaged property, as of course does the other party to the transaction.

2. *The legal mortgage*

For the legal mortgagee of shares who is entered on the register no practical difficulties exist in respect of his own interests because the power to cast the vote is vested in him. In his case the sole issue to be determined is the ability of the mortgagor to protect his beneficial interest by controlling the way in which the mortgagee casts that vote.

The respective rights as to voting of the legal mortgagee and his mortgagor were subjected to extensive argument and precise judicial formulation on an interlocutory appeal in *Siemens Brothers & Co. Ltd.* v. *Burns*.[15] The mortgagees in that case were trustees for debenture stockholders of the mortgagor company, and, as such, were entered on the register of another associated company in which the mortagagor company owned shares. The issue was clouded somewhat by the existence of an express agreement in the debenture trust deed in respect of voting rights. That agreement was not conclusive however because it contemplated that any voting by the mortgagor was to be done only at the mortgagees' discretion. To that end Swinfen Eady M. R. said:[16]

> These shares are specifically mortgaged premises, and the provision that the trustees may permit the company, or any nominee of the company, to exercise any powers and rights incident to the ownership of any of the specifically mortgaged premises, and in particular any voting right, has this operation, that it shows that there was an express agreement between the parties as to the extent to which, if at all, the company was to exercise or have the benefit of any voting rights in respect of the shares . . . the contract itself shows that the mortgagor company was only to have voting rights so far as the trustees for the debenture-holders permitted them to have them."

12 In itself such a deposit is sufficient to create an equitable mortgage — *Coote on Mortgages* (9th ed. Stevens, London, 1927) Vol I, 315.
13 See e.g. E. C. Adams (1944) N.Z.L.J. 264.
14 *Coote* op. cit. 313.
15 [1918] 2 Ch. 324.
16 Ibid. 336.

Having so disposed of any argument based on the terms of the agreement he proceeded to explain the rights of the parties to the transaction in the following terms:[17]

> In the ordinary way, where shares are transferred to and registered in the name of a mortgagee it follows, from his position as owner at law of the shares, that the ownership carries with it the voting right, that this is vested in the owner of the shares; and it would require a contract to exclude that right. Sometimes, where shares form a security, there is a contemporaneous collateral agreement as to the mode in which, and the extent to which, voting rights in respect of the shares shall be exercised. But in the absence of any such agreement the voting rights would be with the legal owners of the shares, and it would require a contract to control the exercise of those rights.

For good measure the Master of the Rolls added that such general principle did not conflict with or detract from a provision in the deed (usual in such documents) that the mortgagor should be permitted to hold and enjoy the mortgaged property and to carry on thereon and therewith its own business.

The Master of the Rolls concluded on this matter, quite unequivocally, that the mortgagees were entitled to exercise their voting rights as in their judgment they deemed best irrespective of any directions of the mortgagor company as to the way in which their votes ought to be recorded.

Puddephatt v. *Leith*[18] is also relevant. Pursuant to an agreement to advance moneys on the security of fully paid shares in a limited liability company those shares were transferred into the mortgagee's name. By a collateral agreement the mortgagee had undertaken to vote, in all cases where a vote was necessary, strictly in accordance with the mortgagor's directions. Subsequently the mortgagee voted at a company meeting against the wishes of the mortgagor and indicated that he intended to do so again at the next meeting of the company. The mortgagor then moved the court for an injunction to restrain the mortgagee from voting in respect of the shares otherwise than in accordance with the mortgagor's directions. Sargant J. held that the collateral agreement had been proved, was binding on the defendant and that the mortgagor's rights under it were clear. His judgment proper turned on her right to a mandatory injunction which he granted to enforce her rights.

3. *The equitable mortgage*

Coote on Mortages[19] states:

> Where the registered owner of shares executes a blank transfer to the mortgagee, he has still, as between himself and the company, a right to exercise the voting power conferred by the shares. But as between himself and the mortgagee, the power is exercisable at the dictation of the mortgagee and the bankruptcy of the mortgagor will not affect that right.

Wise v. *Lansdell*[20] which is the only clear authority on the exercise of voting rights where the mortgagor remains on the register, is cited as authority for that

17 Idem.
18 [1916] 1 Ch. 200.
19 Op. cit. 311.
20 Supra. n. 3.

proposition.[21] In that case Astbury J. decided that the mortgagor's bankruptcy in no way affected his obligation to exercise the voting power on the shares at the direction of the mortgagees. Applying his statement of law to the facts of the case he said:[22]

> I have no evidence as to what instructions, if any, were given to the bankrupt before the meeting of February 28, when the votes which he tendered were refused. It appears to me, although I think the question is a difficult one, that certain machinery was open to the mortgagees under which they could have obtained the right to vote directly in respect of these shares, though whether they would, in the circumstances, have been wise in coming upon the register may possibly be doubtful. It may very well be that before or instead of putting that machinery into operation they made use, or were entitled to make use, of the voting power of their mortgagor as a registered member for the purpose of maintaining their rights. The defendants have not satisfied me that the vote given by Wise on February 28 was, as far as the defendants' rights are concerned, a vote which in the circumstances they were entitled to disregard . . . . The bankrupt's right to take and rely upon [that point] depends upon whether he acted as agent for the mortgagees.

Later in the judgment, referring to the mortgagees the learned Judge said:[23]

> They were advised, apparently, that so long as Wise remained on the register as a member and was willing to act at their dictation it was unnecessary for them to accept the learned judge's offer [to obtain registration in their own names]. I am not prepared to dissent from the accuracy of that view.

4. *Evaluation of the rules relating to mortgages*

The following propositions may be extracted from the above authorities:

(a) As a general rule the legal mortgagee of shares who is on the register of shareholders is entitled to exercise the voting rights in respect of the mortgaged shares as he, in his own judgment, considers best. He is not obliged to vote according to the mortgagor's directions as to the manner in which the latter wishes the vote to be recorded.

It is clear from the judgment of Swinfen Eady M. R. in *Siemens Brothers & Co. Ltd.* v. *Burns*[24] that he was deciding the relevant appeal in that case on the ground that a mortgagee on the register is entitled to vote as he thinks fit. Any objection that his statement of general principle was obiter dictum was subsequently rejected (quite correctly it is submitted) by Russell J. in *Musselwhite* v. *Musselwhite*.[25]

Moreover, although it involved an appeal on an interlocutory application, and, irrespective of the absence of any previous authority cited in support, the judgment of Swinfen Eady M. R. represents in England a binding decision of the Court of Appeal on this point.

Although one must be wary not to overlook any possible criticism of the judgment of the Master of the Rolls by reason of his failure to spell out in exact

21 See also Key & Elphinstone's *Precedents In Conveyancing* (14th ed. Sweet & Maxwell, London, 1940) Vol. 2, 209 for a similar interpretation of that case.
22 Supra. n. 3, 430.
23 Ibid. 431.
24 Supra n. 15.
25 [1962] Ch. 964.

terms that he was dealing not only with the right to cast the vote but also with the question of effective control, it is submitted that that was placed beyond any real doubt by his application of the general principle to the facts of the case before him.

The argument of counsel for the mortgagor company in *Siemens Brothers & Co. Limited* v. *Burns*[26] on this matter appears to have been formulated on the assumption that the law was as it was subsequently expounded in the case by Swinfen Eady M. R. Obviously, if the general rule of law was that the mortgagor might control the mortgagee's votes that would have constituted the logical starting point of his case rather than the less forceful argument based on the reservation to the mortgagor company of the power to carry on its business until default.

Likewise if the general position had been otherwise than here suggested it would have been unnecessary for the mortgagor in *Puddephatt* v. *Leith*[27] to place any reliance on the mortgagee's written undertaking which was required to be proved as a collateral agreement.

(b) The parties to a legal mortgage may by agreement provide for the voting rights to be controlled by the mortgagor. Such an exception to the general rule is consistent with principle as well as the authorities which establish that, subject to adequate proof, the agreement will be upheld inter partes. Unless there is also some agreement as to the mortgagee providing a proxy the rights of the mortgagor are of necessity in the nature of control by direction to his mortgagee, rather than by voting at the meetings of the company.

(c) It is submitted that it follows from proposition (b) above that the equitable mortgagee who is not on the register may control the mortgagor's exercise of the voting power in respect of the mortgaged shares where there is express agreement, either in the mortgage deed or a collateral contract, permitting him to do so.

(d) Whether, in the absence of such express agreement, the equitable mortgagee may expect the court to uphold any right in him to control the voting of the mortgagor who remains on the register is not so clear. Certainly if consistency in regard to beneficial interest were the sole criterion, he might reasonably do so because the interests of the mortgagor were so clearly subjugated to those of the mortgagee in the legal mortgage context in *Siemens Brothers & Co. Limited* v. *Burns*.[28]

Also the two authoritative text-books, *Coote* and *Key & Elphinstone,* both suggest that the mortgagee does have that right. *Wise* v. *Lansdell*[29] which is cited as authority by both provides some support but unfortunately the judgment of Astbury J. is not without its difficulties:

(i) The defence argument that the mortgagees had no right to vote because they were not on the register was not specifically dealt with in the judg-

26 Supra n. 15.
27 Supra n. 18.
28 Supra n. 15.
29 Supra n. 3.

ment. Astbury J.'s statement that "Wise himself before his bankruptcy had the right to vote beneficially in respect of his shares. The right to place himself in a position to exercise that voting power, subject to the rights of the mortgagees passed to the trustees . . . " on his adjudication left that issue unresolved.

(ii) There is no definitive exposition of any right of control vested in the mortgagees. The first extract cited above[30] implies that such a right exists but does not say as much.

(iii) The judgment is in some respects equivocal. The reference in the judgment[31] to the willingness of the mortgagor to act at the mortgagees' direction prima facie suggests that the mortgagor may have had some choice in the matter and that he was not under a binding obligation to vote which would be correlative to any right of control in the mortgagee. This criticism may however be more apparent than real for it is suggested that it is an equally acceptable construction of that part of the judgment that Astbury J. was addressing himself not to the right-duty relationship but to the best method of enforcement of the mortgagees' right which was otherwise assumed.

(iv) Because at the relevant time the mortgagor, by reason of his bankruptcy and the disclaimer by his trustee in bankruptcy, really had no beneficial interest in the shares it is arguable that the judgment does not go so far as the two text writers suggest.

This last criticism of the judgment in *Wise* v. *Lansdell*[32] was taken up in argument by counsel for the plaintiff in *Musselwhite* v. *Musselwhite*[33]. Russell J. in the latter case, confined himself to a consideration of the position of a legal mortgagee who was on the register saying that for the purpose of reaching a decision on the rights of an unregistered transferee it was unnecessary to discuss the implications of Astbury J.'s judgment. Although his description of the earlier case as one[34]

> where the mortgagor was in fact on the register, a bankrupt, whose trustee had disclaimed any interest in the shares, and who was entitled to exercise voting powers, *though at the direction of the mortgagee*

may perhaps be construed as an acknowledgment of some general right of the equitable mortgagee to control the voting of the mortgagor, his comments in that regard were made without the benefit of full consideration and may be construed alternatively as being confined to the circumstances prevailing in the former case.

Casey J. made the same criticism of *Wise* v. *Lansdell*[35] in his judgment in *Cumulative Finance Company Limited* v. *Robertson*[36] given in respect of inter-

30 See extract quoted supra n. 22.
31 Supra n. 23.
32 Supra n. 3.
33 Supra n. 25, 970.
34 Ibid. 984; emphasis added.
35 Supra n. 3.
36 Unreported. Supreme Court, Christchurch Registry, 23 May 1979, A.152/78, A.176/78 and A.194/78.

locutory proceedings brought by the company and certain of its directors for injunctions preventing the defendant shareholder from, inter alia, voting at a general meeting of the company. In brief, the plaintiffs' claim to control the defendant's vote was based upon a lien claimed by the company over the defendant's shares.

Casey, J. took the view that *Wise* v. *Lansdell*[37] could not be regarded as authority for any general proposition that the holder of a lien or other charge (such as an equitable mortgage) over shares had the right to direct how the registered owner should vote. He concluded that[38]

> At best, it establishes a right to control his vote only where the whole beneficial interest in the shares is vested in the person claiming such a right.

That conclusion, it is suggested, is to be preferred to the statements of the two text writers for two compelling reasons. First, the absence of any personal interest of the mortgagor Wise, after his bankruptcy and the disclaimer by his trustee, placed him in a position more closely analagous to that of the bare trustee than that of the solvent mortgagor, a factor which inevitably detracts from the strength of any general statements in *Wise* v. *Lansdell*.[39] The court in that case was therefore not required to balance any conflicting beneficial interests in the shares. Secondly, it seems to accord more closely to the general principles of company law as to voting.

It is submitted then, that in the absence of any agreement or provision in the articles to the contrary, the equitable mortgagee of shares in New Zealand may not as a general rule control the manner in which the mortgagor exercises the voting rights on those shares. In the exceptional situation where the mortgagor has no beneficial interest in those shares the mortgagee may, it seems, direct the mortgagor how to vote provided the whole beneficial interest in the shares is vested in the mortgagee. Even then, in the absence of such directions, it is suggested that the mortgagor's only obligation in exercising the voting rights on the mortgaged shares, is to ensure that the value of the shares is not fraudently undermined to the detriment of the mortgagee's security.

D. Unregistered Transfers

Until an appropriate instrument of transfer is registered by the company the transaction affecting the shares in question remains incomplete and the legal title to the shares remains in the transferor.[40]

In the meantime, the transferee will have acquired some or all of the beneficial interest in those shares and will understandably have an interest in the exercise of the voting rights. That interest will be most acute in four common situations. First, where there is delay on the part of the transferee or the company in completing registration. Secondly, the directors refuse to register the transfer under a

37 Supra n. 3.
38 At p. 12.
39 Supra n. 3.
40 *Smith* v. *Wellington Woollen Manufacturing Company (Limited)* (1888) 6 N.Z.L.R. 654, 658; *Re Copal Varnishing Co. Ltd* [1916-17] All E.R. 914, 917.

general discretion in that behalf contained in the company's articles of association.[41] Thirdly, where the company refuses registration because of non-compliance with pre-emptive provisions in the articles of association. A contract for sale and purchase of shares made in disregard of such provisions is not, ipso facto, a nullity inter partes and may be enforceable not only at the suit of, but also against, the vendor, at least where consideration for the purchase has passed.[42] Fourthly, where the legal title to the shares is retained by an unpaid or partly paid vendor pending receipt of the full purchase price.

The voting rights of a purchaser whose transfer had not been registered by the company were first subjected to detailed examination in *Musselwhite* v. *Musselwhite*.[43] Certain shares in a small private company had been sold to the remaining director-shareholders under a long term agreement for sale and purchase. The purchase price was payable by a lump sum deposit with the balance payable by instalments over the ensuing five years. The vendors remained on the company's register of members as the holders of the shares which were subject to the agreement and at the time when the dispute arose all current instalments under the agreement had been duly paid and only approximately one third of the original purchase price remained outstanding.

This litigation arose out of an annual general meeting purported to be held by the company without notice being given to the vendors — an omission resulting from the directors of the company being under the erroneous impression that having executed transfers in respect of the shares the vendors were no longer members of the company. The vendors sought to have the meeting declared invalid and to have certain other related matters rectified.

Russell J., having noted[44] that counsel had been unable to find any authority on the point at issue, summarised the arguments in the following manner. At one extreme the purchasers, in defence of the defective meeting and their submission that a new meeting would serve no useful purpose, argued that the vendors in exercising their voting rights at any general meeting of the company would by virtue of the beneficial ownership of the purchasers be bound to comply with the directions of the purchasers with only one exception. The exception conceded was any voting direction which would fraudulently deprive the vendors of, or undermine the value of, the vendor's lien. At the other extreme the vendors contended that unpaid or partly paid vendors were not in the position of trustees for the purchasers, who must obey their instructions, and that they remained entitled to exercise the voting and ancilliary powers as they wished without necessary reference to the purchasers; though they would be liable to the purchasers if they took, or threatened to take, action damaging to the subject matter of the purchase.

41 E.g. article 24 Table A; *Stevenson* v. *Wilson* (1907) S.C. 445.

42 *Lyle & Scott Ltd* v. *Scotts Trustees* [1959] A.C. 763; *Hawks* v. *McArthur* [1951] 1 All E.R. 22; *Gold* v. *Penney* [1960] N.Z.L.R. 1032.

43 Supra n. 25.

44 Supra n. 25, 981.

Adopting a reference by Jessel M. R. in *Lysaght* v. *Edwards*[45] to an analogy between a mortgagee and an unpaid vendor, Russell J. decided, that in relation to a specifically enforceable contract for the sale of shares, similar considerations applied. After reviewing the authorities on legal mortgages he said:[46]

> In my judgment, so far as voting powers are concerned, an unpaid vendor remaining on the register is not to be regarded as in a weaker position, so far as the exercise of voting powers is concerned, than a mortgagee. The purchaser acquires the beneficial interest subject to the vendor's lien: the mortgagor retains the beneficial interest subject to the charge in favour of the mortgagee, in the form of an equity of redemption. In the one case the mortgagee is deliberately put on the register to safeguard his money lent; in the other case the vendor is deliberately left on the register until all is paid to safeguard his purchase-money due.
>
> In my judgment an unpaid vendor of shares remaining on the register after the contract for sale retains vis-à-vis the purchaser the prima facie right to vote in respect of those shares.

When that rule was applied to the facts of the case it became apparent that the vendor was entitled to complain of the defect in the purported annual general meeting.

One case that was not referred to either in argument before the court or in the judgment of Russell, J. is *Evans* v. *Wood*.[47] It was not entirely relevant to the question raised in *Musselwhite* v. *Musselwhite*[48] because full consideration for the shares had passed and there were in any event a number of special facts, but it does warrant consideration here.

The plaintiff vendor sought a declaration that the sale was valid and complete in equity and a further order that the defendant should reimburse the vendor for a call he had paid and indemnify him against all future calls and liability. The value of this case for present purposes lies in a brief obiter dictum and the form of the order subsequently made by the court.

Lord Romilly, M. R. held that the vendor was entitled to a decree against the purchaser and at the end of his judgment, almost in passing, he added: "Of course the plaintiff must act in respect of the shares exactly as the defendant may desire."

The order, after declaring the defendant's duty to re-imburse and indemnify the plaintiff, proceeds: "Order that the plaintiff do, in all things relating to the said shares, act as the defendant shall reasonably direct, and as if, the plaintiff were a trustee for the defendant of the shares."[49]

No other case in which the purchaser's position in respect of the voting rights on shares contained in an unregistered transfer has been examined has been located. Nevertheless the following propositions, based on the above two cases and

45 (1876) 2 Ch. D. 499, 505.
46 Supra n. 25, 987.
47 (1867) L.R. 5 Eq. 9.
48 Supra n. 25.
49 See Minutes on p. 16.

general principles, are submitted as a correct statement of the law in England which, it is submitted, will also be applicable in New Zealand.

(a) Where full consideration for the purchase has passed the vendor must comply with the directions of the purchaser.[50] That seems only logical as the vendor's position is analagous, if not identical to that of the bare trustee. That fully paid vendors remaining on the register do so as bare trustees was suggested by Russell J. in *Musselwhite* v. *Musselwhite*[51] and was raised but not completely answered in the course of the judgment in *Hawks* v. *McArthur*.[52] In the latter case Vaisey J. reasoned that as it was a basic principle that a charging order only operates to charge the beneficial interest of the person against whom the order is made it was not possible to obtain an effective charging order over shares where the person against whom the order is made holds them as a bare trustee. His conclusion unfortunately does not go the whole way in establishing that a fully paid vendor is in truth a bare trustee. His finding was simply that the equitable rights of the purchasers prevailed over any rights obtained by the plaintiff under the charging order.

It is suggested that whether such vendor is a bare trustee, or not, is not really important because it is clear that, since his position is so closely analagous to that of the bare trustee his obligations in respect of voting may be safely regarded as the same.

(b) As a general rule in the case of a partly paid or unpaid vendor of shares who remains on the register the purchaser has no prima facie right by direction or otherwise to control the vendor's vote in respect of the shares subject to the sale.[53]

(c) It seems that the unpaid or partly paid vendor may not exercise his voting power so as to damage the subject matter of the purchase. In the event of his doing so it is reasonably clear that the court would intervene to provide some form of restitution to the purchaser.

III. CONCLUSIONS

Such general principles as may be deduced from the authorities and the legislation relating to the rights of the holder of the beneficial interest have been stated at the end of each section of the preceding Part of this paper and need not be repeated here. However, certain other factors, which have been revealed by this paper, must be mentioned in order to ensure a complete overview of the nature of those rights.

(a) Conflicting interests

It is observed that the cases may be divided into two main categories according to the nature of the competing interests with which the courts have been concerned.

50 *Evans* v. *Wood*, supra n. 47.
51 Supra n. 25, 980.
52 Supra n. 42, 25.
53 *Musselwhite* v. *Musselwhite*, supra n. 25.

First, there are those cases where there is a true conflict of interest between the registered holder of the shares and some other person or persons having a beneficial interest therein. Such conflict arises only in the cases of the mortgage of shares (whether legal or equitable) where moneys remain outstanding and of the unpaid or partly paid vendor of shares who remains on the register pending full payment of the purchase price. Both parties to each of those transactions have some beneficial interest in the shares; a factor which perhaps explains the willingness of the court to apply the rules in respect of one by analogy to the other.

The second category, where there is no conflict of interest between the registered holder and the beneficial owners, is illustrated by the special trust and, it seems, the bare trust where there are a number of beneficiaries who are not ad idem. The conflict in those cases arises out of the competing beneficial interests of the cestuis que trust.

There remains to be noted a residual group of cases where no conflict of interest exists. This group is exemplified by the bare trust for a single beneficiary or for a multiplicity of beneficiaries who are in unanimous agreement but is not confined to the trust in the strict sense. Also falling into this category are the cases of the fully paid vendor and, by analogy, the repaid legal mortgagee, who remain on the register pending registration by the company of the instrument of transfer.

(b) The nature of the rights

With one exception, the rights sustained by the authorities are rights to direct or control the voting of the registered shareholder. No right to cast a vote at a meeting of the company has been ascribed to the beneficial owner who is not on the register. An important consequence of this is that once the vote has been cast by the registered holder the enforcement of the beneficial owner's rights presents practical difficulties because the decision of the company will have been made. Once the resolution has been acted upon direct recourse against the company will in general terms be unavailable, although the appropriate result may be achieved indirectly[54] or the registered holder may in appropriate cases be sued for breach of duty.

The exception is the assignee in bankruptcy who for the purposes of this paper has been regarded as the beneficial owner of the shares and whose voting rights are regulated by statute.[55]

(c) The authorities

The cases in which the rights of the beneficial owner in regard to voting have arisen directly are not numerous. This may be an indication that the law is

54 E.g. *Hill and Others* v. *Permanent Trustee Company Limited and Others* (1933) 33 S.R. (N.S.W.) 527 regularising result of a trustee's exercise of discretion based on a mistake of law. See also *Re Davis* [1961] N.Z.L.R. 597; *Musselwhite* v. *Musselwhite* (supra n. 25) ordering a new annual general meeting.

55 Companies Act 1955, s. 85(2).

accepted as well settled and beyond doubt, but more probably it is because the question of voting and control is generally ancillary to the main issue in dispute.[56]

Furthermore, with the notable exception of one judgment of the English Court of Appeal in respect of a special trust[57] few conflicts in the respective groups of authorities have been unearthed.

In the absence of relevant precedent the courts have tended to work from general principles and the decisions reflect a parallel development in other areas of the law. The principles applicable to the unpaid or partly paid vendor afford an illustration of this because in general terms it has long since been established that an unpaid vendor is not a bare trustee, that until payment is made he retains a personal and substantial interest in the property, a right to protect that interest, an active right to assert it if anything in derogation of it should be done, and that any fiduciary relationship is subject to the vendor's paramount right to protect his own interest.[58] Significantly both formulations by the opposing counsel in *Musselwhite* v. *Musselwhite*[59] conceded that there remained in the other party a right of control as an exception in respect of action which might damage or otherwise threaten the value of the shares. Notwithstanding the lack of any decision on this exception it is suggested that there is ample authority in the law relating to sale and purchase generally to enable the court when necessary to develop appropriate rules. For example, an unpaid vendor of realty is bound to take reasonable care that the property does not deteriorate between the date of the contract and the time when possession is delivered to the purchaser. He must act in regard to the property as a provident beneficial owner, and it is clear that he must neither damage it himself nor permit some other person to do so.[60] The extension of such a principle to the unpaid or partly paid vendor of shares appears to face no real impediment.

On balance it is considered that the courts have reached a satisfactory conclusion on most disputes that have come before them. Indeed the general propositions elucidated by them appear to be based as much on common sense as upon first principles and analagous existing rules.

56 E.g. The special trust cases on capital and income: (1980) 10 V.U.W.L.R. 271-275.

57 *Butt* v. *Kelson* [1952] 1 Ch. 197.

58 *Shaw* v. *Foster* (1872) L.R. 5 H.L. 321; *In Re Stucley. Stucley* v. *Kekewich* [1906] 1 Ch. 67; *Allen* v. *Inland Revenue Commissioners* [1914] 1 K.B. 327; *Raffety* v. *Schofield* [1897] 1 Ch. 937.

59 Supra n. 25, 980.

60 *Clarke* v. *Ramuz* [1891] 2 Q.B. 456; followed in *Phillips* v. *Lamdin* [1949] 2 K.B. 33.