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Corporate governance : remedying and ratifying directors' breaches

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CORPORATE GOVERNANCE: REMEDYING AND RATIFYING DIRECTORS' BREACHES

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1. Introduction

Directors are being subjected to increasingly intense scrutiny. The reasons are not hard to divine. Companies contribute enormously to the economic and social well-being of our society. Their pervasiveness is such that few individuals are left untouched by their activities. The inference is that better managed companies will produce benefits for all—hence the focus on directors. The past ten years have seen publication of the Cadbury, Greenbury and Hampel Reports. The Law Commission has released a report on company directors.[1] The DTI, in expansive mode, has announced a comprehensive review of the whole of company law.[2]

If the common aim is to raise the standard of conduct of company directors, then the law seems to have open to it four broad routes: compelling disclosure of directors' activities; introducing more demanding legal duties; imposing onerous remedies for breach; and restricting the power to exonerate defaulting directors. To date reform proposals have focused on the first two avenues. This article focuses on the last two. It is stimulated by the view that all four aspects are integral to the effective functioning of the law. The potential for exculpation (commonly referred to as "ratification") and the detailed remedial consequences of a breach of directors' duties remain poorly appreciated.[3] Left untreated, this is a recipe for inadequate or inefficient law reform.

In the corporate governance arena, the benefits of compulsory disclosure and imposing onerous legal duties, are widely accepted. Instinctively we appreciate that if we compel full and formal disclosure by directors of their various activities and functions, then we are likely to minimise the occurrence of breaches. The fear of discovery is a powerful motivator. Moreover, any breaches which do occur are more likely to be pursued and remedied. If close supervision by independent monitors (*e.g.* by non-executive directors, and perhaps also by powerful institutional shareholders) is added to this disclosure regime, then the risk of breach is likely to fall still further. Even more than this, compulsory disclosure is likely to inspire "good" behaviour, not just deter the bad. These simple ideas underpin much of the input of corporate governance reformers this decade.[4]

When deterrence fails, the focus turns to what will count—or what should count—as a breach of duty. Even if the aim is to improve overall standards of corporate governance, we understand that different rules are appropriate in different contexts. In areas considered vital to the effective operation of companies, high standards may be imposed with little opportunity for relaxation. In intermediate areas, high standards may be demanded as default rules, but with ready provision for simple opt-out agreements. In the least important areas, a low standard may be all that is required as a matter of course, but the parties may be left free to negotiate for something more demanding if they wish. All of this is now routinely rationalised on the basis of economic analysis and the increased efficiency which might be achieved by reducing transaction costs. However, long before this form of rationalisation became popular, directors were familiar with regulation by these different rule forms.

Less attention has been paid to the motivating force of legal sanctions. The law can provide further disincentives to breach by imposing differential remedies on defaulting directors. In the area of corporate governance, the remedies available to a company are usually compensatory.[5] A remedy which requires the director to compensate the company for any loss obliges the director, not the company, to bear the risks associated with any breach. A seemingly minor breach may expose the defaulting director to a substantial damages claim. But this is not always the approach. With certain breaches, the defaulting director may be required to disgorge all the profits of the breach. It is difficult to predict the deterrent effect of this. On the one hand, the director's risk is confined to losing the fruits of the wrongful venture. This may be little deterrent when set against the chance (however slim) of making huge undiscovered gains. On the other hand, the company's incentive to detect and pursue such claims is high. This form of remedy can enable companies to claim windfall profits which the company may never have gained from its own activities.

Finally, the law's impact can be modified by the possibility of exoneration. Whatever the breach or its potential remedial consequences, the company may have freedom to determine whether or not to pursue its claim. The law's deterrent effect is enhanced if it is difficult for the company to effectively exonerate its defaulting directors. The rules on "ratification" suggest that there are limits, albeit uncertain ones, circumscribing the company's right to allow defaulting directors to go free. The uncertainties stem from difficulties in integrating the general law rules on exoneration with the company law principles of perpetual succession and majority rule. The law has to determine not only *whether* a company may exonerate its defaulting director, but also *how* that exoneration must be effected if it is to bind dissenting shareholders and future controllers of the company. To date little attention has been paid to this aspect of corporate governance.

This article focuses exclusively on the interplay between directors and the companies they manage. Its primary concern is not with the content of the duties owed by directors (unlike the most recent Law Commission and the DTI reviews). Rather it is with whether the company is entitled to relax the scope and content of these duties, whether it can forgive or excuse a defaulting director, whether it can adopt impugned transactions, and what remedial consequences follow a breach. The aims are twofold. The first is to map the general territory, so that future reform proposals can be better judged against the existing backdrop of corporate governance regulation. Here the results are not simply descriptive: difficult duty and remedy distinctions are at stake. The second aim is more ambitious. Companies are independent legal entities, yet they can only act through corporate organs comprised of human agents. Unanimity in decision-making is not essential. Predictably, individual dissenters have sought to override the majority, urging that their personal rights have been infringed or that derivative action is warranted. The result is a confused and confusing body of rules. This article advances what seems to be a simple and workable analytical approach to corporate decision-making—especially in relation to the difficult issues of ratification and exoneration—and the interplay with the Companies Act 1985 section 14 contract and the rule in *Foss v. Harbottle*.[6]

2. Differentiating between different directors' duties

Directors are subject to various duties, both common law and statutory. At a very fundamental level, these duties are directed at four well-defined objectives: to compel directors to act in accordance with the strict terms of their mandate; to compel them to exercise care and skill in carrying out their various functions; to compel them to use their wide discretionary powers in good faith and for proper purposes; and, finally, to compel them to act loyally in advancing the interests of their company.

It is important to recognise these different categories of duties and to be rigorous in differentiating between them. Proof of breach depends upon different factors, especially as regards the director's state of mind or intention. The potential defendants are different. So too are the potential remedies. In the realm of directors' duties, such strict categorisation has traditionally been uncommon. The language of fiduciaries has been seductive. At its worst, it has sometimes engendered the assumption that any breach of obligation by a director is a breach of fiduciary obligation. The carelessly accepted inference is then that superior ("fiduciary") remedies are automatically available. At least where the common law is concerned, such loose usage is now explicitly decried: a negligent director, for example, commits a tort, not a breach of fiduciary obligation; an obligation to perform a contractual undertaking honestly and conscientiously does not imply that the obligation is fiduciary. The related recognition that not all breaches of directors' equitable obligations are breaches of fiduciary obligation seems later in coming. True, such terminology is a matter of choice, but there are underlying "fiduciary" and "non-fiduciary" distinctions which need explicit recognition: somehow we need to differentiate between fiduciary obligations of loyalty (i.e. obligations demanding self-denial), equitable obligations of confidence (which are not breaches of fiduciary obligation) and equitable obligations to exercise powers in good faith and for proper purposes.[7] This article makes those distinctions.

But this approach is not the only one. Such distinctions are in contrast with the general approach of the Companies Act 1985 Part X.[8] The statutory regime provides for a wide-ranging remedial menu (rescission of the underlying transaction, compensation for any corporate losses, disgorgement of any gains made from the breach) to be available to the company against a variety of potential defendants (the perpetrators of the impugned transaction, any directors who received a benefit, and any connected persons). Before embracing this approach as the appropriate general model in the corporate governance field, we need to be sure that it delivers the social and economic motivations, incentives and consequences that we intend. On the whole the common law's more discriminating approach seems preferable: rigorous classification assists us to treat like cases alike and so to deliver justice in different circumstances; it is also important because it recognises that the different obligations imposed on directors are designed to achieve different ends, and that those different ends are best achieved by the imposition of different sanctions; finally, it is less likely to lead to inappropriate generalisations when "ratification" (using the term in the widest possible sense) becomes an issue. In short, the differential approach allows for the minimum degree of legal intervention necessary to achieve the ends desired.

3. Corporate decision-making in relation to directors' duties

Before addressing the specifics of the particular duties imposed on directors, it is useful to consider some of the general features of corporate decision-making. In the context of this article, the issue for the company will be whether particular duties owed by directors can be relaxed or waived; whether impugned transactions can be ratified (*i.e.* either adopted[9] or affirmed[10]) so as to bind the company to a third party in contract; or whether the defaulting directors can be exonerated (or forgiven) for their breaches.

The cases present a confused picture. Frequently the appropriate decision-making organ in all these instances is simply assumed to be the general meeting. "Ratification" is used as an umbrella term regardless of the real decision being made. Finally, there is often little attempt at rigorous analysis of the decision-making process itself. As a consequence, there is uncertainty about whether the "decision" binds the company (including a subsequently appointed board of directors or liquidator), or only its dissenting minority shareholders (thus preventing a derivative action).[11]

The issues ought not to be so complicated. The real concern is always whether the *company* is bound by a decision which must necessarily be made by a company organ (be it the board of directors, or the general meeting, or even some individual within the corporate hierarchy). In particular, in the context of this article, the concern is whether the company has effectively waived or varied the duties owed to it by its directors, so that it cannot later demand some higher standard of conduct; or whether the company has effectively adopted or affirmed an unauthorised or voidable contract so as to make it binding on the company (or has perhaps done the reverse, so as to ensure that the contract is not adopted, or is avoided); or whether the company has effectively released its claims against certain directors for past breaches of duty, so that it is bound by its decision not to sue them. If the company has *effectively* made any of these decisions, then the company is bound by that state of affairs: a new board of directors, or a liquidator appointed to the company, cannot go back on the decision.[12]

Moreover, a dissenting minority of shareholders cannot pursue a derivative action in defiance of an effective decision by a corporate organ: derivative actions are premised on the company having a legitimate claim to some remedy. If there is a effective company decision to release a claim, or vary obligations, or ratify a dealing, then that is the end of the matter. Most derivative actions are therefore concerned to establish that any purported decision was not (or would not be) effective to bind the company. Nor can a dissenting shareholder pursue a personal action (alleging breach of the Companies Act 1985 s 14 contract) in defiance of an effective decision by a corporate organ. The principle of majority rule ensures that.[13]

The crucial issue is clear, then: what constitutes an effective and binding corporate decision? The thesis advanced here is that, for each decision, there are only three question to be answered. First, does the company have the *capacity* to make the decision? Secondly, does the relevant corporate organ (often the general meeting) have the *authority* to make the decision? And, finally, has that authority been *properly* exercised?[14] These questions are listed in their logical order, but also in order of increasing difficulty. Each question must be answered in the affirmative if a decision is to be binding on the company.[15]

Much of the existing case law can be seen as directed at answering one or other of these three questions. However, many of the difficulties and inconsistencies in the case law have arisen because the issues have usually been addressed only in isolated contexts—first, in concerns about "personal rights" and the proper ambit of the s 14 contract; secondly, in the reach of the exhortation that the general meeting must act "bona fide and in the interests of the company" in the context of the effectiveness of (usually) a special resolution; and, finally, in the meaning of "fraud on the minority" in the context of derivative actions. The result has been akin to having several teams tunnelling through a mountain from different directions. The work of one team is not necessarily recognised—or taken advantage of—by another. In reality, all these categories of cases are directed at establishing whether or not a purported exercise of power by a corporate organ (often the general meeting) is effective to bind the *company* to the decision made.[16]

3.1 Corporate capacity

Consider first the *capacity* of the company to make the decision. In general terms, a company's capacity may be limited by the general law (which, as with individuals, makes certain dealings illegal), the Companies Act 1985, and the company's own memorandum and articles. In the context of decisions to vary directors' duties, or to waive, ratify or exonerate breaches, any decision which purports to run counter to these restrictions will be void.[17] It is irrelevant which corporate organ makes the decision, or how great the voting majority in favour, or how bona fide the motivations of the actors. Several statutory provisions illustrate the potential impact of corporate capacity in limiting the company's dealings with its directors.[18]

3.2 Authority of the corporate organ

Matters are a little more complicated when it comes to considering the *authority* of a corporate organ to make the particular decision in issue. If the corporate organ lacks authority to waive, vary, ratify or exonerate, then any purported decision it takes will be void and of no effect.[19] The company will not be bound by the decision, and an individual shareholder may[20] be able to pursue a derivative action, either to prevent the company acting on the decision or to remedy any action already taken in accordance with the decision.

Deciding whether a corporate organ has the necessary authority is not always easy. Occasionally the Companies Act 1985 or the company's constitution will make it clear that a decision can *only* be taken by one organ, the general meeting for example, either by ordinary resolution or by special resolution.[21] More often the issue is a matter of subtle interpretation. Consider the case where the articles reserve certain decisions to a particular organ. This could be interpreted as leaving the general meeting (or any alternative corporate organ) with no power to ratify dealings taken in defiance of the constraints (here using ratification in its usual agency sense).[22] But more usually such restrictions are regarded as leaving the general meeting with power to ratify on the company's behalf.[23] These are hard cases. In the final analysis the courts seem to adopt an intuitive sense of the precise form of protection being sought by the provision in the company's constitution, and then to pursue a purposive interpretation of the restriction so as to deliver that protection as far as is possible.

In *Quin & Axtens v. Salmon*,[24] for example, a power of veto given to an individual director would have had little protective force in determining corporate direction if the general meeting could override its effect by an ordinary resolution ratifying the board of directors' unauthorised acts.[25] On the other hand, in *Grant v. United Kingdom Switchback Railways Co.*[26] the protection derived from provisions denying interested directors the right to vote would not be abrogated by allowing the general meeting the authority to ratify the board of directors' unauthorised (self-interested) acts.[27] In each of these cases the protective provisions were directed at the company itself. This is not always the case. Sometimes the protection is directed at individual shareholders. There too, the process of interpreting the relevant provisions—to see whether the general meeting has power to ratify an otherwise unauthorised proposal—seems to follow the same rather intuitive path.[28] These difficult distinctions lie at the heart of the confused area of personal rights and the section 14 contract.

Even without these difficulties in interpreting the company's constitution, it is not easy to decide which corporate organ has the necessary authority to act. Since the board of directors usually has general powers of management of the company, it might be supposed that the board has the authority to make most (but not all) of the decisions which are the concern of this article[29]—subject of course to the usual rules which apply when the board is resolving issues in which board members have a personal interest.[30] But the cases suggest otherwise. They suggest that the general meeting has exclusive (not merely concurrent) authority. This issue is taken up later; it seems to rest on historical accident rather than on sound theoretical foundations.

3.3 The 'proper' exercise of authority by a corporate organ

The final issue is whether the exercise of authority by the corporate organ is *proper*. This is the most difficult and controversial limitation, especially as it applies to exercises of power by the general meeting. Nevertheless, this form of equitable restriction, which requires powers to be exercised bona fide and for proper purposes, has a long history of wide-ranging applications. This restriction controls the exercise of all discretionary powers intended to bind dissenting minorities.[31] As long ago as 1758, Lord Northington in *Aleyn v. Belchier*[32] asserted: "No point is better established than that, a person having a power, must exercise it bona fide for the end designed, otherwise it is corrupt and void."[33] It is a central part of the thesis advanced here that a decision will not be effective to bind the company unless it is taken bona fide and for proper purposes. A decision taken for private advantage or for some other purpose foreign to the power can be impugned. Moreover, this is true regardless of the corporate organ taking the decision. However, the possibility that this form of equitable limitation applies to restrict the voting power of the general meeting has been the subject of much controversy.

On the one hand, any limitation on a shareholder's voting power is seen to be an inconsistent and therefore unacceptable infringement of the property rights inherent in share ownership.[34] The existence of any constraints is therefore denied. On this approach, a general meeting resolution might be effective notwithstanding that the majority of shareholders may have a personal interest in the outcome inimical to the interests of the company.[35] In particular, directors—by exercising their votes as shareholders—may be in a position to ensure that they are not required to remedy their defaults. This possibility has led to some plainly unsatisfactory attempts to deny the logical consequences of this approach. The propriety of the voting exercise is left unexamined, but it is said that the corporate organ (the general meeting) lacks the necessary authority to excuse the directors because certain wrongs (although not all wrongs) committed by directors are simply "unratifiable".[36] The impossibility, and the undesirability, of relying on such distinctions is taken up later.

On the other hand, a general meeting resolution is—and is intended to be—binding on the company (and thus on dissenting shareholders). It follows that the shareholders' power to vote is a power to bind dissenting (or silent) minorities, and so it inevitably comes with the equitable limitation that its exercise is only effective if it is bona fide and for proper purposes. This is simply another way of saying that the exercise of power must not be beyond the scope of the power.[37] Given the fundamental principles which underpin the corporate constitution and the notion of corporate personality, the assertion that this form of equitable restriction has general application to decisions of the general meeting seems unanswerable, notwithstanding the continuing controversy.[38]

One common misconception needs to be laid to rest at the outset. This form of equitable restriction on exercise of power by the general meeting does not impose fiduciary obligations on shareholders. Shareholders are not required to put the interests of the company or the other shareholders *ahead* of their own, as a fiduciary would.[39] They may vote in their own interests in every case *except* where to do so would be to use their voting power to achieve ends (personal or otherwise) outside the scope of the power granted to them. This is the essence of the restriction. It is a "fraud on the power" to exercise the power for purposes "outside the fair scope of the social contract".[40] The limitation does not demand altruism. It simply denies any efficacy to this form of equitable fraud.[41]

It is true that the clearest precedents supporting this form of general equitable restriction on the voting power of the general meeting are not English. The development of the law in England has, it seems, been hampered by history. The early idea—now discredited—that the shareholders were the "owners" of the company, and therefore had individual rights to regulate the disposition of "their" assets, either directly or via "their" agents, the directors, continues to cloud the truth. The company is at law a separate person with its own assets. Those assets do not belong to the shareholders. Moreover, the directors are not the agents of the shareholders. For some reason—perhaps simply because we have difficulty with the notion of a non-human "person"—it seems to have been difficult to gain unqualified commitment to this idea. The theory that the company is an entity completely separate from its human organs is not always matched by the practice. In truth, the voting power of individual shareholders in general meeting serves two functions. It is a means by which certain corporate acts are carried out. It is also the means by which the relationship between individual shareholders is regulated. In both cases a majority of shareholders (sometimes an ordinary majority, sometimes a special majority) has the power to bind either the "voiceless" company or the "dissenting" minority of shareholders to some planned course of action. This discretionary power to set the course of action for another comes with equitable restrictions. Even if the English cases have not been rigorous in defining or describing these restrictions, they have certainly recognised their existence.[42]

Moreover, this recognition of an equitable "proper purposes" restriction is not confined to attempts by shareholder meetings to alter either the corporate constitution or the class rights attached to shares. It is evident, at least implicitly, in a wide range of circumstances. In validating an improper share issue by the board of directors, for example, the "new" shares cannot be voted.[43] This is not because the new shares do not carry the right to vote—their allotment is voidable at the instance of the company (and even then only as against knowing third party recipients); it is not void. Rather it is, it seems, because it is appropriate to assume that the power to vote would be exercised by these new shareholders simply (or substantially) in order to confer a personal benefit on themselves. The power to vote in these circumstances is not given for this "improper" purpose. Any general meeting confirmation tainted by such improper purposes would be ineffective as a corporate decision. To save head-counting, it is simpler if the shareholders who are (or would be deemed to be) motivated by improper purposes simply abstain from voting.[44]

There are other instances. Courts will intervene, and allow a derivative action, where the general meeting vote to commit the company to a particular course of action is (or would be) a “fraud on the minority”. What this usually means is that the vote is a “fraud on the company”. This, in turn, simply means a use of power inimical to the purposes for which the power was granted. It is judged by whether the power is used to deliver benefits to individual voters which were not contemplated in the grant of voting power: the power must only be used bona fide and in the interests of the company as a whole.[45] Moreover, in making this determination of whether the power was properly exercised, the courts are clearly “head-counting” to discover whether the vote was tainted by improper purposes. They are not simply excluding the wrongdoers from judging their own cause. This is evident from their approach to “wrongdoer control”—it is assumed that the wrongdoers have voted for improper purposes, *and* that so too have those who voted with the wrongdoers either out of apathy or because of their influence. Where the outcome of a vote has been delivered by “wrongdoer control”—so that the exercise of power by the corporate organ is for an improper purpose—the vote is not effective as a corporate decision. Depending on the way the issue arose, the company may then be in a position to pursue a remedy, either in its own name or via a derivative action.

The same idea underpins complaints when the general meeting voting power is used to bind dissenting shareholders to a new course of conduct, even where the altered course is potentially advantageous to the company. The majority shareholders are not allowed to use their power for purposes outside those contemplated in the grant. This seems a more intelligible way of expressing the principles at play in cases which assert that shareholders must act bona fide and in the interests of the shareholders as a body.[46]

In practice, any decision about whether the majority has abused its voting power in the general meeting turns on fairly crude tests. What counts as a “proper” purpose depends intimately on context—it depends upon the particular issue at stake. Individual voters are generally assumed to be voting for proper purposes. The contrary allegation is sustainable only where the irresistible inference is that their votes have been cast “as a means of securing some personal or particular gain, whether pecuniary or otherwise, which does not fairly arise out of the subjects dealt with by the power and is outside and even inconsistent with the contemplated objects of the power.”[47] Clearly this assessment involves difficult value judgements rather than reasoned legal analysis.[48] Where a general meeting resolution is carried only by counting the votes of those who can be shown (or deemed) to have abused their power, then the resolution is voidable.[49] However, where the exercise of power is proper (and effected by an organ with the necessary authority, and within corporate capacity), it operates as an effective and binding corporate decision. This means that it binds all of the company’s shareholders (including the dissenters), and any subsequent controllers (including any liquidator who might be appointed). These issues are taken up in more detail in the discussion which follows.

4. The duty to exercise care and skill

It is now possible to turn to the specific duties imposed on directors. First, directors are under a common law duty to exercise care and skill in the conduct of their management functions.[50] The scope of this duty has attracted a great deal of criticism from those who believe that the common law standard is too low to meet the demands of a modern competitive economy. The usual suggestion is that the combination of subjective and objective standards applied by the Insolvency Act 1986 s. 214 should be adopted generally.[51] This may be so, although it has also been suggested that the common law standard already parallels this formulation[52] and, moreover, that a general statutory provision would necessarily introduce difficulties which might prove insurmountable.[53] That debate, although important, falls outside the scope of this article.

Whatever one's views on the standard of care and skill demanded of directors, the duty is clearly regarded as so significant that companies are prohibited from relieving directors from its imposition.[54] Directors found to be in breach of this duty are liable in damages to compensate the company for any losses caused. The usual tort rules apply in assessing the quantum of damages, although the court has power to relieve in whole or in part directors who have acted "honestly and reasonably and . . . ought fairly to be excused".[55] In addition, just as any legal person can decide after the commission of a tort whether or not to sue the tortfeasor, it seems reasonable to suppose that a company too can elect whether to sue its defaulting directors. In short, although companies lack the capacity to waive the duty in advance, they are not compelled to sue for its breach after the event. Of course, since the common law rule is that a gratuitous release is not binding (unless given by deed), either consideration or proof of an estoppel may be necessary to ensure that the company cannot go back on its decision in the future.[56] Moreover, since directors are in a fiduciary relationship with the company, and since any release is obviously a dealing in which the director's personal interest is in conflict with his or her duty to the company, effective release is conditional on full disclosure being made by the director. The cases, however, suggest that the matter is neither so simple nor so clear-cut.

The first step in the analysis is not difficult: has the director committed a breach of duty? Although all directors owe a duty of care to their companies, it does not follow that directors are inevitably liable for every negligent management decision. Directors are only liable when it is *their* negligence which causes the company to embark on a losing venture. Given the management structure of most companies, this will often be the case. But it is not always so. If the company's decision to embark upon a particular venture is taken by a different corporate organ (such as the general meeting), and is taken without relying on the care and skill of the company's directors, then the company cannot afterwards sue its directors in negligence.[57] It follows that it is important to ask which corporate organ took the negligent decision: was it the directors (who owe a duty of care) or the shareholders (who do not, although they cannot act fraudulently or for improper purposes)? This distinction was, it seems, the basis upon which Lawton L.J. concluded that the defendant directors were not liable in negligence in *Multinational Gas and Petrochemical Co. Ltd v. Multinational Gas and Petrochemical Services Ltd*.[58] In adopting this analysis to show that directors are not liable in negligence, the critical issue is that the company's (negligent) management decision was not made by the directors, but by another corporate organ. Unanimity, or the size of the shareholder majority within that other organ, is irrelevant. Since the directors did not take the negligent decision, they cannot be sued in negligence.[59]

Where the directors *are* liable in negligence to the company, then it is important to know whether the company can legitimately decide not to sue, but to "waive" or "release" the breach. Since the board of directors has general powers of management of the company, it might be supposed—as noted earlier—that the board can decide whether to release its defaulting directors.[60] However, it is invariably assumed that this is a decision reserved to the general meeting. It is difficult to see why, unless, of course, the board of directors is unable to act because there are insufficient disinterested directors to constitute a quorum.[61] This query is a general one. It is not restricted to directors' duties of care and skill, but applies to other directors' duties too. Directors' duties are owed to the company. It is the company that ought to decide whether to pursue its claims. The power to do this generally resides in the board of directors. Certainly this is so when the company is deciding to *pursue* its claims, whether against the directors or against outsiders.[62] One would expect the position to be the same when the company is deciding to *release* its claims. The only credible explanation of the contrary position seems to be that it is the result of an historical accident, or, more accurately, a failure of the law in this area to keep pace with developments in the accepted principles underpinning company law. The board of directors was initially regarded as a mere agent of the company; it was expected to act in accordance with the directions of the general meeting, which was assumed to be the real repository of corporate power. On this view it is defensible to suppose that decisions about whether to sue defaulting directors should be reserved to the general meeting. Now, however, this agency theory is discredited. The company is a separate legal person. Its powers are exercised by human organs, certainly, but the repository of different powers is determined according to the terms of the corporate constitution. It ought to follow that, legally, the decision to sue the company's negligent directors—or not—ought to reside in the board of directors, not in the general meeting.[63]

The analytical difficulties do not end there. There are cases which suggest that it is *not* always possible for a company (regardless of the operative organ) to decide that it will not to sue its negligent directors. *Daniels v. Daniels*[64] is frequently cited as proof. That case is always contrasted with *Pavlides v. Jensen*,[65] where "ratification"—forgiveness of the defaulting directors—was deemed acceptable. In both cases the allegations of negligence rested on a gross undervaluation of property sold by the company. In both cases, therefore, the remedy for negligence would have required the defaulting directors to compensate the company for the losses suffered. But in *Daniels* the property was sold to one of the defaulting directors, and in *Pavlides* it was sold to an associated company. Accordingly, in *Daniels* the transaction also involved a breach of fiduciary duty by the director concerned. That difference—that there was self-serving negligence in the former case, but not in the latter—is routinely used to justify the difference in outcomes. Release in the former case is said to involve disposal of the company's assets, whereas release in the latter does not. The results in both cases may be right, but the reasoning is suspect. It warrants further comment.

Only a little reflection suggests that it is impossible to divide the actions available to a company into two classes, one where a release would be impermissible because it would involve disposing of the company' assets, and another where it would not. By definition a legal claim in the hands of the company is a valuable corporate asset and any release of it involves, effectively, giving away that asset to the potential defendant. In *Daniels*, if the company had been permitted to release its damages claim then the defaulting director would have been allowed to keep a large sum of money which she might otherwise have been required to pay out to the company; the company would, in effect, be making a gift of that sum to the director. But the situation in *Pavlides* cannot be distinguished. Release of the damages claim against the defaulting directors in that case also involved giving away corporate assets to the potential defendants.[66] It follows that distinctions drawn on the basis that certain wrongs are "ratifiable" while others are not will not withstand scrutiny.

Absent express restrictions, it is difficult to see why any company does not have the *capacity* to determine whether or not to sue its defaulting directors—or to pursue any other claim available to it. All legal actors have such capacity. Assuming that the general meeting is the appropriate organ authorised to exercise that capacity, then the final requirement for an effective corporate decision is that the election to release the company's claims must be taken *properly*—*i.e.* bona fide and for proper purposes. As already noted, this latter limitation is attached in equity to the exercise of any discretionary power where exercise of the power may result in dissenting minorities being bound by the decision. On this basis it might be legitimate to distinguish the decisions in *Daniels* and *Pavlides*. In *Daniels*, the defaulting director, with her husband, was a controlling member of the general meeting which allegedly determined the release from suit: the director was a judge in her own cause, and so the appearance of bias—improper purposes—is unanswerable. In *Pavlides*, on the other hand, although there might have been suspicion of bias, it was not accepted as properly proved; if the general meeting vote to release the directors was not impugned on the grounds of improper purposes (or "fraud on the minority"), then it stood as an effective exercise by the company of its power to determine whether or not to pursue claims available to it. It ought to follow that the same result might have obtained in *Daniels* if an independent majority of the general meeting had *properly* voted for the defaulting director's release—and there are certainly "proper" reasons why such a decision might be taken by a company.[67] The overtones of fiduciary breach by the director, discussed later, do not upset this conclusion.

In summary, a company cannot waive in advance the duties of care and skill it is owed by directors. However, after a proven breach—*any* type of negligent breach—the company ought to be free to decide whether or not to pursue its claims. Since any decision must necessarily be taken by a corporate organ, it must be taken properly if it is to be effective. This simply matches the analogous rights of individual legal persons, with the overlay that the power to take the decision on behalf of the company lies with the company's organs, not the company directly, and so is a power which comes subject to equitable limitations. None of this impinges on the issue of what standards of care and skill are (or should be) demanded, an issue which is equally the subject of controversy.

5. The duty to act in accordance with the terms of any mandate

The duty imposed on directors to act in accordance with the strict terms of the mandate given to them has now lost much of its commercial significance. Historically the duty was imposed by analogy with the trustee's duty of strict compliance with the terms of the trust deed.[68] In this context the company's memorandum and articles were seen as serving the same function as the terms of a trust deed. The duty is now less relevant because few corporate constitutions (or other documents) impose explicit limits on the capacity of companies or their directors, although the potential to do so remains. Any acts beyond the director's given authority[69] (and, by necessary implication, any acts beyond the company's stated capacity) are regarded as being in breach of the director's duty of strict compliance with the terms of the mandate. As with trustees, the defaulting director is then strictly liable to reinstate the lost assets.[70] The director's bona fides are irrelevant.[71] The company's claim is a personal claim for equitable compensation from the defaulting directors.[72] It is not a claim against the recipient of the corporate assets.[73] The "but for" causation test used to assess the extent of the loss attributable to the breach is fairly crude: the loss is assessed without regard for any mental element or any limitation based on foreseeability, although directors are permitted to prove that certain losses would have occurred in any event despite the breach.[74]

The company is free to relax the terms of the general mandate under which its directors act.[75] Sometimes this can be achieved quite simply by the board of directors altering the terms of a delegation of power to one of its number. At other times the process is quite demanding, requiring alteration of the company's constitution in accordance with the provisions of the Companies Act 1985. The authority to make changes and the appropriate process to be followed depend upon the terms of the original grant of power. Where the original grant of power is contained in the company's constitution, the fact that alteration frequently requires a special resolution of the general meeting indicates the rigour of the rule requiring strict compliance. This rigour is justified by a need to protect both the company's creditors and its equity holders. Moreover, even where the general meeting has the *authority* to make the decision to alter the mandate, the decision must be taken *properly*—*i.e.* bona fide and for proper purposes—if it is to be effective. Interestingly, in this context the equitable restriction on the general meeting's voting power is not controversial.[76]

If the company does not desire general relaxation, but only exoneration of its defaulting directors from a specific exercise or threatened exercise in excess of power, then the picture is slightly different. If the restriction on the directors' power arises because of the company's limited objects, then a special resolution is necessary for effective exoneration.[77] Otherwise an ordinary resolution will do.[78] This assumes that a company always has the *capacity* to exonerate its defaulting directors (*i.e.* release them from liability). It is difficult to see why it would not.[79] This is not the same as asserting that the company always has the capacity to ratify the impugned transaction—it does not.[80]

Releasing the directors from their potential liability is not the same as ratifying the impugned and unauthorised transaction. The issues of corporate capacity and general meeting authority (assuming this is the ratifying organ[81]) are less straightforward if the company wishes to ratify (*i.e.* adopt as its own) the impugned transaction. If the restriction on the directors' power arises because of the company's limited objects, then the Companies Act 1985 alters the common law to allow ratification, but only by a special resolution of the general meeting.[82] In other cases, the issues of capacity and authority need separate and rigorous consideration. Nothing can be assumed. Sometimes the company has the capacity and the general meeting (or other corporate organ) has the authority which is necessary to make ratification possible. At other times they do not.[83] For example, the general meeting cannot ratify (*i.e.* adopt as the company's act) any dealings which are illegal—although the general meeting can exonerate the defaulting director.[84] The problem is not a difficult one; it simply needs explicit recognition. In every case the same bona fide and proper purposes limitations apply to the vote to ratify. If the vote is to be fully effective, it must be within corporate capacity, authorised *and* properly taken. With ratification, this additional requirement is unlikely to be problematic unless the party to the unauthorised dealing with the company is in a position to influence the outcome of the vote of the general meeting, and needs the benefit of ratification to make the dealing binding.[85] The assumption may then be that the voting power was improperly used for personal advantage.[86]

If those setting up companies have in practice relinquished the control which this duty of strict compliance enabled them to exercise via the company's memorandum and articles, the legislature has not been so reticent. The Companies Act 1985 prohibits certain dealings and, following the common law model, it imposes obligations of strict liability on defaulting directors to make good any consequential losses suffered by the company. Many—although certainly not all—of these restrictions are to be found in the Companies Act 1985 Part X. Familiar examples include absolute prohibitions on the company paying dividends except out of distributable profits[87] (not a Part X restriction) and prohibitions on the company entering into most forms of loan or guarantee arrangements with its directors.[88] Other restrictions are not so strict. For example, certain substantial property transactions are prohibited only if they are not consented to by the general meeting.[89] Directors who implement any of these deals in breach of the statutory restrictions are strictly liable to make good any consequential losses suffered by the company.[90] Notably these statutory provisions also impose liability on other parties, especially on directors and other connected persons who are parties to the deal.[91] If a common law analogy is required for these additional remedial routes, it can most often be found in fiduciary law.[92]

To summarise, the common law position is quite simple: if a director disposes of corporate assets without authority, then he or she is strictly liable to compensate the company for the loss caused. The remedy is available against the defaulting director, not against the recipient of the corporate property. It is equitable compensation, calculated in the same way as is a trustee's duty to reinstate the trust fund after a misapplication. It is irrelevant that the defaulting director acted in good faith (liability is strict), or made no profit (the remedy is compensatory only), and if the director did make a profit, this route will not enable the company to recover it (although another might). The statutory restrictions are more complicated but, at least in their application to directors who instigate the unauthorised dealing, there are clear analogies with the general common law position. The complications arise because of the overlay of different liabilities imposed on different parties for their different roles in the impugned transaction.

6. The duty to use discretionary powers in good faith and for proper purposes

Directors must use their authority bona fide in the interests of the company and for proper purposes.[93] This limitation is often seen as comprised of two separate duties, the first requiring subjective honesty and the second imposing an objective limitation to "proper" purposes.[94] As already noted, this limitation is imposed in equity on all those who exercise discretionary powers intended to be binding on others. Directors may be in breach of the "proper purposes" aspect of the rule notwithstanding that they are acting honestly, carefully and from the best of motives, and have nothing to gain from their actions. This is well illustrated by the legal analysis commonly applied to directors' defensive tactics in the face of unwelcome takeover bids.[95]

With the law as it stands, it remains important to maintain the distinction between this duty (to act bona fide and for proper purposes) and the duty considered in the previous section (to act in accordance with the strict terms of the mandate). This is because breaches of the duties have different impacts on third parties dealing with the company and, perhaps, on the remedies available against the defaulting directors themselves.

Consider first the impact on third parties. A dealing entered into by the directors on behalf of the company, but for improper purposes, may nevertheless be an authorised dealing. An abuse of power does not negate the existence of the power.[96] If this is the case, the only third parties who will be affected by the breach are those who know of it,[97] and are therefore classed as third party constructive trustees taking subject to the equities, rather than as bona fide purchasers for value. An abuse of power is thus less likely to impact on third parties than an absence of power. If the third party does know of the abuse of power, then the transaction is voidable, not void (as it would be with absence of authority).[98]

In those rare instances where the transaction is voidable (because the third party knows of the abuse of power), then the election should, it seems, be one for the board of directors to take on behalf of the company.[99] However, as with the cases already discussed, the usual inference is that the general meeting should take the decision. Whichever organ acts, the election to *avoid* is subject to further equitable constraints, the principal and inherently limiting one being that the company must be in a position to effect *restitutio in integrum*.[100] In practice, a decision to *affirm* the transaction is more common. Either way, the election must be made bona fide and for proper purposes.[101] To take the familiar example, a company may wish to affirm an improper share issue in order to protect the favoured takeover bidder who is probably aware of the breach. It is possible for the company, via its general meeting, to take this decision for quite proper purposes, but clearly the self-aggrandisement of the bidder is not a "proper purpose". This is the basis of the "rule" that excludes the holders of the newly issued shares from voting to ratify or affirm the voidable allotment: it can reasonably be assumed that they will vote in favour of the new share issue for the improper purpose of benefiting themselves.[102] On the other hand, the directors who have "old" shares (including the defaulting directors) are permitted to vote those shares; there is nothing to suggest that they will inevitably be motivated by improper purposes. The decision to affirm a voidable transaction will bind the company (including dissenting shareholders and subsequently appointed controllers) only if it is *properly* taken by an organ with the necessary *authority*.

The more difficult issue is what remedy a company may have against directors found to be in breach of this duty. It is clear that an injunction can issue to prevent an anticipated breach. It is also clear that if the impugned transaction is one between the company and its defaulting director, the transaction will be voidable.[103] However, if the breach has already been committed (so that it is too late for an injunction), and if the dealing is not with the defaulting director but is with some innocent third party, then the position is not so clear. The transaction with the third party will stand, but the better view is that the defaulting director will be liable to make equitable compensation to the company for any resulting loss suffered by the company.[104] The analogy is with directors who fail to comply strictly with their mandate because they act *without* authority. As between the principal and the agent (the company and the director), an abuse of authority *is* a failure to comply with the strict terms of the agent's mandate. However, as between the principal and the third party, the distinction between abuse and absence of authority remains critical.

If defaulting directors are liable to make equitable compensation for their breaches, then the earlier discussion suggests that a company might legitimately release them from this liability.[105] All that is necessary is that the company's decision be properly taken by a corporate organ with the necessary authority. Since the impact of such a resolution is to exonerate the directors and forgive them their liability to the company, it follows that the interested directors must be excluded from the voting process: the inference is that they would vote for the improper purpose of saving themselves from any claims for equitable compensation, a purpose not legitimately within the scope of the power.[106]

In summary, at least in relation to matters internal to the company, there are significant parallels between a director's failure to comply with the strict terms of the mandate (*i.e.* an absence of power) and a director's abuse of power (*i.e.* an exercise of power which is not bona fide and for proper purposes). In relation to outsiders, however, there are important differences between these two forms of breach.

7. The fiduciary duty to act loyally

Breach of the duty which requires directors to act loyally is the breach most often alleged when a company decides to sue its directors rather than simply to get rid of them.[107] It is easy to see why. An appearance of disloyalty, rather than active disloyalty, is sufficient to constitute a fiduciary breach; the director's carefulness, good faith or bona fides are irrelevant. Moreover, the company need not have suffered any loss, but it can nevertheless claim all the profits gleaned by the defaulting director from the breach.[108]

Familiar though this duty is, application of the relevant law is not easy. There are difficulties in defining the scope of the duty, difficulties in determining the reach of the remedy which should be awarded, and difficulties in deciding whether exoneration is possible. It is the last two issues which are properly the subject of this article, but some brief comments on the first are also material.

The fiduciary duty of loyalty is designed to deter directors from acting in ways which might prejudice the interests of their company. The duty is necessary because, in granting directors the power to protect and advance the interests of their company, they are also necessarily given the opportunity to do the exact opposite. The company cannot be adequately protected from this risk by the laws of contract. Directors are not required to achieve a defined end, with failure to do so rendering them liable in damages for breach of contract. Nor can the company be adequately protected by the equitable rules relating to abuse of power. The abuse of power rules will, it is true, catch some disloyal acts,[109] but they cannot prevent directors from acting lethargically in pursuing the company's interests and enthusiastically in promoting their own. Nor can duties of care and skill. The fiduciary duty of loyalty is designed to fill this void.

It is clear from this that the duty of loyalty is about proscriptive rules, not prescriptive ones. A director is prohibited from engaging in certain conduct which is deemed potentially inimical to the interests of effective corporate management. The duty demands self-denial: certain attractive opportunities are open to all bar the director, unless, of course, the company grants its fully informed consent. It is commonly said that the prohibitions imposed on directors are adequately described by two distinct but overlapping rules:[110] directors must not misuse their positions for personal profit; and directors must not take advantage of opportunities which involve a conflict of duty (the director's duty to the company) and interest (the director's personal interest in the transaction). The danger in allowing otherwise is that the director will be swayed by personal interest rather than by duty.[111] When the policy behind the rule is considered, certain situations are clearly "risky": for example, a director's use of corporate confidential information for personal gain;[112] or transactions between the company and one of its directors.[113] But other situations are, in principle, potentially trouble-free: a director who uses skills acquired with one company to move on to bigger and better things with another company; perhaps even a director who leaves to pursue opportunities ignored by, rejected by, or unavailable to the company he leaves.[114] The difficulty is clear. It is to find a balance between compelling directors to act exclusively for the benefit of the company by denying them the possibility of taking a personal benefit from any available opportunities and, as against that, allowing the most productive and efficient—but fair—use of resources by all the players in the market. This tension is clear in judicial statements of the duty. In misuse of position cases, the profit must have been made "by reason and only by reason of the fact that they were directors ... and in the course of the execution of that office".[115] In conflicts of duty and interest cases there must be a "real and sensible" possibility of conflict.[116] How to define these boundaries has been a major concern of fiduciary law.[117]

If this elusive duty can be adequately defined, can the company modify the rigour of its operation in advance? Although companies cannot waive entirely the imposition of fiduciary duties,[118] they can certainly modify their general operation. Companies can expressly restrict either the director's management role or the company's sphere of activity, thereby limiting the circumstances in which a conflict of duty and interest can arise.[119] Companies can also make it easier for directors to have the duty waived when the circumstances warrant it. This is done by providing very simple mechanisms for making full disclosure to the company and obtaining the company's consent to an activity which would otherwise be prohibited. Provision is commonly made for disclosure to the board of directors rather than to the general meeting,[120] and for general disclosures to operate in place of repeated disclosure every time an interest may be relevant. Given this, these fiduciary rules must be regarded as simple default rules. They will operate to protect the company in the absence of alternative rules, but the parties are left relatively free to tailor their own provisions.

If a director is in breach of this duty of loyalty, then the remedies available to the company are potentially lucrative: the company is entitled to demand that the defaulting director disgorge all the profits gleaned from the breach. It is irrelevant that the company could not, or would not, have made those profits itself had the director acted loyally. But the flip side is that profit disgorgement is the limit of the remedy for breach of fiduciary obligation. There is a modern tendency to ignore this. Because of this limitation, it follows that if the director's disloyal behaviour is not profitable to the director, then the company cannot obtain a remedy *for breach of the duty of loyalty*. This is another way of saying that the company cannot use this route to recover incidental losses it has suffered, or to have its corporate assets reinstated, although the facts might support alternative claims to achieve these ends. The duty of loyalty is not designed to remedy losses; other duties fulfil that role. The full extent of remedies for breach of fiduciary duty merits some further amplification. To simplify the analysis it is preferable to isolate and consider separately those cases where the breach involves a transaction between the company and the defaulting director[121] and those cases which do not.

It is clear that any undisclosed contract between a director and his or her company necessarily involves a conflict of duty and interest and perhaps also a misuse of position. The director's duty requires the director to make the best deal for the company, while personal interest prefers the best deal for the director. In this situation the company's remedy is commonly said to be restricted to rescission.[122] The reason is clear: a fiduciary breach entitles the company to require the director to disgorge any profits, but a court is reluctant to try to quantify the director's profit margin on the impugned deal. Instead, the company must decide whether the deal should stand or not. The transaction is voidable; the company can elect to affirm or rescind it. Rescission allows the company to recover the director's profits on the deal. But it follows that if rescission is barred then the company is left without a remedy. This can be harsh, and the traditional view is therefore increasingly under attack.

The first assault arose, perhaps predictably, when it was the defaulting fiduciary who had made it impossible for *restitutio in integrum* to be effected. In *McKenzie v. McDonald*,[123] a woman was persuaded by her real estate agent to sell her farm to him and to buy his shop at valuations which were extremely disadvantageous to her. Rescission of the transaction was impossible because the farm had been resold by the agent to a third party. Nevertheless, the court awarded the plaintiff monetary compensation calculated to give her what she should have received had rescission still been open.[124]

But whether the onslaught will end there is not clear. The Companies Act 1985 Part X takes this approach further, applying it even where the *plaintiff* company has made *restitutio* impossible: a director engaged in an unauthorised dealing with his or her company is required to account for any profits made on the deal regardless of whether the transaction has been avoided.[125] At times there seems to be merit in this approach. For example, where the impugned transaction is a contract for services rather than for sale or purchase, this "monetary equivalent of rescission" is the only approach which can deliver the company a remedy: by definition, the services themselves cannot be returned by the company in order to effect *restitutio in integrum*. Where there is tension in this approach, it seems to arise not because of problems in assessing the "monetary equivalent" of rescission, but because rescission itself does not always appear to fit the policy underpinning fiduciary law. An example illustrates the difficulty.

Assume a transaction for the sale and purchase of land by a company and one of its directors. Such a transaction involves a breach of fiduciary duty unless it is backed by the appropriate consents. Without these consents the deal is voidable by the company. If the transaction is avoided immediately, then the defaulting director is effectively denied the profit which she might have hoped to make on the deal. Moreover, this result is achieved without the courts having to enter upon the difficult task of quantifying the exact profit margin. The remedy fits with the policy of stripping fiduciaries of gains made in breach of their duty of loyalty. The fit continues to be regarded as acceptable even if the vendor company avoids the transaction later down the track, thereby recovering from the purchasing director both the profit margin on the initial sale and any profits due to market increases in the value of the land. This time the fit is acceptable because it is easy to say that the director would not have made either of those forms of profit if she had not entered upon the impugned transaction.[126] Moreover, provided this "but for" test is kept firmly in sight, there would seem to be few difficulties in the way of seeing a "monetary equivalent" of rescission as an equally appropriate remedy in the circumstances.

But change the facts slightly, putting the company in the position of purchaser of the land rather than vendor. Assume the initial sale is at a fair price, but that over time the real estate market collapses, perhaps dramatically. The company, as purchaser, is still entitled to avoid the sale transaction. But now the effect is not simply to strip the defaulting director of the profit made on the initial transaction (nil here, as assessed at the time of the transaction), but also to compel the director to bear the risk of *loss to the company* caused by market revaluations over time. This remedy does not strip the director of profits which she would not have made but for the impugned transaction. Instead it requires her to pay over to the company the "losses she has saved" because the transaction was entered into. But "losses saved" cannot be automatically equated with "profits gained", and certainly this cannot be done unless there is proof that the director *would* have incurred those losses *but for* the disloyal transaction with her company. She might equally well have sold the land to some independent third party, and so still avoided the impact of the collapse of the real estate market. And if any sale to an independent third party would have been at a lower price than the sale to the company, then *that* difference is the measure of the profit the director has gained by acting disloyally in entering into the transaction with her company.

Where *restitutio in integrum* remains possible, it is perhaps easy to ignore these difficulties on the grounds that rescission provides a simple, certain and cost-effective remedy to the company, and moreover the remedy is one which is sure to act as a general deterrent to defaulting fiduciaries. But where *restitutio* is no longer possible, and the "monetary equivalent" of rescission is desired, it may be both appropriate and necessary to return to the policy underpinning the fiduciary rules. The "monetary equivalent" should be designed to strip the defaulting director of only those profits which would not have been made but for the director's disloyalty. The particular facts will always be relevant, but often this can best be done by effecting the notional rescission at the date of entry into the impugned transaction,[127] rather than at some later date when other factors have clouded the central issues.

Certainly if this extended view of rescission *is* adopted to permit the monetary equivalent of rescission when *restitutio* is impossible, then some care must be taken in identifying what ought to be valued. The approach adopted in *Swindle v. Harrison*[128] is illustrative. That case concerned a loan made by a firm of solicitors to its client in order to assist in the purchase of a restaurant, a purchase which turned out to be a financial disaster. The loan transaction was in breach of the solicitor's fiduciary duty, since it involved a secret profit which had not been disclosed to the client. The conventional remedy would be rescission of the loan: repayment of the loan funds by the client in return for release from the repayment obligations (including the obligation to pay the interest which constituted the secret profit to the solicitor). That was no longer possible. The client had already expended the funds in purchasing the restaurant. The client in effect tried to argue that she could make *restitutio* not simply by repaying the loan funds originally received but alternatively by repaying the value of the asset which currently represented those funds—*i.e.* the restaurant (or part of it). This is not true. The risk involved in the principal using the funds to purchase a poor investment—or a good one—does not lie with the fiduciary. The only dealing which is liable to be undone is the loan itself. Market revaluations of the *original* asset (in this case, the loan funds) may be material to the calculations necessary for notional rescission, but the re-investment risk, if other assets are acquired in substitution for the original ones, lies with the re-investing party.[129] These issues of quantification need careful attention.

The second group of cases concerning fiduciary breaches are those where the director's disloyalty does *not* involve a transaction between the company and its director. Here the analytical difficulties are even greater. At least a contract between a company and one of its directors always involves a potential breach of duty. With other ventures, however, the issue is not so clear-cut. The first step, then—although it is not an issue for this article—is to determine whether the impugned venture constitutes a breach of the director's fiduciary duty. It will only fall into this category if it involves a *misuse* of position for profit or a *real* conflict of duty and interest. The boundaries are not clear, and this uncertainty underpins popular calls for a "corporate opportunity doctrine". Notwithstanding this groundswell, the introduction of such a doctrine seems unnecessary so long as the courts take a sensitive view of the particular scope of the fiduciary's obligations. Then, except within the area so defined (whether tightly or loosely circumscribed), the fiduciary retains full economic freedom. Within the defined area, however, the sledge-hammer of fiduciary loyalty requires self-denial from the fiduciary.[130] The difficulty lies in the fact that this boundary needs to be judged with a careful eye to the *purpose* of the rule requiring loyalty. But, having negotiated this process and established a breach (sometimes no easy matter), the second step is to determine the appropriate remedy. The obligation to disgorge the profits of breach is non-controversial—what *is* controversial is quantifying the profits attributable to the breach and then categorising the remedy as either personal or proprietary.

In quantifying the profits attributable to the breach, there is a causation test: only those gains derived from the breach need to be disgorged; other incidental gains are beyond the company's reach. The distinction is not always easy to draw. Sometimes proper assessment means that directors have to disgorge all the profits of an activity;[131] at other times they must disgorge only part of the total profit derived;[132] and possibly there are times when directors may keep the profits subject to disgorgement of a fee regarded as sufficiently representative of the gains attributable to the breach of duty.[133] The particular facts of the case indicate the appropriate method of quantification. There is no hard and fast rule. Only slowly has this been recognised and the rule applied more sensitively and more carefully.

The Australian High Court case of *Warman v. Dwyer*[134] illustrates a considered approach to distinguishing between recoverable and non-recoverable profits. A director had resigned from his company in order to enter into a pre-negotiated joint-venture arrangement with a third party, an Italian gearbox manufacturing company. As a result, the director's Australian company lost its own established distribution agency agreement with the third party. Predictably, the Australian company sued its ex-director for breach of his duty of loyalty. The High Court had to quantify the profits the defaulting director had acquired as a result of his breach (and it distinguished these profits from any *losses* the Australian company may have suffered as a result of the breach[135]). The High Court decided that the director's profits from the breach did not encompass the entire profits of the new joint-venture arrangement. Instead, the High Court awarded an account of the profits of the venture for two years, less an allowance for director's efforts, expenses, skill and expertise. This can be seen as a context-sensitive assessment of the real profits actually derived by the defaulting director from the breach of his duty of loyalty.

The final issue in determining the appropriate remedy for breach of the director's duty of loyalty is to decide whether the remedy is personal or proprietary.[136] The advantages, if the remedy is proprietary, are well appreciated. Sometimes the answer is easy; more often it is not. This is so whether the appropriate remedy is rescission or pure profits disgorgement. If the remedy is proprietary, the relevant proprietary interest arises by operation of law, not by agreement between the parties. These are not circumstances where the parties have negotiated for secured remedial claims. To say that a proprietary interest arises by operation of law is simply a shorthand way of saying that the law imposes a mandatory and unconditional obligation on the defendant director to transfer an identified asset to the plaintiff company.[137] The difficulty arises in determining when the law might impose such an obligation.

Where the director's breach suggests that the proper remedy is rescission, the company is given the right to elect to undo the impugned contract. If that election is made effectively, then the law compels the unravelling of the transaction. Assets transferred under the dealing must be returned. If an analogy is needed, the *undoing* of the dealing is then treated much like a specifically enforceable sale contract.[138] If the plaintiff company has sold an asset to the defaulting director, for example, then rescission requires that the identified asset be returned to company upon repayment by the company of the purchase price. In these circumstances the traditional view is that the company acquires an equitable proprietary interest in the asset once the transaction had been effectively rescinded and the purchase price repaid.[139] In these circumstances, the director is seen as under a mandatory and unconditional obligation to return the identifiable sale asset.[140] On its face the rule might appear somewhat one-sided, in that it favours vendors over purchasers. A *purchasing* company entitled to rescind would rarely be able to claim a proprietary interest in any fund representing the purchase money paid to the defaulting director, for the simple reason that those purchase funds would not be identifiable at the time of rescission. However, by analogy with specifically enforceable contracts of sale, this *undoing* of the original transaction might be seen as giving the purchasing company an equitable lien on the returned asset to secure (as far as possible) the director's obligation to refund the purchase money. All of this has obvious advantages for companies claiming rescission of transactions with their defaulting directors, yet there are now distinct signs of a reappraisal of the rules. The reappraisal is welcome, as the area has always had its difficulties and uncertainties, yet much of the commentary which advocates abolition of these proprietary consequences is based on flawed assumptions about their impact on insolvency.[141] Given this, the better view still seems to be that rescission can have proprietary consequences.

That leaves cases of directors' breaches where the proper remedy is profit disgorgement. These are the more difficult cases in which to assess the incidence of proprietary remedies. Current scholarship would see the remedy as proprietary if the plaintiff company can show an initial proprietary base and can identify an unbroken chain of events linking that base to identifiable substitutions.[142] This will sometimes be possible where the defaulting director has made an unauthorised profit by exchanging the *company's* assets for other assets. Then the analogy with adopting unauthorised trustee investments assists the assertion that the company's claim is proprietary. But otherwise the argument is not so easy.

This is especially so where the company's property has not been used for an exchange, but instead the director has taken a corporate opportunity or misused his or her position. It is true that disgorgement of the fiduciary's profits has often been delivered as a proprietary remedy,[143] but the issue remains controversial. Even at a theoretical level, it is difficult to determine which is the better approach. One approach is to concede that the disgorgement remedy is punitive and that it delivers a windfall to the plaintiff company which is justified only on the basis of its desirable deterrent effect. With this as its justification, there is perhaps little force in any suggestion that the company should also have the added advantage of priority over the defaulting director's other creditors.[144] Going further, it has even been suggested that the company's remedy should be subordinated to the claims of the defaulting director's other creditors.[145]

On the other hand, *if* the obligation to disgorge the profits is seen as an obligation imposed by law to disgorge them *in specie* (and this is the critical issue), and *if* the profits are identifiable, then analogy with other cases arising in different contexts suggests that equity will treat as done that which ought to be done and the plaintiff company will be treated as the owner in equity of the profits as soon as they are derived.[146] If the defaulting director subsequently becomes bankrupt, then the insolvency regime as it currently operates will do nothing to upset these pre-insolvency property rights. There is a great deal at stake in this debate, and the policy issues need very careful consideration before a superior court could convincingly adopt one or other approach—or before a defensible plan for codification could be advanced with confidence.[147]

In this discussion of directors' duties of loyalty, there remains one final issue to consider: can the company excuse its defaulting directors from breach of their fiduciary duties? Recourse to the cases presents a very confused and unsatisfactory picture. The cases suggest that the general meeting is the only body competent to make such a decision on behalf of the company.[148] Moreover, a superficial reading of the cases suggests that there is a fundamental distinction between breaches which are remedied by rescission and breaches which are remedied by disgorgement.[149] The former can be affirmed by the company with impunity. It even appears not to matter that the defaulting director controls the general meeting making the decision to affirm.[150] But where disgorgement is the remedy, the picture is more complicated. The company can exonerate its directors if this does not involve giving away corporate assets, but not otherwise.[151] Again, the composition of the general meeting appears not to matter.[152]

None of this makes much sense. A company can give away its assets, provided the decision is taken for proper purposes and does not contradict any express restrictions in the company's constitution. The company will be doing exactly this *whenever* it decides to exonerate its defaulting directors. If it decides to affirm a voidable transaction, then it allows the director to retain any profit margin on the deal. The company cedes its legal rights to it. If it decides not to pursue a disgorgement remedy, then it allows the director to retain the profits of the impugned transaction. Again, the company cedes its rights. In each case these are rights which have an incontrovertible money value. In this respect no distinction can be drawn—as some commentators have argued— between voidable transactions, profits derived from corporate opportunities which would "certainly" have gone to the company except for the breach, and profits derived from corporate opportunities which might not (or would certainly not) have gone to the company even absent the breach.[153] The company is not suing for its own loss of the corporate opportunity, when such distinctions would be material. It is suing (or not suing) for disgorgement of the profits from the director's successful pursuit, a pursuit judged to be in breach of duty. In principle a company ought to be able to exonerate its directors for *any* breach of fiduciary duties. There is no sensible way to deny a competent legal actor this right in any context,[154] much less to distinguish between the different contexts of different breaches.

If it is accepted that all fiduciary breaches can, in theory, be exonerated, then the real issue is to determine whether a purported exoneration is *effective* to bind the company. The rules ought to be exactly the same as those discussed earlier in relation to non-fiduciary breaches.[155] Either the decision should be made properly by the board of directors, or it should be made properly by the general meeting. In determining whether a decision by either organ is "proper", the focus is on the bona fides and proper purposes of the voting constituency. With *either* organ, the equitable restrictions must mean that the defaulting directors cannot themselves be counted towards the majority favouring exoneration.[156] They would be judges in their own cause, and therefore might be presumed to be biased and inclined to use their voting powers for what must constitute improper purposes. As with other breaches, then, the critical issue is not the capacity of the company to exonerate its directors, or the authority of the appropriate corporate organ to take the decision,[157] but the *propriety* of any decision purportedly taken.[158]

In summary, a director's duty of loyalty is perhaps the most necessary but least well analysed duty imposed on directors. The issue of whether there has been a breach must be taken sensitively, with an eye to the policy underpinning the fiduciary restrictions. In determining the appropriate remedy, transactions between the company and its defaulting director must be distinguished from other breach situations. The appropriate remedy in the former case is rescission (or perhaps its monetary equivalent). In the latter it is profits disgorgement. Whether or not the remedy has proprietary consequences is an important but still unsettled issue. Perhaps the most that can be said is that precedent favours proprietary consequences but academic comment does not. Finally, principle suggests that the company ought to be able to exonerate its directors from any breach of their duty of loyalty so long as the decision is taken bona fide and for proper purposes. The cases, however, present a different and far from consistent picture of the possibilities. This area of law stands at the heart of corporate governance. Given its policy underpinnings and its practical reach, it is difficult to conceive that statutory rules could adequately cover the ground.[159] An authoritative, rigorous and considered re-evaluation of the reach of the rules would be better. The result is likely to be a more flexible and context-sensitive contribution to corporate governance.

8. Conclusion

When directors are under-performing, in breach of the duties required of them by law, the facts will often allow the company to pursue alternative routes to different remedies. The route leading to the best remedy will be the one pursued with the most vigour. Given this, it is sometimes suggested that the most efficient approach would be to allow the court to respond in the manner which seems most appropriate in the circumstances once there is proof of a breach of duty. This discretionary approach to remedies seems to be advanced with more vigour in the context of equitable breaches than common law wrongs, perhaps because the conventional "discretionary" nature of equitable remedies suggests a flexibility not present elsewhere. In a sense, Part X of the Companies Act 1985 has adopted this route. It limits the ambit of a director's authority in circumstances where the director receives a benefit, so contributing to the mandate rules and overlapping with the fiduciary rules. It then gives all possible remedies against all possible players.

This is not necessarily the best general strategy. This article advocates retaining the existing common law distinctions between different breaches and their different remedial consequences. This seems to be the most efficient way—the least intrusive way—for the law to persuade directors to deliver good performances. That said, the common law position is beset with unacceptable uncertainties and inconsistencies which undermine its effectiveness. This article advances a strict analytical approach. Directors are subject to a duty of care, a duty of strict compliance, a duty to act bona fide and for proper purposes, and a duty of loyalty. Quite different facts must be established to prove a breach of each. The remedies, too, are different. Of the available alternatives, both common law damages and equitable compensation are personal remedies only; profits disgorgement, on the other hand, can be either a personal or a proprietary remedy.

The company has only limited capacity to waive in advance the breach of any of these duties.[160] However, in principle there seems to be no reason why a company does not have the capacity to exonerate its directors after the event, regardless of the breach. All that is needed, in addition to this necessary corporate capacity, is an organ with the necessary authority to make a proper determination of the issue at stake. These three requirements—*capacity*, *authority* and *propriety*—also determine whether any decision to adopt or ratify an impugned transaction is binding. Each requirement deserves careful consideration. The capacity of a company is determined by the general law and the company's constitution. The authority of any corporate organ is usually a matter of interpretation of the company's constitution. The propriety of any resolution rests on the bona fides and proper purposes of the decision-making body. All are necessary if a decision is to effectively bind the company. Finally, and very importantly, to say that the company is effectively bound is the equivalent of saying that no future controller (whether a new board of directors or a liquidator) or dissenting shareholder can attempt to go back on the decision.[161]

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[1] Law Commission, *Company Directors: Regulating Conflicts of Interest and Formulating a Statement of Duties* (No. 261, 1999) ('LCR').
[2] DTI, *Modern Company Law for a Competitive Economy* (1998); and DTI: *Modern Company Law for a Competitive Economy: The Strategic Framework* (Feb 1999).
[3] At a superficial level there are few difficulties in describing the remedial consequences of directors' breaches, but dig deeper, to issues of whether the remedy is proprietary, or whether certain remedies can be "given up" by the company, and the picture soon becomes more confused.
[4] See, *e.g.*, the principles enshrined in the Combined Code (Appendix to the London Stock Exchange Listing Rules), adopted following reports from the Cadbury, Greenbury and Hampel Committees.
[5] But see, *e.g.*, Insolvency Act 1986 s. 213 (fraudulent trading), where the assessment of damages is designed to be penal.
[6] (1843) 2 Hare 461; 64 E.R. 189. In this context, this article is intended as a reassessment of the views advanced in the classic article by K. W. Wedderburn, "Shareholders' Rights and the Rule in Foss v. Harbottle" [1957] C.L.J. 194 and [1958] C.L.J. 93. See especially Section 3 below.
[7] For detail, see S. Worthington, "Fiduciary Obligations: When is Self-Denial Obligatory?" [1999] C.L.J. 500.
[8] Also see *Aquaculture Corp.* v. *New Zealand Green Mussel Co. Ltd* [1990] 3 N.Z.L.R. 299, 301.

[9] If the initial attempt to contract with a third party was ineffective because the organ or individual acting for the company lacked authority, then the company, via another organ, may be able to adopt the unauthorised contract: this is "ratification" used in its familiar context in agency law.

[10] If the contract to which the company is a party is voidable by the company, then company has the right to elect whether to affirm or avoid.

[11] Also see K. W. Wedderburn, "Shareholders' Rights and the Rule in Foss v. Harbottle" [1957] C.L.J. 194 and [1958] C.L.J. 93; R. J. C. Partridge, "Ratification and the Release of Directors from Personal Liability" [1987] C.L.J. 122; R. Cranston, "Limiting Directors' Liability: Ratification, Exemption and Indemnification" [1992] J.B.L. 197; J. P. Lowry, "Ratifying Directorial Wrongdoing—the Legal Fiction of Shareholder Consent in England" in B. A. K. Rider (ed.), *The Corporate Dimension* (1998, Bristol) ch 10.

[12] Or at least not without bearing the normal legal consequences of such a change of heart.

[13] See the following footnote. Whether or not the corporate decision is effective, disaffected shareholders may still have a Companies Act 1985 s. 459 claim against the company or against particular individuals because of the course of conduct adopted.

[14] Disaffected shareholders seeking to pursue *derivative* actions usually assert that the third requirement has not been met: *i.e.* that although the company, via the chosen organ, *could* take the decision it has purported to take, it has not done so properly and the decision is therefore ineffective to bind the company to the proposed course of action. On the other hand, disaffected shareholders seeking to pursue *personal* claims usually assert that the first or second requirement has not been met: *i.e.* that the company itself cannot take the purported decision, or, failing that, that the chosen organ cannot take the decision, which is therefore ineffective to impinge on the personal rights of the shareholder.

[15] If this approach is to apply quite generally—and there is no reason that it should not—then the answer to each question must be either "Yes, in fact", or "Yes, because the third party wishing to rely on the corporate decision is entitled to assume that the answer is yes". Assumptions permitted by the Companies Act 1985 ss. 35, 35A and by the common law rules of ostensible authority can often be invoked to assist third party strangers in their dealings with the company, but they will not assist directors who wish to assert that a decision binds the company. Directors will only be able to rely on a purported decision if *in fact* the answer to all three questions is "yes". (See Companies Act 1985 s. 322A, and cases such as *Hely-Hutchinson v. Brayhead Ltd* [1968] 1 Q.B. 549 (CA), where the validity of the transaction between the company and one of its directors depended crucially upon a finding that the company chairman, as the company's agent, had *actual* authority to contract—although contrast the more indulgent approach of the trial judge, Roskill J., in the same case, *ibid*.) Since this article is solely concerned with directors and their relationship with the company, the context in which the assumptions might be available is not considered. However, this aspect of the law is neither difficult nor controversial.

[16] And this inevitably means that all of the company's organs are bound, so that both future controllers and dissenting shareholders are bound.

[17] Although for the general position, see note 15 above.

[18] See, *e.g.*, Companies Act 1985 ss. 310, 263, 330-342. These sections denying corporate capacity would deny the general meeting (or any other organ) the authority to ratify a dealing in contravention of these provisions. See *Re Halt Garage (1964) Ltd* [1982] 3 All E.R. 1016, 1039; *Aveling Barford Ltd v. Perion Ltd* [1989] B.C.L.C. 626, [1989] B.C.C. 677.

[19] In the context of this article, it is the actual authority of the organ which is relevant, not its power: see note 15 above. This is not true when the company is dealing with outsiders.

[20] But not if another corporate organ could properly reach the same position. In these circumstances it may also be possible for a shareholder to take a *personal* action to remedy detriments suffered personally.

[21] See, *e.g.*, Companies Act 1985 ss. 4, 17, 9, 35.

[22]*Boschoek Pty Co. Ltd v. Fuke* [1906] 1 Ch. 148; *Quin & Axtens v. Salmon Quin & Axtens v. Salmon* [1909] A.C. 442 (HL).

[23] *Irvine v. Union Bank of Australia* (1877) 2 App. Cas. 366, at pp. 375-6 (PC); *Grant v. United Kingdom Switchback Railways Co.* (1888) 40 Ch. D. 135 (CA); *Re Horsley & Weight Ltd* [1982] Ch. 442 (CA). As a general rule, if there is no board of directors competent to act, then the general meeting can decide the issue: *Barron v. Potter* [1914] 1 Ch. 895.

[24] [1909] A.C. 442 (HL).

[25] Although the general meeting could eliminate the constraint by altering the company's constitution (provided it had the necessary majority and provided the vote was a *proper* exercise of power—see below): *Imperial Hydropathic Hotel Co., Blackpool v. Hampson* (1882) 23 Ch. D. 1 (CA).

[26] (1888) 40 Ch. D. 135 (CA).

[27] The distinction cannot be based on the fact that the transaction in this case was merely voidable rather than void: the company's articles denied the directors authority; they did not merely render the transaction voidable

for breach of fiduciary duty. See the argument adopted in *Guinness v. Saunders* [1990] 2 A.C. 663 (HL), notwithstanding suggestions to the contrary in *Grant v. United Kingdom Switchback Railways Co.* (1888) 40 Ch. D. 135 (CA).

[28] *Wood v. Odessa Waterworks Co.* (1889) 42 Ch. D. 636; cf. *MacDougall v. Gardiner* (1875) 1 Ch. D. 13 (CA). To assert that a shareholder has a personal right which cannot be denied by ordinary resolution of the general meeting seems to be merely a less direct way of saying that the general meeting lacks the necessary authority to ratify: see, *e.g.*, *Pender v. Lushington* (1877) 6 Ch. D. 70; *Edwards v. Halliwell* [1950] 2 All E.R. 1064 (CA); *Re a Company* [1987] B.C.L.C. 82, at p. 84 *per* Hoffmann J.; *Residues Treatment & Trading Co. Ltd v. Southern Resources Ltd (No. 4)* (1988) 51 S.A.S.R. 177, 14 A.C.L.R. 569. If the corporate organ lacks authority, then note that any remedy which might be claimed by a shareholder pursuing a personal action is not the same as that sought by the company pursuing the wrongdoers.

[29] Moreover, if the board of directors did have authority, then the general meeting could not give it mandatory orders: *Automatic Self-Cleansing Filter Syndicate Co. Ltd v. Cunninghame* [1906] 2 Ch. 34 (CA); *John Shaw & Sons (Salford) Ltd v. Shaw* [1935] 2 K.B. 113 (CA).

[30] If the board of directors has interested directors amongst its numbers, then see (i) Companies Act 1985 s. 317, breach of which does not affect the validity of the board's decision, but exposes the defaulting director to liability for a fine: *Guinness v. Saunders* [1990] 2 A.C. 663; and (ii) Table A arts 85, breach of which will render the dealing with the defaulting director voidable at the option of the company: *ibid*.

[31] For example, in property law it applies to a power to distribute among a class; in administrative law it applies to the exercise of administrative discretions; in corporate insolvency, it applies to the power of receivers, liquidators and administrators.

[32] (1758) 1 Eden 132, 138; 28 E.R. 634, 637.

[33] The complaint is not *absence* of authority, but *abuse* of authority. This is a matter between the principal (the company) and its defaulting—power-abusing—agent (the relevant corporate organ). It is not, at least directly, a matter between the principal (or the agent) and the third party. It is therefore probably more accurate to say that the agent's decision is voidable rather than void. It cannot always be set aside. This can only be done as against a third party who was aware of the abuse of power. Often strangers dealing with the company will be entitled to make assumptions about the bona fides and proper purposes of the corporate organ. In the context of the issues discussed in this article, however, such assumptions are unlikely to be available to directors. With them (and with strangers lacking bona fides), the usual but unilluminating terminology adopted is that of constructive trusteeship.

[34] *Pender v. Lushington* (1877) 6 Ch. D. 70, at pp. 75-6 *per* Jessel M.R.

[35] As might be suggested by a superficial reading of *Burland v. Earle* [1902] A.C. 83; *North-West Transportation v. Beatty* (1887) 12 App. Cas. 589; *East Pant Du United Lead Mining Co. v. Merryweather* (1864) 2 H. & M. 254.

[36] *Cook v. Deeks* [1916] 1 A.C. 554 (PC); *Daniels v. Daniels* [1978] Ch. 406; K. W. Wedderburn, "Shareholders' Rights and the Rule in Foss v. Harbottle" [1957] C.L.J. 194 and [1958] C.L.J. 93.

[37] *Vatcher v. Paull* [1915] A.C. 372, at p. 378 *per* Lord Parker; *Peter's American Delicacy Co. Ltd v. Heath* (1939) 61 C.L.R. 457, at pp. 511, 513 *per* Dixon J.; *Ngurli v. McCann* (1953) 90 C.L.R. 425, at pp. 438, 447; *Winthrop Investments Ltd v. Winns Ltd* [1975] 2 N.S.W.L.R. 666, at pp. 701-3 *per* Mahoney J.A.

[38] And certainly there is support for its existence. See *Allen v. Gold Reefs of West Africa Ltd* [1900] 1 Ch. 656, at p. 671 *per* Lindley M.R.; *Peter's American Delicacy Co. Ltd v. Heath* (1939) 61 C.L.R. 457; *Gambotto v. WPC Ltd* (1995) 182 C.L.R. 432; *Millers (Invercargill) Ltd v. Maddams* [1938] N.Z.L.R. 490; *Western Mines Ltd v. Shield Development Co. Ltd* [1976] 2 W.W.R.300; P. D. Finn, *Fiduciary Obligations* (1977, Sydney), at p. 73; G. Farwell, *A Concise Treatise on Powers* (3rd ed, 1916, London), at pp. 458-9. Even in England the restriction is not confined to alteration of the articles: see, *e.g.*, *Clemens v. Clemens Bros* [1976] 2 All E.R. 268; *Eastmanco (Kilner House) Ltd v. Greater London Council* [1982] 1 W.L.R. 2; *Multinational Gas and Petrochemical Co. v. Multinational Gas and Petrochemical Services Ltd* [1983] Ch. 258, at pp. 280-1 *per* May L.J.

[39] *Peter's American Delicacy Co. Ltd v. Heath* (1939) 61 C.L.R. 457, at p. 504 *per* Dixon J.

[40] *Dutton v. Gorton* (1916) 23 C.L.R. 362, at p. 395. In certain circumstances this might include acting in defiance of the interests of the company's creditors: *Kinsela v. Russell Kinsela Pty Ltd (in liq)* (1986) 4 N.S.W.L.R. 222, (1986) 10 A.C.L.R. 395; *Multinational Gas and Petrochemical Co. Ltd v. Multinational Gas and Petrochemical Services Ltd* [1983] Ch. 258 (May L.J.).

[41] Whether the improper purpose must be a *substantial* or *primary* reason for the exercise of the power, or whether the higher "*but for*" test must be met remains a moot point. The same issue in the context of directors' voting power seems to be resolved in favour of the former test in England, but the latter in Australia: see

Howard Smith Ltd v. Ampol Petroleum Ltd [1974] A.C. 821 (although a PC decision) and *Whitehouse v. Carlton Hotel Pty Ltd* (1987) 162 C.L.R. 285 respectively.

[42] See especially *Allen v. Gold Reefs of West Africa Ltd* [1900] 1 Ch. 656, at p. 671 *per* Lindley M.R.

[43] *Bamford v. Bamford* [1970] Ch. 212.

[44] These cases underline the fundamental difference between a shareholder's personal right to vote and the effectiveness of any particular decision of the general meeting. The latter is not determined by a simple head-count of those shareholders entitled to vote on the matter. It is true that the court cannot order that certain shareholders be disenfranchised (*Mason v. Harris* (1879) 11 Ch. D. 97), but it can adjudicate upon the effectiveness of any resolution passed at a general meeting. That determination may well depend upon its assessment of the views of the disinterested shareholders: *Rights and Issues Investment Trust Ltd v. Stylo Shoes Ltd* [1965] Ch. 250; *Hogg v. Cramphorn Ltd* [1967] Ch. 254; *Bamford v. Bamford* [1970] Ch. 212; *Prudential Assurance Co. Ltd v. Newman Industries Co. Ltd (No. 2)* [1982] Ch. 204 (CA); *Smith v. Croft (No. 2)* [1988] 1 Ch. 114.

[45] *Cook v. Deeks* [1916] 1 A.C. 554 (PC); *Atwool v. Merryweather* (1867) L.R. 5 Eq. 464n; *Menier v. Hooper's Telegraph Works* (1874) 9 Ch. App. 350 (CA).

[46] *Allen v. Gold Reefs of West Africa Ltd* [1900] 1 Ch. 656 (CA); *Re Holders Investment Trust Ltd* [1971] 1 W.L.R. 583; *Ebrahimi v. Westbourne Galleries Ltd* [1973] A.C. 360 (HL); *Scottish Co-operative Wholesale Society Ltd v. Meyer* [1979] A.C. 324 (HL); *Clemens v. Clemens Bros Ltd* [1976] 2 All E.R. 268, at p. 282; *Re Halt Garage (1964) Ltd* [1982] 3 All E.R. 1016. The last two cases suggest some movement in English jurisprudence to a more general statement of the equitable restriction. But it is also possible to read other cases as advancing similar ideas: see, *e.g.*, *British America Nickel Corpn Ltd v. O'Brien* [1927] A.C. 368 (PC) (class rights); *Re Hellenic & General Trust Ltd* [1976] 1 W.L.R. 123 (scheme of arrangement). On rare occasions the courts have even intervened to restrain shareholders from acting perversely: *Standard Chartered Bank Ltd v. Walker* [1992] 1 W.L.R. 561; *Theseus Exploration NL v. Mining & Associated Industries Ltd* [1973] Qd. R. 81.

[47] *Peter's American Delicacy Co. Ltd v. Heath* (1939) 61 C.L.R. 457, at p. 511 *per* Dixon J. The same idea is repeated in many of the cases already cited.

[48] *Crumpton v. Morrine Hall Pty Ltd* [1965] N.S.W.R. 240, at p. 244 *per* Jacobs J.

[49] See notes 15 and 33 above.

[50] *Re City Equitable Fire Insurance Co. Ltd* [1925] Ch. 407.

[51] See LCR, note 1 above, Part 5.

[52] *Re D'Jan of London Ltd* [1994] 1 B.C.L.C. 561, [1993] B.C.C. 648 (Hoffmann J.); S. Worthington, "The Duty to Monitor: A Modern View of the Director's Duty of Care" in F. Macmillan (ed), *Perspectives in Company Law: 2* (Kluwer, 1997) ch 11 and the references cited therein.

[53] See K. Santow, "The Codification of Directors' Duties" (1999) 73 A.L.J. 336.

[54] See Companies Act 1985 s. 310, although s. 310(3) allows the company to purchase insurance on the director's behalf and to indemnify the director for liabilities incurred in successfully defending actions.

[55] Companies Act 1985 s. 727. See *Re D'Jan of London Ltd* [1994] 1 B.C.L.C. 561 (Hoffmann J.).

[56] Directors who continue to perform as directors may be able to rely on this fact, either as being consideration for the release or as founding an estoppel. The release will then bind the company (and therefore any future controllers). Note however that even a gratuitous release, which the company might go back on at a future date, is an effective decision of the *company* not to sue its directors *now*; it will therefore bind dissenting shareholders. As already noted, and as discussed again below, their only avenue for attack will be to deny that the decision to release *was* effective (*i.e.* within the company's capacity, authorised and properly taken).

[57] This is as true for companies as it is for individuals. An individual might, for example, rely on the advice of a stockbroker, but might also simply give instructions to the broker to implement an investment decision made independently of the broker. The broker can only be sued for negligent advice in the first case, not in the last.

[58] [1983] Ch. 258.

[59] The fact that the general meeting cannot impose its will on the board of directors in determining management direction (unless the articles allow this) does not alter the analysis. If the company (via the general meeting) decides on a course of action which the directors are *prepared* to implement, then the directors escape liability in negligence (at least to the extent that their skill and care was not relied upon). The same approach is routinely adopted in the case of trustees and beneficiaries. The trustees are not obliged to manage the trust according to directions from the beneficiaries but, to the extent that they do, they are immune from suit by the directing beneficiaries. Note that the parallel is between the *company* and the beneficiaries, not between the *shareholders* and the beneficiaries.

[60] Subject to note 30 above.

[61] In which case the general meeting can act: *Barron v. Potter* [1914] 1 Ch. 895.

[62] *Automatic Self-Cleansing Filter Syndicate Co. Ltd v. Cuninghame* [1906] 2 Ch. 34 (CA); *Quin & Axtens Ltd v. Salmon* [1909] A.C. 442 (HL); *John Shaw & Sons (Salford) Ltd v. Shaw* [1935] 2 K.B. 113 (CA).
[63] As recognised in *Whitehouse v. Carlton Hotel Pty Ltd* (1987) 162 C.L.R. 285, at pp. 289-90 *per* Mason, Deane and Dawson J.J. (obiter). This does not mean that the board of directors might not act in accordance with the wishes of the general meeting, but it does mean that they need not accede to such wishes and, provided the decision is properly taken, the company will be bound. Nor does this legal position deny the practical problem that market *perceptions* (and questions of corporate reputation and standing) might sometimes make general meeting approval advisable, even though functionally unnecessary.
[64] [1978] Ch. 406. The case was decided on the basis that this *type* of negligence (self-serving) could not be waived by the general meeting: it could not be made binding on *any* dissenting minority of shareholders. It must follow that such a decision would not be binding on a subsequently appointed liquidator or other corporate controller—in short, it is not binding on the company. On the analysis favoured here, the focus would not be on the type of negligence, but on the propriety of the general meeting resolution to waive the breach: see the discussion below.
[65] [1956] Ch. 565.
[66] Obiter dicta in *Re Horsley & Weight Ltd* [1982] Ch. 442 (CA) support this: see the comments of Cumming-Bruce L.J. (at p. 455) and Templeman L.J. (at p. 456), suggesting that directors would not be allowed to vote to ratify their own negligence notwithstanding that they did not benefit directly from the transaction. Also see *Multinational Gas and Petrochemical Co. Ltd v. Multinational Gas and Petrochemical Services Ltd* [1983] Ch. 258, at pp. 280-1 *per* May LJ, suggesting that even a unanimous vote of all the shareholders could not gratuitously release the directors and thereby give away corporate assets; as discussed later, this seems to go too far—a decision to give away corporate assets is not automatically "improper".
[67] For example, the potential damage to reputation and goodwill may outweigh the sums likely to be recovered.
[68] Notwithstanding that directors are not trustees and that the company's assets are not held on trust. See *Re Lands Allotment Co.* [1894] 1 Ch. 616; *Bishopsgate Investment Management Ltd (in liq) v. Maxwell (No. 2)* [1994] 1 All E.R. 261 (CA).
[69] A careful distinction may need to be drawn between acts which are *beyond* a director's authority and acts which are an *abuse* of authority: see *Rolled Steel Product (Holdings) v. British Steel Corp.* [1986] 1 Ch. 246. The latter is discussed in the next section.
[70] *Re Lands Allotment Co. Ltd* [1894] 1 Ch. 631, at p. 638.
[71] *Charterbridge Corpn Ltd v. Lloyds Bank Ltd* [1970] Ch. 62.
[72] I. E. Davidson, "The Equitable Remedy of Compensation" (1982) 13 M.U.L.R. 349.
[73] Such recipients are usually protected by Companies Act 1985 ss. 35, 35A and the common law rules on ostensible authority. If they are not, then the transaction is void: *Westdeutsche Landesbank Girozentrale v. Islington London Borough Council* [1996] A.C. 669; *Guinness plc v. Saunders* [1990] 2 A.C. 633. If the defaulting director is a party to the mis-dealing, and so is a recipient of corporate assets, then a claim against the recipient director for breach of fiduciary duty (since such a transaction will automatically involve a conflict of duty and interest) will allow the company to claim disgorgement of any profits the director may have gleaned from the breach (as discussed later). At common law, the claim against the perpetrators for loss and the claim against the recipient for disgorgement are alternatives: the company cannot approbate and reprobate the transaction at the same time. The Companies Act 1985 s. 322A, on the other hand, provides for a menu of remedies available against a range of potential defendants.
[74] *Target Holdings Ltd v. Redferns* [1997] 1 A.C. 421.
[75] Although it cannot relieve then from the duty to comply with the terms which are in place: Companies Act 1985 s. 310.
[76] *Allen v. Gold Reefs of West Africa Ltd* [1900] 1 Ch. 656, at p. 671 *per* Lindley MR; *Peter's American Delicacy Co. Ltd v. Heath* (1939) 61 C.L.R. 457; *Gambotto v. WPC Ltd* (1995) 182 C.L.R. 432.
[77] Companies Act 1985 s. 35(3), and this resolution must be in addition to any resolution affirming the transaction.
[78] *Grant v. United Kingdom Switchback Railways Co.* (1888) 40 Ch. D. 135 (CA). Also see Companies Act 1985 s. 727.
[79] See Section 4, above.
[80] *Smith v. Croft (No. 2)* [1988] 1 Ch. 114, at pp. 178-83.
[81] And it need not be. Ratification is by the company, acting through an appropriate organ; it is not ratification *by* the organ. For example, ratification might be effected by the liquidator: see *Alexander Ward & Co. Ltd v. Samyang Navigation Co. Ltd* [1975] 1 W.L.R. 673 (HL), at p. 678 *per* Lord Hailsham.

[82] Companies Act 1985 s. 35(3). Absent this statutory rule, the general meeting would not have the authority to ratify the transaction: being a transaction outside the company's objects, it would be beyond the capacity of *either* of the company's organs; see *Boschoek Pty Co. Ltd v. Fuke* [1906] 1 Ch. 148.
[83] See Section 3.2, above.
[84] *Smith v. Croft (No. 2)* [1988] 1 Ch. 114, at pp. 178-83.
[85] Of course, ratification is only needed if someone is attempting to deny the validity of the dealing. In most cases the other party to the transaction will be keen to enforce the deal, and will have the benefit of Companies Act 1985 ss. 35, 35A and the common law rules of ostensible authority.
[86] *North-West Transportation v. Beatty* (1887) 12 App. Cas. 589 might be taken as suggesting the contrary, but both the facts and the tenor of the judgment suggest otherwise.
[87] Companies Act 1985 s. 263.
[88] Companies Act 1985 ss. 330-342.
[89] Companies Act 1985 s. 320.
[90] Companies Act 1985 ss. 322, 322A, 341.
[91] *Ibid.*
[92] See Section 7, below.
[93] *Punt v. Symons & Co. Ltd* [1903] 2 Ch. 506; *Re Smith & Fawcett Ltd* [1942] Ch. 304; *Hogg v. Cramphorn Ltd* [1967] Ch. 254; *Howard Smith Ltd v. Ampol Petroleum Ltd* [1974] A.C. 821 (PC); *Mills v. Mills* (1938) 60 C.L.R. 150. Companies Act 1985 s. 310 prevents any general release from this duty.
[94] *Hogg v. Cramphorn Ltd* [1967] Ch. 254; *Howard Smith Ltd v. Ampol Petroleum Ltd* [1974] A.C. 821 (PC). Historically, "bona fide" was seen as equivalent to "genuine": L. S. Sealy, "'Bona Fides' and 'Proper Purposes' in Corporate Decisions" (1989) 15 *Monash University Law Review* 265. It might even be possible to see the restriction as demanding only "proper purposes": see *Peter's American Delicacy Co. Ltd v. Heath* (1939) 61 C.L.R. 457, at pp. 511-512 *per* Dixon J.
[95] *Howard Smith Ltd v. Ampol Petroleum Ltd* [1974] A.C. 821 (PC).
[96] *Rolled Steel Products (Holdings) Ltd v. British Steel Corpn* [1986] 1 Ch. 246 (CA).
[97] And the issue of what will count as "knowledge" is controversial.
[98] Note, however, that where a *director* is the "knowing third party" dealing with the company, it is often easier to obtain a remedy by asserting that the transaction also involves a breach of the director's *fiduciary* duties: see Section 7, below. Secondly, the statement that the transaction is voidable, not void, merits further comment (also see note 33, above). It hides some controversy. In *Rolled Steel Products (Holdings) Ltd v. British Steel Corpn* [1986] 1 Ch. 246 (CA), a case raising both absence and abuse of authority, Browne-Wilkinson L.J. appears to adopt the analysis advocated here. His analogy with trustees acting in abuse of their powers makes it clear that he regards the improper purposes issue as one of *abuse* of authority by the agent, not *absence* of authority. As such, the issue is one between the company (as principal) and its directors (as agents). Third parties would only be affected if the company could show that the third party had constructive knowledge of the breach of equitable duty. In those circumstances the transaction would be voidable. Note that this reverses both the presumption of regularity and the onus of proof when compared with the analysis based on absence of authority. Where the agent has *no* authority, the transaction is *void* unless the *third party* can show that it is entitled to rely on the agent's ostensible authority. Where the agent has *abused* its authority, the transaction is *valid* unless the *company* (the principal) can prove that the third party was aware of the agent's breach. These distinctions are important for the analysis advanced here. Most cases do not make these distinctions so aggressively. Nevertheless, the distinction does find support in cases such as *Spackman v. Evans* (1868) L.R. 3 H.L. 171, at p. 244 *per* Lord Romilly; *Bamford v. Bamford* [1970] Ch. 212 (CA); *Gaiman v. National Association forMental Health* [1971] 1 Ch. 317, at p. 330 *per* Megarry J. On the other hand, again in *Rolled Steel Products (Holdings) Ltd v. British Steel Corpn* [1986] 1 Ch. 246 (CA), Slade L.J. (with whom Lawton L.J. agreed) suggested that directors had *no* authority to engage in acts which were not for "company purposes", being purposes defined in the company's memorandum. He was content to adopt this analysis notwithstanding that it was not one adopted (at least expressly) in any of the authorities upon which he relied. Moreover, his stated approach seems counter to his obiter comments on shareholder ratification: if the board of directors has no authority to act for non-corporate purposes, then it seems contradictory to assume that the other corporate organ, the general meeting, can be authorised to act in this way. Finally, this analysis seems to invite a distinction between "non-*corporate* purposes" (which deny the directors authority) and other "improper purposes" (which render the transaction voidable). Such a degree of subtlety seems unwarranted.
[99] Unless there is no board of directors competent to act. See Section 3, above.
[100] If the law develops to allow the "monetary equivalent" of rescission, the impact of this limitation will disappear: see the discussion in Section 7, below.

[101] The judgment of Oliver J. in *Re Halt Garage (1964) Ltd* [1982] 3 All E.R. 1016 can be seen as supporting this (shareholders approving directors' remuneration).
[102] *Hogg v. Cramphorn Ltd* [1967] Ch. 254; *Bamford v. Bamford* [1970] Ch. 212 (CA). Also see Section 3.3, above.
[103] See note 98. The transaction will probably also be a breach of the director's fiduciary duty, allowing the company to pursue those remedies if they are more advantageous.
[104] Acknowledging that proof of any loss may be very difficult. Consider, for example, the problems of assessment where there has been a share issue for improper purposes. But, supporting this approach, see *Bishopsgate Investment Management Ltd (in liq) v. Maxwell (No. 2)* [1994] 1 All E.R. 261 (CA); *Knight v. Frost* [1999] B.C.C. 819.
[105] So too might the court: Companies Act 1985 s. 727.
[106] See Section 3.3 above, especially note 44.
[107] Either under the terms of the director's contract or pursuant to the Companies Act 1985 s. 303.
[108] *Regal (Hastings) Ltd v. Gulliver* [1967] 2 A.C. 134n, at pp. 144-5 *per* Lord Russell.
[109] For example, the abuse of power rules can be used against directors who use their powers for the improper purpose of causing the company to enter into contracts designed to benefit the director, although then the claim is against all those instigating the deal on behalf of the company, not simply against the profiting director.
[110] *Bray v. Ford* [1896] A.C. 44, at pp. 51-52 *per* Lord Herschell; *Chan v. Zacharia* (1984) 154 C.L.R. 178, at pp. 198-9 *per* Deane J.
[111] *Bray v. Ford* [1896] A.C. 44, at pp. 51-2 *per* Lord Herschell.
[112] *Lac Minerals v. International Corona Resources Ltd* [1989] 2 S.C.R. 574, [1990] F.S.R. 441; *Boardman v. Phipps* [1967] 2 A.C. 46.
[113] *North-West Transportation v. Beatty* (1887) 12 App. Cas. 589; *Guinness plc v. Saunders* [1990] 2 A.C. 663.
[114] *Peso Silver Mines Ltd (NPL) v. Cropper* [1966] S.C.R. 673, (1966) 58 D.L.R. (2d) 1 (SCt of Canada); *Island Export Finance Ltd v. Umunna* [1986] B.C.L.C. 460; but cf. *Industrial Development Consultants Ltd v. Cooley* [1972] 1 W.L.R. 443; *Regal (Hastings) Ltd v. Gulliver* [1967] 2 A.C. 134n (HL); *Boardman v. Phipps* [1967] 2 A.C. 46.
[115] *Regal (Hastings) Ltd v. Gulliver* [1967] 2 A.C. 134n, at p. 149 *per* Lord Russell. But cf. *Industrial Development Consultants Ltd v. Cooley* [1972] 1 W.L.R. 443.
[116] *Boardman v. Phipps* [1967] 2 A.C. 46, at p. 124 *per* Lord Upjohn. Also see *Chan v. Zacharia* (1984) 154 C.L.R. 178, at p. 199 *per* Deane J.
[117] See, *e.g.*, R. P. Austin, "Fiduciary Accountability for Business Opportunities" in P. D. Finn (ed.), *Equity and Commercial Relationships* (1987, Sydney), ch 6; G. Jones, "Unjust Enrichment and the Fiduciary's Duty of Loyalty" (1968) 86 L.Q.R. 472; *Peso-Silver Mines Ltd v. Cropper* [1966] S.C.R. 673, (1966) 58 D.L.R. (2d) 1 (SCt Canada).
[118] Companies Act 1985 s. 310, although see *Movitex Ltd v. Bulfield* [1988] B.C.L.C. 104.
[119] *Boulting v. ACTAT* [1963] 2 Q.B. 606, at pp. 637-8 *per* Upjohn L.J.; *Birtchnell v. Equity Trustees, Executors & Agency Co.* (1929) 42 C.L.R. 384, at p. 408 *per* Dixon J.; *British American Oil Producing Co. v. Midway Oil Co.* (1938) 82 P. (2d) 1049, at p. 1053 *per* Welch J. Otherwise a wide test of duty prevails: *Cranleigh Precision Engineering Ltd v. Bryant* [1965] 1 W.L.R. 1293.
[120] See, *e.g.*, Companies Act 1985 Table A, art. 85. Although see earlier for the suggestion that the board of directors is, in any event, the appropriate organ. Of course, there may be good policy reasons for interfering with this common law position: see, *e.g.*, the statutory requirements in Companies Act 1985 ss. 320ff (enacting prohibitions on substantial property transactions between a director and the company unless there is full disclosure to the general meeting and it consents to the transaction).
[121] Or a related party, since such parties—if they know of the breach—will take any benefits subject to the equities.
[122] *Erlanger v. New Sombrero Phosphate Co.* (1878) 3 App. Cas. 1218; *P&O Steam Navigation Co. v. Johnson* (1938) 60 C.L.R. 189.
[123] [1927] V.L.R. 134 (Vic. SCt).
[124] Although note that the remedy was described as an indemnity rather than an account of profits.
[125] See Companies Act 1985 ss. 322(3)(a), 322A(3)(a). On the other hand, the *indemnity* provisions (ss. 322(3)(b), 322A(3)(b)), are better seen as having parallels with the issues discussed in Sections 5 and 6 above. Note that the remedy of equitable compensation discussed in these earlier contexts was available against the party who acted as the corporate agent (often defaulting directors constituting the board of directors), not against the third party recipient of the company's assets. In the present fiduciary context, however, the claim is against the third party recipient (again, a defaulting director).
[126] And it is irrelevant that she might have made more or less profit on some alternative deal.

[127] As was done in *McKenzie v. McDonald* [1927] V.L.R. 134, although the court noted that arguments for a different approach might have been, but were not, raised.
[128] [1997] 4 All E.R. 705.
[129] Also see *Canson Enterprises Ltd v. Boughton & Co.* (1991) 85 D.L.R. (4th) 129.
[130] *E.g.*, *Industrial Development Consultants Ltd v. Cooley* [1972] 1 W.L.R. 443.
[131] Perhaps subject to an allowance which appropriately reflects the fiduciary's contribution to the choice and operation of the profit-making venture: *Boardman* v. *Phipps* [1967] 2 A.C. 46 (HL).
[132] *Warman International Ltd* v. *Dwyer* (1995) 182 C.L.R. 554; *Scott* v. *Scott* (1963) 109 C.L.R. 649, at p. 662; *Paul Davies (Aust) Pty Ltd (in liq)* v. *Davies* [1983] 1 N.S.W.L.R. 440; *Australian Postal Corpn* v. *Lutac* (1991) 21 N.S.W.L.R. 584. Also see L. Aitken, "Loan Funds and Trustee's Profit" (1993) 13 *Legal Studies* 371.
[133] It is true that the facts are unlikely to suggest a breach and yet find the profits not attributable, at least in part, to the breach. However, (and in another context) the controversial decision in *Re Tilley's WT* [1967] 1 Ch. 1179 suggests the possibility.
[134] (1995) 182 C.L.R. 554.
[135] As an alternative claim, the Australian company might have elected to sue its director for breach of his duty in managing the company's assets (either at common law for negligence or in equity for lack of bona fides or proper purposes in acting in a way that allowed—or even simply hastened—the cancellation of the company's distributorship). The appropriate remedy would then be either common law damages or equitable compensation to remedy the *losses* suffered by the company as a result of such activity.
[136] This is never a relevant consideration in relation to the remedies of common law damages or equitable compensation, where there is no possibility of a defined damages or compensation fund which might have to be paid over *in specie* to the plaintiff company.
[137] See S. Worthington, *Proprietary Interests in Commercial Transactions* (1996, Oxford) at pp. 161-168 and also "The Proprietary Consequences of Contract Failure" in F. Rose (ed.), *Failure of Contracts: Contractual, Restitutionary and Proprietary Consequences* (1997, Oxford) ch 5.
[138] This is regardless of whether the sale itself would have been specifically enforceable.
[139] But possibly not before repayment, since return of the identified asset is conditional on repayment of the purchase money, and an equitable interest will not arise except to treat as done that which ought to be done: see S. Worthington, *Proprietary Interests in Commercial Transactions* (1996, Oxford) ch 8.
[140] Obviously it is crucial to this analysis that the asset remain identifiable. If it does not, then it is impossible for rescission to have proprietary consequences; in fact, the rescission can then only be effected by way of a "monetary equivalent", discussed earlier.
[141] S. Worthington, "The Proprietary Consequences of Contract Failure" in F. Rose (ed.), *Failure of Contracts: Contractual, Restitutionary and Proprietary Consequences* (1997, Oxford) ch 5, at p. 74.
[142] P. Birks, *An Introduction to the Law of Restitution* (rev'd edn 1989, Oxford) at pp. 378-85.
[143] *E.g. Boardman v. Phipps* [1967] 2 A.C. 46; *A-G Hong Kong v. Reid* [1994] 1 A.C. 324.
[144] See, *e.g.*, R. Goode, "Property and Unjust Enrichment" in A. Burrows (ed.), *Essays on the Law of Restitution* (1991, Oxford) ch 9; R. Goode, "The Recovery of a Director's Improper Gains: Proprietary Remedies for the Infringement of Non-Proprietary Rights" in E. McKendrick (ed.), *Commercial Aspects of Trusts and Fiduciary Obligations* (1992, Oxford) ch 7.
[145] See especially P. Jaffey, "Restitutionary Damages and Disgorgement" [1995] R.L.R. 30, at p. 44.
[146] See the reasoning in *A-G Hong Kong v. Reid* [1994] 1 A.C. 324. Also see R. Goode, "Proprietary Restitutionary Claims" in W. R. Cornish, R. Nolan, J. O'Sullivan and G. Virgo (eds), *Restitution: Past, Present and Future* (1998, Oxford) ch 5; and S. Worthington, "Three Questions on Proprietary Restitution", *ibid*, ch 6, and the references cited therein.
[147] Notwithstanding the proposals in LCR, note 1 above, especially Part 4.
[148] *North West Transportation v. Beatty* (1887) 12 App. Cas. 589, at pp. 593-4, 601; *Regal (Hastings) Ltd v. Gulliver* [1967] 2 A.C. 134n, at p. 150; *Furs Ltd v. Tomkies* (1936) 54 C.L.R. 583, at p. 599. *Queensland Mines Ltd v. Hudson* (1978) 18 A.L.R. 1, (1978) 52 A.L.J.R. 399 (PC) is generally regarded as anomalous, although also see *New Zealand Netherlands Society 'Oranje' Inc v. Kuys* [1973] 1 W.L.R. 1126 (PC).
[149] *Cook v. Deeks* [1916] 1 A.C. 554 (PC).
[150] *North-West Transportation Co. Ltd v. Beatty* (1887) 12 App. Cas. 589 (PC), 593-4 *per* Sir Richard Baggallay; *Burland v. Earle* [1902] A.C. 83 (PC), both without adverting directly to the possibility of any restrictions on a shareholder's power to vote.
[151] *Regal (Hastings) Ltd v. Gulliver* [1967] 2 A.C. 134n, at pp. 139, 150, 157; cf. *Cook v. Deeks* [1916] 1 A.C. 554 (PC); *Menier v. Hooper's Telegraph Works* (1874) 9 Ch. App 350.

[152] Although see *Prudential Assurance Co. Ltd v. Newman Industries (No. 2)* [1981] 1 Ch. 257, at p. 308, suggesting that the directors in *Regal Hastings* could not have forgiven themselves by controlling the votes of the general meeting.
[153] R. Goode, "Proprietary Restitutionary Claims" in W. R. Cornish, R. Nolan, J. O'Sullivan and G. Virgo (eds), *Restitution: Past, Present and Future* (1998, Oxford) ch 5 and the references cited there.
[154] Unless the company's constitution limits its competence in this regard.
[155] Although the traditional view is that release or waiver or exoneration—whichever term is preferred—does not require consideration to be binding where the duty breached is a duty owed exclusively in equity.
[156] See, *e.g.*, *Atwool v. Merryweather* (1867) L.R. 5 Eq. 464n (Page-Wood V-C), where the defaulting directors' votes were ineffective to affirm a voidable transaction (although this could be because the shares were obtained as part of the consideration for the voidable sale).
[157] On the issue of *which* is the appropriate organ, see Section 3.2 above.
[158] In addition, as with other breaches, the court has powers under the Companies Act 1985 s. 727 to relieve defaulting directors of their liability in whole or in part, although *Guinness plc v. Saunders* [1990] 2 A.C. 663 may have severely limited the scope to do this.
[159] But see LCR, note 1 above.
[160] Companies Act 1985 s. 310.
[161] Except under Companies Act 1985 s. 459.