

## NOMINEE DIRECTORS

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Nominee directors lie outside the mainstream of company law doctrine and scholarship. There is only a slight body of case law applying specifically to them and little by way of text-book analysis and scholarly examination.<sup>1</sup> They are not subject to specific statutory regulation. Such formal disregard belies their importance, for the office is widely employed in Australian business and raises some nice questions of legal doctrine and policy. This article seeks to identify these issues and to evaluate the competing regulatory responses which might be made to them.

### I. THE SPECIES OF NOMINEE DIRECTOR

The phrase “nominee director” has no clear meaning. The term is not employed in legislation and courts have been little troubled with problems of definition. In commercial practice, however, the term is often applied to “a person appointed as a director of a company on the understanding that he will represent the interest of some other person or group of persons.”<sup>2</sup> Persons may, of course, be nominated to company boards without being under any obligation or expectation that they will represent their appointor’s interests. Such persons fall outside the conception of a nominee director adopted in this article. Here the term is used to refer to persons

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- 1 Commentary on the topic is contained in H.A.J. Ford, *Principles of Company Law* (4th ed., 1986) 396-398; C. Penman, “Nominee Directors in Hong Kong” (1985) 15 *Hong Kong LJ* 5; A.B. Afterman, *Company Directors and Controllers* (1970) 55-61 and “Directors’ Duties in Joint-Venture and Parent Subsidiary Companies” (1968) 42 *ALJ* 168-171.
- 2 H.A.J. Ford, G.W. Hinde and M.S. Hinde, *Australian Business Dictionary* (1985) 127.

who, independent of the method of their appointment, but in the performance of their office, act in accordance with some understanding, arrangement or status which gives rise to an obligation (in the wide sense) to the appointor.<sup>3</sup>

Typically, such an appointor might be an individual shareholder, a class of shareholders, a major lender to the company, a participant in a corporate joint venture or, less commonly, a group of employees of the company.<sup>4</sup> The understanding may also take a variety of forms, from provisions in the articles formally appointing a director as nominee of another to tacit understandings or mere expectations that a nominee will represent particular interests upon the board.

A distinction has been drawn between "representative" and "independent" nominee directors with the former acting more explicitly as the guardian of the appointor's interests.<sup>5</sup> Thus a "representative" nominee director might be an executive appointed to the board of a subsidiary company with the express purpose of protecting the parent's interests or to the board of a joint venture company to represent the interests of an individual venturer. Other nominees will differ only in the degree of independence they bring to the representation or interpretation of appointor interests. Thus a director might be appointed to a subsidiary company to safeguard minority interests but allowed wide latitude in the exercise of judgment. Perhaps an independent nominee director will merely be expected to report back to the appointor on company affairs, either generally or with respect to some particular transaction. However, if the independent director is to be a nominee director within the definition adopted, he or she will be under an obligation of partisan loyalty.

It is impossible to identify with any precision the incidence of nominee directors and the particular interests which they are appointed to represent. There is no obligation to register nominee appointments or to notify such understandings except as arises under general statutory provisions requiring disclosure of interests which a director has in contracts with his or her company or of offices or property which raise the possibility of conflict with duties as a director.<sup>6</sup> Company articles of association may impose similar

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3 Companies and Securities Law Review Committee, *Nominee Directors and Alternate Directors*, Discussion Paper No. 7, 1987, para. 101.

4 Perhaps the best known instance of formalised nominee representation is the European co-determination structures which ensure employee representation on supervisory or managing boards. For a survey and analysis of those structures see E. Batstone and P.L. Davies, *Industrial Democracy: European Experience* (1976) and Commission of the European Communities, "Employee Participation and Company Structure" (1975) *Bulletin of the European Communities* Supplement 8/75. The merits and implications of the European structures for British industrial and company law systems are examined in Dept of Trade (U.K.), *Report of the Committee of Inquiry on Industrial Democracy* Cmnd 6706, 1977 (Bullock Committee).

5 See note 3 *supra*, paras 102-105.

6 See Companies Code s.228. The term Companies Code will be used throughout this article to refer compendiously to the Companies Act 1981 (Cth) (which is expressed to apply only to the Australian Capital Territory) and the State and Northern Territory statutes applying the Commonwealth Act to the other Australian jurisdictions. This nomenclature follows that of the application statutes; see, e.g., Companies (Application of Laws) Act 1981 (N.S.W.) s.10.

obligations of disclosure but neither body of provisions is addressed specifically to the nominee director and will in most cases not apply to compel disclosure of the fact or terms of the nominee's understanding with the appointor.

## II. THE LANDSCAPE OF THE COMPANY DIRECTOR'S FIDUCIARY OBLIGATION

Our legal system imposes upon directors rigorous obligations of good faith and disinterested conduct towards their company. One element of obligation is the duty to exercise powers and perform functions by reference to director's perception of the interests of the company as a whole. The duty requires directors to consult the interests of the shareholders as a general body and not merely those of a particular section of the membership, an individual shareholder or, much less, an outsider. Accordingly, where directors act solely for the benefit of a single shareholder (even one who holds a majority of the capital or voting rights in the company) they will breach their duties of good faith.<sup>7</sup> In short, directors' allegiance is to the collective interests of members and they are obliged to act impartially in interpreting and advancing those interests.

The second element of fiduciary obligation is the duty to shun engagements which create the real sensible possibility of conflict between personal interest (or another interest which the director is bound to protect) and the director's duty of loyalty to the company.<sup>8</sup> This conflict avoidance obligation is not discharged merely by the director preferring the claims of duty to those of self-interest. Rather, the obligation is prophylactic and requires directors to avoid the occasion of temptation and not merely to resist its thrall. It rests upon the judgment that it is neither wise nor practicable for the law to look for a criterion of liability beyond the fact that duty has been opposed to self interest: "[t]he consequences of such a conflict are not discoverable. Both justice and policy are against their investigation."<sup>9</sup> Indeed, a nineteenth century judge thought that the "safety of mankind" would be put at risk by a rule which made a fiduciary liable only for preferring interest to duty.<sup>10</sup>

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7 See, e.g., *Ngurlu Ltd v. McCann* (1953) 90 CLR 425; *Greenhalgh v. Arderne Cinemas Ltd* [1951] Ch 286, 291.

8 A seminal decision is *Aberdeen Railway Co. v. Blaikie Bros* (1854) 1 Macq. 461; [1843-60] All ER 249. For a modern restatement (albeit not decided with respect to company directors) see *Phipps v. Boardman* [1967] 2 AC 46.

9 *Furs Ltd v. Tomkies* (1936) 54 CLR 583, 592 per Rich, Dixon and Evatt JJ.

10 *Parker v. McKenna* (1874) LR 10 Ch App 96, 124 per James L.J. A century later another judge suggested that "[i]n the nuclear age [this assessment] may perhaps seem something of an exaggeration, but, nonetheless, it is eloquent of the strictness with which ... courts of the highest authority have always applied this rule." (*Industrial Development Consultants Ltd v. Cooley* [1972] 1 WLR 443, 452 per Roskill J.)

Nominee directors therefore occupy a most delicate position. At first sight appointment of a nominee director appears inconsistent with the director's duties of loyalty and of conflict avoidance. Thus, is not the duty of loyalty to general shareholder interests compromised where a nominee director is appointed for the very purpose of acting partially, whether by subordinating the interests of the general body of members to those of the appointor or by identifying company interests with those of the appointor? As to the conflict avoidance obligation, is it likely (if not inevitable) that the nominee's agreement or understanding with the appointor will create either a personal stake or a duty to the appointor in possible conflict with the duty to advance general shareholder interests? The Companies Code contains a provision that the removal of a director appointed to represent the interests of a particular class of share or debenture holders does not take effect until a successor has been appointed.<sup>11</sup> This provision implies that the appointment of a nominee director is not in itself unlawful but the Code is silent as to the adjustment of conflicting loyalties. How that adjustment should be made is the central concern of this article.

### III. THE DISTINCTIVE AUSTRALIAN CASE LAW ON THE NOMINEE DIRECTOR'S DUTY OF LOYALTY

In the 1960s Sir Kenneth Jacobs, sitting as a single judge in the Supreme Court of New South Wales, delivered two judgments which lent legitimacy to the practice of appointing nominee directors and relaxed the duties of good faith applying to them. They are the only Anglo-Australian decisions which pay more than passing attention to the duties of nominee directors.

In *Levin v. Clark*<sup>12</sup> Levin purchased the controlling shareholding in a proprietary company and simultaneously mortgaged the shares to the vendor to secure payment of the purchase price. The company's articles of association had named Clark and Rappaport as governing directors and conferred extensive powers upon them. Pursuant to the sale agreement the articles were amended to make the powers of Clark and Rappaport exercisable only in the event of Levin's default under the mortgage agreement. The articles and agreements did not expressly identify Clark and Rappaport as nominees of the mortgagee/vendor and did not specify any special duties or loyalties for them (apart, of course, from their suspended offices as governing directors). However, it was evident that they retained those offices to protect the interests of the mortgagee in the event of Levin's default under the mortgage.

Levin subsequently defaulted under the mortgage and Clark and Rappaport proceeded to exercise their powers as governing directors. Levin

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11 Companies Code s. 225(1).

12 [1962] NSW 686.

challenged their assumption of power and certain resolutions which they purported to pass, upon the grounds that they were acting solely in the interests of the mortgagee and not in the interests of the company. Jacobs J. concluded that Clark and Rappaport had acted primarily in the interests of the mortgagee once they resumed their powers as governing directors. He said:

[h]owever, I consider that it was permissible for them so to act. It is of course correct to state as a general principle that directors must act in the interests of the company... However, that leaves open the question in each case — what is the interest of the company? It is not uncommon for a director to be appointed to a board of directors in order to represent an interest outside the company — a mortgagee or other trader or a particular shareholder. It may be in the interests of the company that there be upon its board of directors one who will represent these other interests and who will be acting solely in the interests of such a third party and who may in that way be properly regarded as acting in the interests of the company as a whole. To argue that a director particularly appointed for the purpose of representing the interests of a third party, cannot lawfully act solely in the interests of that third party, is in my view to apply the broad principle, governing the fiduciary duty of directors, to a particular situation, where the breadth of the fiduciary duty has been narrowed, by agreement amongst the body of the shareholders. The fiduciary duties of directors spring from the general principles, developed in courts of equity, governing the duties of all fiduciaries — agents, trustees, directors, liquidators and others — and it must be always borne in mind that in such situations the extent and degree of the fiduciary duty depends not only on the particular relationships, but also on the particular circumstances. Among the most important of these circumstances are the terms of the instrument governing the exercise by the fiduciary of his powers and duties and the wishes, expressed directly or indirectly, by direction, request, assent or waiver, of all those to whom the fiduciary duty is owed.<sup>13</sup>

While the articles of association in *Levin v. Clark* did not make explicit Clark and Rappaport's role as representatives of the mortgagee, it was not difficult to infer that their primary duty was to protect the mortgagee's interests in the event of default. Two years later similar questions came before Jacobs J. in circumstances where the articles were less explicit in their attempt to tailor the general fiduciary doctrine to particular circumstances.

The decision in *Re Broadcasting Station 2GB Pty Ltd*<sup>14</sup> arose out of the transfer of control of the operator of Sydney broadcasting station 2GB in 1964. For some years the issued capital of Broadcasting Station 2GB Pty Ltd (2GB) had been held as to 45% by Broadcasting Associates, as to 14% by the Fairfax group of companies and the balance by various minority shareholders. The 2GB articles contained a provision entitling the Fairfax group to board representation by one director but was silent as to other nominee appointments. Of the other six 2GB directors, however, four were nominees of Broadcasting Associates.

Fairfax acquired control of Broadcasting Associates and directed the latter's nominees upon the 2GB board to resign. When two refused Fairfax acted to appoint sufficient additional directors to ensure a majority of its nominees on the board. One of the minority directors petitioned for orders

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<sup>13</sup> *Id.*, 700-701.

<sup>14</sup> [1964-5] NSW 1648.

that the affairs of 2GB were being conducted in an oppressive manner. (The oppression remedy, now contained in Companies Code section 320, empowers the Supreme Court to make a wide range of remedial orders which are discussed further below.) The alleged oppression lay in (1) the steps taken to secure the appointment of a majority of Fairfax directors on the board, being steps taken solely in the interests of the Fairfax companies, and (2) the withholding of information concerning negotiations which the Fairfax interests were conducting with the Commonwealth government to preserve the 2GB licence after the change in control of Broadcasting Associates.

Jacobs J. concluded that the question whether the Fairfax conduct was oppressive should be resolved by reference to doctrines defining the duties of directors and majority shareholders. Describing the steps taken by Fairfax to reconstitute the 2GB board, Jacobs J. said:

[Such conduct] is not reprehensible unless it can also be inferred that the directors, so nominated, would so act even if they were of the view that their acts were not in the best interests of the company. This is not a conclusion which can lightly be reached and I see no evidence in the case upon which I can reach that conclusion. It may well be, and I am inclined to regard it as the fact, that the newly appointed directors were prepared to accept the position that they would follow the wishes of the Fairfax interests without a close personal analysis of the issues. I think that at the board meetings ... that is what they did, but I see no evidence of a lack in them of a bona fide belief that the interests of the Fairfax company were identical with the interests of the company as a whole. I realize that, upon this approach, I deny any right in the company as a whole to have each director approach each company problem with a completely open mind, but I think that to require this of each director of a company is to ignore the realities of company organization. Also, such a requirement would, in effect, make the position of a nominee or representative director an impossibility.<sup>15</sup>

On this view, the nominees' conduct was proper "so long as they bona fide believed that the Fairfax companies would act in the interests of the company as a whole."<sup>16</sup> The words quoted suggest that nominee directors will breach their duty only if they knowingly sacrifice company interests for those of their appointor. To require a higher standard of nominee loyalty would be "to ignore the realities of company organization [and] ... make the position of a nominee or representative director an impossibility."<sup>17</sup>

The essential heterodoxy of the two decisions is illustrated by another decision of the Supreme Court of New South Wales just three years after the 2GB case. In *Bennetts v. Board of Fire Commissioners of New South Wales*<sup>18</sup> the loyalties in question here were not those of company directors but of members of a statutory corporation charged with responsibility for fire prevention and control. The board comprised representatives of interested groups — of local government, insurance companies and firemen. The board obtained legal advice as to whether it should appeal from an industrial determination affecting its firemen. The firemen's representative on the

<sup>15</sup> *Id.*, 1663.

<sup>16</sup> *Ibid.*

<sup>17</sup> *Ibid.*

<sup>18</sup> (1967) 87 WN (NSW) 307.

board was refused access to the advice when he declined to give an undertaking not to disclose its contents to the union. He sought unconditional access to the advice. Street J. (as he then was) said:

[a] board member must not allow himself to be compromised by looking to the interests of the group which appointed him rather than to the interests for which the board exists. He is most certainly not a mere channel of communication or listening post on behalf of the group which elected him...[A view] is apparently held that, because a board member is appointed or elected by a particular group, he owes some overriding obligation or duty to the group which has conferred upon him his status as a member. The error inherent in this view must be exposed... It is entirely foreign to the purpose for which this or any other board exists to contemplate a member of the board being representative of a particular group or a particular body. Once a group has elected a member he assumes office as a member of the board and becomes subject to the overriding and predominant duty to serve the interests of the board in preference, on every occasion upon which any conflict might arise, to serving the interests of the group which appointed him. With this basic proposition there can be no room for compromise.<sup>19</sup>

Street J. acknowledged the bona fides of the representative's perception that he was subject to conflicting loyalties and that he owed the higher duty to his electors. This bona fides notwithstanding, Street J. concluded that "[t]he principle governing the manner in which that conflict should be resolved is that the overriding duty is the duty to the board, and that that duty must not be compromised in any degree whatever."<sup>20</sup> The judge made no reference to the recent decisions of Jacobs J. imposing quite different standards of loyalty upon nominee directors of trading companies.

#### IV. COMPARATIVE APPROACHES TO STANDARDS OF NOMINEE DIRECTOR LOYALTY

The decisions in *Levin v. Clark* and the *2GB* case generally stand alone. They do not appear to have been considered in any reported judicial decision in the United Kingdom or Canada.<sup>21</sup> They run counter to the grain of the general fiduciary principle applied to company directors in those jurisdictions and in the United States whose corporation law does not recognise any special doctrine for nominee directors.<sup>22</sup> Consider first the appointment of nominee directors. The state of United Kingdom doctrine is reflected in *Boulting v. Association of Cinematograph, Television and Allied Technicians*<sup>23</sup> where Lord Denning M.R. referred to the appointment of a nominee director, "that is, a director of a company who is nominated by a large shareholder to represent his interests". He said:

19 *Id.*, 310-311.

20 *Id.*, 313.

21 They have, however, been followed in a New Zealand decision *Berlei Hestia (NZ) Ltd v. Fernyhough* [1980] NZLR 150, discussed below.

22 See e.g. the discussion in H.G. Henn and J.R. Alexander, *Laws of Corporations* (3rd ed., 1983) 625-663 and W.L. Cary and M.A. Eisenberg, *Corporations* (5th ed., 1980) Ch.6.

23 [1963] 2 QB 606.

[t]here is nothing wrong in it. It is done every day. Nothing wrong, that is, so long as the director is left free to exercise his best judgment in the interests of the company which he serves. But if he is put upon terms that he is bound to act in the affairs of the company in accordance with the directions of his patron, it is beyond doubt unlawful.<sup>24</sup>

Similarly, in *Lindgren v. L. & P. Estates Ltd*<sup>25</sup> Harman L.J. considered it “quite irrelevant” to the liability of a director of a subsidiary company that the director may have been appointed to represent the interests of its parent company.

The United Kingdom case law recognises a second constraint upon the appointment of nominee directors. Where the appointor is in commercial competition with the company or in other respects the interests of the company and the appointor conflict, the nominee’s appointment may raise such a conflict as to inevitably place the director in breach of duty. In *Scottish Co-operative Wholesale Society Ltd v. Meyer*<sup>26</sup> the articles of a company empowered its parent company to nominate three out of five directors to act as nominees of the parent. The parent nominated three of its own directors. Lord Denning M.R. said of their appointment:

[s]o long as the interests of all concerned were in harmony, there was no difficulty. The nominee directors could do their duty by both companies without embarrassment. But, so soon as the interests of the two companies were in conflict, the nominee directors were placed in an impossible position... It is plain that, in the circumstances, these three gentlemen could not do their duty by both companies, and they did not do so.<sup>27</sup>

Conflict arose for the nominee directors when the parent company decided to dispense with the subsidiary and to set up its own department to conduct parallel activities. The nominee directors actively assisted in this policy of running down the subsidiary. An order was made under the oppression provision for the compulsory purchase of the minority shareholdings at a price calculated on the basis that the oppressive conduct had not taken place.

Because of such conflicts the principal United Kingdom association of company directors “deprecates the appointment of nominee directors if the primary motive of the nominator is simply to ensure that his own interests are preferred above others.”<sup>28</sup> Adopting a Burkean distinction a director should act “as a representative of all shareholders, not as a delegate of all shareholders.”<sup>29</sup> Accordingly, investor interest in board representation “is best accomplished by the investor exerting his influence to ensure that the members of the company as a whole appoint appropriate directors.”<sup>30</sup>

24 *Id.*, 626. Similarly, the Bullock Committee’s proposals for employee representation upon the boards of large British companies were drawn upon the basis that the employee director must be “free to express his opinions and to reach his own conclusions about which policies will work for the greater good of the company, not a delegate, told how to vote by his constituents” (Dept of Trade (U.K.), note 4 *supra*, 85).

25 [1968] Ch 572, 594.

26 [1959] AC 324.

27 *Id.*, 366-367.

28 Institute of Directors, *Nominee Directors* (Guide to Boardroom Practice No. 8, 1985) para. 1.

29 *Id.*, para. 9.

30 *Id.*, para. 2.



If we assume the validity both of the nominee's appointment and of any understanding with the appointor, to what extent may the director identify company interests with those of the appointor? Is the director's obligation to act bona fide in the interests of the company as a whole qualified in its application to nominee directors to enable them to honour their understandings with appointors? Statements in several United Kingdom cases suggest that the fiduciary obligation is in no way compromised and that nominee directors owe the same duty of loyalty to their company as other directors. Thus they will breach their duty to the company if they subordinate its interests to those of their patron, even if this subordination merely takes the form of passive inactivity in the face of improper conduct by the patron.<sup>31</sup>

The only other reported decision in Australasia or the United Kingdom which has canvassed an attenuated standard of loyalty for nominee directors is that of the Supreme Court of New Zealand in *Berlei Hestia (NZ) Ltd v. Fernyhough*.<sup>32</sup> The capital of a New Zealand company was held, as to 40%, by an Australian company and as to the balance by a group of New Zealand shareholders. The company's articles gave the Australian and New Zealand shareholders equal representation upon the board. Each group nominated three directors to represent its interests. No provision was made for a casting vote. The New Zealand company began to export its product to Australia in direct competition with its Australian shareholder. The Australian directors claimed that the New Zealand directors used this development as a pretext to exclude them from management participation in the company. In the course of determining the directors' rights of access to corporate information, Mahon J. attempted to reconcile the traditional doctrine of undivided director loyalty with the attenuated standard adopted by Jacobs J. He said:

[i]t was strongly contended by [counsel for the New Zealand company] that the interests of the Australian company as a minority shareholder could be adequately preserved by disclosure to that company of the general financial position and trading results of the New Zealand company. But I am afraid I cannot agree. Notwithstanding that the Australian directors are the nominees of the Australian company, they nevertheless have responsibilities to the whole body of shareholders... But despite the width of that proposition, there have been attempts to bring this theoretical doctrine of undivided responsibility into harmony with commercial reality, upon the basis that when Articles are agreed upon whereby a specified shareholder or group of shareholders is empowered to nominate its own directors, then there may be grounds for saying that in addition to the responsibility which such directors have to all shareholders as represented by the corporate entity, they may have a special responsibility towards those who nominated them. Such a view proceeds on the basis that the Articles were so constructed with the intent and belief that the institution of such a special responsibility towards one class of shareholders was conducive to the interests of the company as a whole. For an illustration of this line of thinking I refer to the dicta of Jacobs J. in *Levin v. Clark*.. and in *Re Broadcasting Station 2GB Pty Ltd*.. In the present case this business undertaking, stripped of its corporate shell, is a trading partnership between two organisations operating in

31 See *Boulting v. Association of Cinematograph, Television and Allied Technicians* note 22 *supra*, 627; *Scottish Co-operative Wholesale Society Ltd v. Meyer* note 25 *supra*, 367.

32 Note 21 *supra*.

different countries. They agreed, when the company was incorporated, that each partner nominate three directors, and they impliedly agreed, as the Articles show, that one class of directors was at liberty to bring the Board's functions to a stand-still when a disagreement arose, and that disagreement would almost certainly have its origin in a dispute between the two sets of shareholders. These consequences were all well known to the incorporators when the Articles were drawn. As a matter of legal theory, as opposed to judicial precedent, it seems not unreasonable for all the incorporators to be able to agree upon an adjusted form of fiduciary liability, limited to circumstances where the rights of third parties vis-a-vis the company will not be prejudiced. The stage has already been reached, according to some commentators, where nominee directors will be absolved from suggested breach of duty to the company merely because they act in furtherance of the interests of their appointors, provided that their conduct accords with a bona fide belief that the interests of the corporate entity are likewise being advanced.<sup>33</sup>

## V. SHOULD THE NOMINEE DIRECTOR BE PERMITTED AN ATTENUATED STANDARD OF LOYALTY?

The general doctrine of fiduciary loyalty is startling in its rigour. James L.J. thought that the "safety of mankind" would be put at risk by a less exacting standard of self denial.<sup>34</sup> In *Keech v. Sandford* the trustee who had been absolutely denied renewal of a lease for his beneficiary was himself "the only person of all mankind who might not have the lease".<sup>35</sup> The strictness of fiduciary doctrines may, however, be relaxed in their application to company directors. Thus there are dicta acknowledging that articles of association may be so framed as to permit directors to act in a way which would otherwise offend their duties of loyalty.<sup>36</sup> Similarly, the conflict avoidance obligation may be modified by provisions in articles which permit a director to have an interest in a contract with the company<sup>37</sup> or to derive a profit from office.<sup>38</sup> In *Levin v. Clark* and the *Berlei Hestia* case the courts placed considerable weight upon provisions in the articles for the appointment of nominee directors as justifying an attenuated duty of loyalty to general shareholder interests.

Should company law compromise the standard of loyalty expected of nominee directors? If so, should the right of a nominee director to have special regard for the interests of the appointor depend upon whether the memorandum or articles of association make special provision for the appointment of the nominee and the modification of his or her duties? The Australasian case law does not make attenuation conditional upon express

33 *Id.*, 165-166.

34 Note 10 *supra*.

35 (1726) Sel Cas Ch 61, 62; 25 ER 22; *cf. Ex parte James* (1803) 8 Ves Jun 337; 32 ER 385 and *Regal (Hastings) Ltd v. Gulliver* [1967] 2 AC 134n.

36 See *Whitehouse v. Carlton Hotel Pty Ltd* (1987) 61 ALJR 216, 217.

37 See, e.g., *Imperial Mercantile Credit Association v. Coleman* (1871) LR 6 Ch App 588, 567-568 and *Peninsular & Oriental Steam Navigation Co. Ltd v. Johnson* (1938) 60 CLR 198, 234-236.

38 See, e.g., *Re Northern Rivers Finance Co. Pty Ltd (in liq.)* (1979) 4 ACLR 545, 551 and *Guinness plc v. Saunders (No. 2)* (1987) 3 BCC 520. Companies Code s. 237 fixes somewhat uncertain limits to the permissible attenuation of duty through the memorandum or articles; see *Movitex Ltd v. Bulfield* (1986) 2 BCC 99, 403.

provision in the memorandum or articles. In the *2GB* case the appointment of all but one of the nominee directors was made dehors the articles and the attenuation of their duty was not attributable to special provision there.<sup>39</sup> Further, the articles in *Levin v. Clark* and the *Berlei Hestia* case, although they provided for the appointment of nominee directors, did not expressly state that the directors were nominees for another or modify the duties applicable to them. There appears, therefore, little scope for rationalising the attenuated standard of loyalty in the cases as depending upon special provision in the articles, although such provision undoubtedly assists in justifying the compromise of loyalty. In no case did the attenuation turn upon special corporate consent outside the memorandum or articles such as through a resolution of shareholders in general meeting.

Under the legal rules for corporate governance, the fiduciary obligations of directors provide the principal incentive for the disinterested exercise of powers to general corporate advantage. This incentive is secured by the complex of fiduciary duties enjoining directors to fidelity to shareholder interests and against exploitation of office for personal or sectional gain. The writer suggests that a case has not been made out for dismantling this protective structure. It may be the commercial reality that some directors will owe their appointment to a particular individual or group and will conceive their primary loyalty as due to them. Where these appointors do not beneficially own the whole of the equity of the company, minority interests will generally be ill served by this displacement of loyalty. It is not clear, however, why the law should lend its sanction to this erosion of minority rights. The compromised standard of loyalty is also inconsistent with the received legal model of board structure which conceives the board as a collectivity of individuals not representative of particular sectional interests but united by a common allegiance to the general interest. Other doctrines relating to the governance of the corporation proceed upon this assumed model. To dismantle the model is to weaken an accountability structure which is fundamental to the protection of shareholder interests. Such a step should not be taken without substituting other protective mechanisms.

If some attenuation of nominees' loyalty is to be permitted it should at the least proceed from an expression of corporate consent — by the modification of duty through the memorandum or articles or by special resolution

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39 See note 14 *supra*. Similarly, in the *Scottish Co-operative Wholesale Society* case, note 25 *supra*, the nominee directors who were held to the general fiduciary standard were appointed pursuant to special provision in the articles.

releasing a particular nominee director to partial loyalty.<sup>40</sup> Both devices, however, are at considerable cost to the integrity of the general loyalty rule.

If, however, nominee directors are to be permitted some latitude for partisan loyalties (whether conditional upon some expression of corporate consent or otherwise), how far should such latitude extend? Specifically, should nominee directors be permitted to identify company interests exclusively with those of their appointor? The *2GB* case suggests that nominee directors may follow the wishes of their appointor unless by doing so they knowingly sacrifice company interests to those of the appointor. Acceptance of a compromised standard of loyalty need not extend so far. An intermediate formulation is that adopted in the Companies Code 1963 of Ghana which empowers representative directors to give “special, but not exclusive, consideration” to the interests of their appointor.<sup>41</sup> Such a formulation provides a more secure and principled adjustment to the interests of the appointor and the general membership than a rule which attaches liability only to the wilful sacrifice of company interests to those of the appointor. It is suggested that, if standards of loyalty may be relaxed for nominee directors, that attenuation extend no further than the Ghanaian formulation.

If the duties applying to nominee directors are to be relaxed, a definition will need to be adopted to identify those directors who should receive the benefit of the dispensation. Further, whether or not the fiduciary standard is attenuated for nominee directors, it is undesirable that a director’s partisan loyalties should not be publicly disclosed. If the director’s primary allegiance is not to general shareholder interests, this fact will usually be material to the judgment of other directors, shareholders and persons dealing with the company. The Companies Code requires a director to disclose to the board any office held or property possessed which might create duties or interests in conflict with those as director.<sup>42</sup> The terms of this obligation, however, are not such as to engage the generality of nominee — appointor understandings. Respect for the prophylactic ideology underlying the fiduciary rules and for the reasonable expectations of the groups mentioned requires public disclosure of a director’s status as nominee for another, the identity of that

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40 There are, however, doubts surrounding the permissible scope of each resolution. First, it is not clear whether a special resolution relaxing the standards of loyalty of directors who are nominees would fall within the prohibition of Companies Code s.237 upon provisions in articles exempting directors from or indemnifying them against liability for breach of duty or trust. Second, the resolutions are susceptible to challenge as a fraud upon the minority, *i.e.*, for breach of the general law obligation of shareholders to use voting power bona fide for the benefit of the company as a whole. The scope of each limitation is discussed in P. Redmond, *Companies and Securities Law* (1988) 429-430, 433-463.

41 Companies Code 1963 s.203(3) (Ghana). The provision derives from reforms proposed by Professor L.C.B. Gower as Royal Commissioner: see *Final Report of the Commission of Enquiry into the Working and Administration of the Present Company Law of Ghana* (1961), Appendix 1, 145-146.

42 s.228(5).

other person and the nature of any commitment which the nominee has undertaken. Ideally, disclosure should be made in the register which companies are required to maintain of their directors, principal executive officer and secretaries.<sup>43</sup> The register is open to inspection by members without charge and by others upon payment of a sum not exceeding that prescribed.<sup>44</sup> These particulars should also be disclosed in the company's annual return which is open to public inspection.<sup>45</sup> Alternatively, disclosure might be effected through a specific register of nominee directors along the lines of the register of disqualified company directors and officers maintained by the National Companies and Securities Commission.<sup>46</sup>

## VI. SOME RELATED ISSUES

If the duties of nominee directors are to be reappraised, some ancillary doctrines will also require review. The following notes identify such issues and briefly consider consequential reforms.

### 1. *The Proper Scope of a Nominee Director's Commitments*

It is a basic rule of company law that directors should maintain, and bring to bear, an independent judgment in the exercise of powers. The rule is an application of the general equitable obligation requiring fiduciaries to shun the possibility of conflict between duty and interest. Thus, in the absence of an empowering provision in the articles, directors may not delegate their discretionary powers to another group or individual<sup>47</sup> or impair their independence of judgment by binding themselves as to the future exercise of discretionary powers.<sup>48</sup> Although there is little authority directly on point, the rule undoubtedly prohibits directors from binding themselves, by agreement with each other or with outsiders, as to how they shall vote as directors. Thus, in *Boulting v. Association of Cinematograph, Television and Allied Technicians* Lord Denning M.R. said:

[i]t seems to me that no one, who has duties of a fiduciary nature to discharge, can be allowed to enter into an engagement by which he binds himself to disregard those duties or to act inconsistently with them. No stipulation is lawful by which he agrees to carry out his duties in accordance with the instructions of another rather than on his own conscientious judgment; or by which he agrees to subordinate the interests of those whom he must protect to the interests of someone else. Suppose a Member of Parliament should be in the pay of some outside body, in return for which he binds himself to vote as he is directed to do. The agreement would clearly be void as against public policy.<sup>49</sup>

43 Companies Code s 238.

44 s. 238(5).

45 See Companies Code s.263(1) and Companies Regulations, Sched.2, Form 66, cl.6.

46 The register is kept pursuant to Companies Code s.238A.

47 See, e.g., *Re Leed's Banking Co., Howard's Case* (1866) LR 1 Ch App 561 and *Re County Palatine Loan & Discount Co., Cartmell's Case* (1874) LR 9 Ch App 691.

48 Not every fetter upon the future exercise of power will offend the rule; see *Thorby v. Goldberg* (1964) 112 CLR 597.

49 Note 22 *supra*, 626.

Any such an agreement by directors would be invalid if the directors thereby assumed obligations to act “in a specified manner to be decided by considerations other than [their] own conscientious judgment at the time as to what is best in the interests of [their company]”.<sup>50</sup> Thus in *Clark v. Workman*<sup>51</sup> directors were empowered by the articles to approve the transfer of a controlling interest in the company. Several had promised a potential purchaser to use their best endeavours to get the controlling interest into his hands. The board decision honouring this promise was set aside. These directors had, by this fetter upon their judgment, disqualified themselves from acting bona fide in the company’s interests.

In practice, however, it may often be assumed that the nominee will retain office as director only so long as he or she acts in accordance with the wishes of the appointor. In these circumstances, the boundaries of this fetter rule may be thought uncertain and its application to understandings between nominee and appointor which fall short of strict legal commitment unclear. It is desirable that the law should attempt to define with some precision the scope of the commitments which the nominee may properly make to his or her appointor. How should that definition be expressed? Specifically, should the nominee be permitted to bind him or herself in advance to act on the direction of the appointor?

The Australasian cases supporting a compromise of nominees’ duties have not addressed the permissible scope of commitments to appointors. The writer suggests that the general law principle is well founded and should not be compromised in its application to nominee directors. Even if the nominee director is to be permitted to pay special regard to an appointor’s interests it does not thereby follow that the nominee should be permitted to bind the future exercise of discretionary powers. Arguably, compromise of the fetter rule is a more egregious inroad upon fiduciary ideology than the licence in a particular case to place appointor interests before those of the general body of shareholders. It is not clear what commercial expectation requires for its vindication the dismantling of a doctrine so central to the legal model of corporate governance.

## 2. *The Personal Liability of the Nominee Director*

Company directors are personally liable for breaches of duty to the company. The question of breach will often turn upon the state of knowledge of the individual director. If an appointor uses a nominee director in the manner of a puppet — to do the appointor’s bidding but with little appreciation of the significance of the acts he or she is performing — how is the nominee director’s understanding of the transaction to be assessed? In *Selangor United Rubber Estates Ltd v. Cradock (No.3)*<sup>52</sup> nominee directors

50 *Osborne v. Amalgamated Society of Railway Servants* [1909] 1 Ch 163, 187 per Fletcher Moulton L.J.

51 [1920] 1 Ir R 107.

52 [1968] 1 WLR 1555.

were sued for misapplication of company funds. They denied any knowledge of the impropriety of a scheme which, it appeared, they executed as the uncomprehending instruments of their appointor. The Divisional Court held that a director who acts in a transaction on the direction of a third party is fixed with that person's knowledge of the nature of that transaction and may not rely upon his or her own limited appreciation. The directors were accordingly liable to restore the misapplied funds.

Does this doctrine work unfairly against nominee directors, exposing them to liability on the basis of knowledge possessed by the appointor but withheld from the nominee? The writer suggests, however, that it is quite reasonable that the nominee director should be liable on this basis. The insulation of nominee directors from knowledge possessed by their appointor would provide a dubious incentive for the proliferation of nominees. By appointment of a nominee director who may lawfully pay special regard to appointor interests, the appointor secures the principal economic advantages of directorship but without direct exposure to the liability rules securing faithful fiduciary service.<sup>53</sup> If the nominee director is exposed to those rules only on the basis of knowledge he or she actually possesses, the route to evasion of liability mechanisms through puppet directors is effectively flagged. The legitimacy of the corporate model of business organisation lies in the accountability of those who wield power under it. The step should be taken reluctantly which secures the directorial advantages without exposure to the corresponding liabilities.

### 3. *The Appointor's Liability*

There are several potential bases of appointor liability for the nominee's defaults. Liability may arise under either limb of the rule in *Barnes v. Addy*.<sup>54</sup> Under the first limb, an appointor who receives company property from a nominee will hold it on trust for the company where he knows, or the circumstances are such that he ought to know, that the nominee is acting in breach of duty. In the *Selangor United Rubber Estates* case the appointor was liable upon this basis.

The second limb of the rule may apply where the appointor does not receive company property but nonetheless participates in the nominee's misapplication. The appointor will be liable where he or she knowingly assists a nominee director in a dishonest design on the nominee's part to misappropriate assets or funds of the company.<sup>55</sup> This limb has potentially wide application where the nominee has acted as mere cipher for the appointor in the disposition of corporate assets. The limb may also apply where the nominee has acted independently of the appointor but where the latter has some apprehension of the nominee's fraudulent application of

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<sup>53</sup> The appointor's liability for acts of the nominee is discussed in the following section.

<sup>54</sup> (1874) LR 9 Ch App 244.

<sup>55</sup> For an application of the limb to company transactions see *Belmont Finance Corp. v. Williams Furniture Ltd (No. 2)* [1980] 1 All ER 393, 405-406.

corporate assets. The degree of apprehension which will attract liability under the second limb was described by Gibbs J. (as he then was) in *Consul Development Pty Ltd v. D.P.C. Estates Pty Ltd*:<sup>56</sup>

[i]t may be that it is going too far to say that a stranger [such as the appointor] will be liable if the circumstances would have put an honest and reasonable man on inquiry, when the stranger's failure to inquire has been innocent and he has not wilfully shut his eyes to the obvious. On the other hand, it does not seem to me to be necessary to prove that a stranger who participated in a breach of trust or fiduciary duty with knowledge of all the circumstances did so actually knowing that what he was doing was improper. It would not be just that a person who had full knowledge of all the facts could escape liability because his own moral obtuseness prevented him from recognizing an impropriety that would have been apparent to an ordinary man.

In the same case Stephen J. (with whom Barwick C.J. agreed) said that if the stranger "knows of facts which themselves would, to a reasonable man, tell of fraud or breach of trust", he may be liable under the second limb as he would be if he had "consciously refrained from enquiry for fear lest he learn of fraud".<sup>57</sup>

Another basis of appointor liability may arise under the extended definition of "director" in Companies Code section 5(1). The definition applies in the Code, subject to a contrary intention appearing, to include "any person in accordance with whose directions or instructions the directors of the corporation are accustomed to act". Whether the definition has the effect of extending the Code's provisions on directors to a nominee's appointor has yet to be decided. In particular, it is not clear that the statutory definition would apply if only a minority of the board were nominees.<sup>58</sup> If the statutory definition does apply to a nominee director and his or her appointor it will apply only for the purposes of the Code and will not extend the judge-made principles of fiduciary liability to an appointor. However, it appears that the appointor would be thereby exposed to the directorial obligations under Code section 229 to act honestly and with reasonable care and diligence.<sup>59</sup>

#### 4. *The oppression remedy*

Early cases on the oppression remedy in both the United Kingdom and Australia concerned the conduct of nominee directors. We have seen that in 1959 the House of Lords in the *Scottish Co-operative Wholesale Society* case held that the conduct of nominee directors in preferring the interests of their appointor to those of minority shareholders was oppressive conduct within the section. Further, (as we have also seen) in the *2GB* case the behaviour of the nominees in leaving to their appointors the conduct of licence negotiations did not amount to oppression under the Uniform Companies Act provision. Jacobs J. found no evidence of a lack in the nominee directors of a bona fide belief of identity between the company's interests and those of

<sup>56</sup> (1975) 132 CLR 373, 398.

<sup>57</sup> *Id.*, 412.

<sup>58</sup> See Afterman, *Company Directors and Controllers*, note 1 *supra*, 40-44.

<sup>59</sup> *Corporate Affairs Commission v. Drysdale* (1979) 57 ALJR 144.



the appointor, although he was in any event prepared to absolve them from a "close personal analysis of the issues". Since the directors had left the conduct of the particular negotiations to their appointors, the focus in the oppression suit shifted to their conduct of those negotiations and whether they had preferred their own interests to those of shareholders generally. Had the company been constituted with an independent board, the shareholders would have been insulated from such an inquiry. In the circumstances, however, their conduct was held not to amount to oppression.

In the *2GB* case Jacobs J. adopted the definition of "oppressive" conduct applied in earlier case law, viz., conduct which is "burdensome, harsh and wrongful".<sup>60</sup> In 1983 the oppression provision in Companies Code section 320 was amended to provide for wider grounds of relief. The Supreme Court, on the application of a member, may now make remedial orders if it is of the opinion that the affairs of a company are being conducted in a manner that is "oppressive" or "unfairly prejudicial" to, or "unfairly discriminatory" against a member or in a manner that is contrary to the interests of the members as a whole (section 320(1)(a)). Parallel provisions apply in relation to an act or omission by or on behalf of the company or a resolution of the company (section 320(1)(b)). The orders that may be made under the section are also cast in wider terms. The newly introduced expressions "unfairly prejudicial to" and "unfairly discriminatory" against clearly contemplate conduct of greater amplitude than was previously embraced by the term "oppressive" and accordingly have widened the categories of conduct in respect of which a shareholder is entitled to complain.<sup>61</sup>

While the question has yet to arise for decision, it may be doubted whether the *2GB* or Scottish Co-operative directors would be immune from an order under the revised terms of section 320. Proceedings under the section usually require the court to examine the policy of a course of action pursued by those in control of a company to determine its fairness or unfairness in the particular circumstances of the company. In *Thomas v. H.W. Thomas Ltd* the New Zealand Court of Appeal described the fairness determination under the section thus:

[f]airness cannot be assessed in a vacuum or simply from one member's point of view. It will often depend on weighing conflicting interests of different groups within the company. It is a matter of balancing all the interests involved in terms of the policies underlying the companies legislation in general and [section 320] in particular: thus to have regard to the principles governing the duties of a director in the conduct of the affairs of a company and the rights and duties of a majority shareholder in relation to the minority; but to recognise that [section 320] is a remedial provision designed to allow the Court to intervene where there is a visible departure from the standards of fair dealing; and in the light of the history and structure of the particular company and the reasonable expectations of the members to determine whether the detriment occasioned to the complaining member's interests arising from the acts or conduct of the company in that way is justifiable.<sup>62</sup>

60 See, e.g., *Scottish Co-operative Wholesale Society* case, note 25 *supra*, 324.

61 See *Re G. Jeffrey (Mens Store) Pty Ltd* (1984) 9 ACLR 193, 198.

62 (1984) 2 ACLC 610, 618 *per* Richardson J.; see also *Wayde v. New South Wales Rugby League Ltd* (1985) 59 ALJR 798, 801, 803.

The inherently imprecise nature of this fairness enquiry confounds easy prediction as to the latitude which nominee directors will enjoy under the revised section 320 to promote appointor interests. It seems clear, however, that the conduct that will sustain an order under the previous section 320 is wider than that remediable under the general law of directors' duties.<sup>63</sup> Accordingly, if the view were to be adopted (contrary to that urged above) that nominee directors are permitted to have a special solicitude for their appointors' interests, some consequential adjustment to the oppression remedy would be necessary.

One serious deficiency in the application of the oppression remedy to nominee directors has recently become apparent. In *Morgan v. 45 Fleurs Avenue Pty Ltd*<sup>64</sup> a shareholder in company A complained of conduct of a nominee which the company had appointed to the board of company B. (Company A held 45% of the equity of company B.) The Supreme Court of New South Wales dismissed the oppression suit on the ground that the complaint related not to the affairs of company A but to those of company B in which the petitioner had no direct shareholding interest and therefore no standing under section 320. The outcome is anomalous in view of the widespread adoption of the group of companies as a model of business organisation.<sup>65</sup> The *Morgan* decision effectively denies shareholders in the parent company a right of complaint concerning the conduct of nominees appointed to the board of a subsidiary company.<sup>66</sup> Since parent company shareholders would lack standing at general law to challenge decisions of the subsidiary's directors, the usual accountability mechanisms of company law are displaced. All that remains is scrutiny of the subsidiary company's directors by those responsible for their appointment, normally the board of the parent company.<sup>67</sup> Where the company to which the nominees are appointed is not a subsidiary of the appointor (as in *Morgan's* case) this mechanism may be of dubious worth. Thus where nominees are appointed from two or more sources, none appointing a majority, nominee directors may be effectively insulated from suit by shareholders in each of the appointor companies who suffer a corresponding loss of control prerogatives over their investment.

63 See *Wayde, id.*, 801, 803-804.

64 (1987) 5 ACLC 222.

65 On the adoption of the corporate company group structure (and some consequential legal issues), see T. Hadden, *The Control of Corporate Groups* (1983) and (1984) 12 *Intl J Soc Law*, 346; F. Wooldridge, *Groups of Companies: The Law and Practice in Britain, France and Germany* (1981).

66 Under Companies Code s.7 a company is a subsidiary of another company if the latter company controls the composition of the first company's board of directors or holds more than one half of the voting rights or issued capital of the first company. The controlling company is called the holding company or, colloquially, the parent of the subsidiary.

67 It may be that egregious failure by the parent directors to seek redress for breach by the subsidiary directors will amount to conduct of the affairs of the parent company in respect of which an order may be made under the section at the suit of a shareholder in the parent (e.g., an order under s.320(2)(g) directing the parent company to institute proceedings in respect of the nominees' default).

The writer suggests that the scope of the oppression remedy should be expanded to enable a shareholder to complain about the conduct of nominees appointed by the company to the board of a subsidiary. Whether the remedy should lie in respect of nominees appointed to the boards of other companies is a more difficult question. Where, however, (as in *Morgan's* case) the appointor company has a substantial equity in the company to which the nominee is appointed, a strong case can be made for the expanded remedy. Perhaps the optimum solution lies in expanding further the definition of the "affairs" of a company, in respect of which an oppression suit will lie, by general provision which leaves to case by case judicial decision the determination of the boundaries of legitimate shareholder interest here.<sup>68</sup>

### 5. *Nominee Directors and Company Groups*

Perhaps the principal category of nominee directors is of persons appointed by holding companies to the board of a subsidiary.<sup>69</sup> The question of nominee loyalty arising from such appointments is closely linked with the general definition of group and individual company interests. The case law establishes that directors of a company within a corporate group must act by reference to their perception of the interests of *that* company, and not those of another company in the group or of the group as a whole.<sup>70</sup> Since creditors of a company may look only to that company for discharge of their debts and, absent fraud or other wrongdoing, not to its parent or other related company,<sup>71</sup> the directors' duty to their company requires them to consider the interests of its creditors.<sup>72</sup> Where the company is a wholly owned subsidiary, its interests may be safely identified with those of its holding company. Its directors may then properly act by reference to the parent's interests and in accordance with its wishes with due solicitude, of course, for the interests of the subsidiary's creditors. Where, however, there is an independent minority shareholding in the subsidiary, the obligations of the subsidiary's directors will be little different from those of nominee directors generally.

In partly-owned subsidiaries the parent company, although it owns less than 100% of equity, will usually be entitled to appoint all of its directors. Their loyalty to the parent may generally be assumed, however solicitous they may also be for the minority interests. Lord Denning's formulation in the *Scottish Co-operative Wholesale Society* case assigns the subsidiary directors to an "impossible position" when a conflict arises between parent

68 The present scope of the term "affairs" is defined in Companies Code s.7.

69 The proceedings in each of the *2GB* case, the *Scottish Co-operative Wholesale Society* case and the *Berlei Hestia* case arose in such a context.

70 See *Walker v. Wimborne*, (1976) 137 CLR 1; *Lindgren v. L. & P. Estates Ltd* [1968] Ch 572; *Charterbridge Corporation Ltd v. Lloyds Bank* [1970] Ch 62.

71 See *Re Southard & Co. Ltd* [1979] 1 WLR 1198, *Re Sarflax Ltd* [1979] 2 WLR 202.

72 See *Walker v. Wimborne*, note 67 *supra*, 6-7; *Kinsela v. Russell Kinsela Pty Ltd (in liq.)* (1986) 4 NSWLR 722.

73 Note 26 *supra*.

and subsidiary.<sup>73</sup> The *2GB* formulation, however, attaches liability only if it can be inferred that the subsidiary directors would sacrifice the interests of the subsidiary (or its minority shareholders) to those of the parent. Further, Jacobs J. apparently thought it unobjectionable that the nominee directors would follow Fairfax instructions “without a close personal analysis of the issues”.<sup>74</sup> Lord Denning’s formulation may be criticised for applying the conflict avoidance rule rigorously to a situation where conflict is endemic and ubiquitous. The *2GB* formulation, on the other hand, offers slight protection to minority interests in partly owned subsidiaries. The optimum rule, it is suggested, lies somewhere between these two positions.

#### 6. *Reporting Back to the Appointor*

Although the understanding will vary with the particular relationship, a nominee director will often be expected to report back to his or her appointor as to the state of company affairs. Indeed, in many cases the reporting back function may be the primary motive for the nominee’s appointment. Two questions particularly arise. First, are the nominee director’s rights of access to corporate information qualified by reason of his or her nominee status? Secondly, what are the limits on the rights of the nominee director to disclose to the appointor information acquired as a director?

The general law concedes to directors a right of access to corporate records which is not conditional upon proof of the director’s bona fides or “need to know.”<sup>75</sup> In *Bennett’s* case<sup>76</sup> the representative director, with striking candour, admitted that it was his intention to communicate the terms of the advice obtained by the board to his union to be used to best advantage in its dispute with the board. Since the director’s intended use of the advice was in breach of his duty, the Court exercised its discretion to deny the enforcement of this general law right of access.

It will ordinarily be assumed, however, unless the contrary is demonstrated, that a director appointed to a statutory body to represent a sectional interest will act in the interests of the body, and not that of his or her electors. It seems that a similar rule applies to companies registered under the Companies Code. Thus in the *Berlei Hestia* case<sup>77</sup> the Australian nominee directors were granted access to records of the New Zealand company notwithstanding the direct commercial competition between the two companies. The principle is further exemplified in *Molomby v. Whitehead*<sup>78</sup> where the managing director of the Australian Broadcasting Corporation had

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74 Note 14 *supra*, 1663.

75 *Edman v. Ross* (1922) 22 SR (NSW) 351. It is less clear whether directors are entitled to papers of committees of the board of which they are not members; see *Birmingham City District Council v. O* [1983] AC 578, 594.

76 Note 18 *supra*.

77 Note 31 *supra*.

78 (1985) 63 ALR 282.

denied a staff elected director access to documents concerning the management of the Corporation. No suggestion was made that the staff director was seeking the documents for an ulterior purpose and not in discharge of his fiduciary responsibilities. In the Federal Court of Australia, Beaumont J. upheld the director's access rights, saying that "no initial burden of proof rests upon [the director] to show any particular reason for, or utility in, the grant of access. This will ordinarily be assumed."<sup>79</sup>

As for the second question, viz., the limits on the nominee's right to report back to the appointor, the conflict avoidance obligation prevents a director from exploiting, without the consent of his company, information acquired in the course of office. Companies Code section 229(3) & (4) strengthen this rule with a prohibition upon the director's improper use of office, or of information acquired by virtue of office, to gain an advantage for him or herself or for any other person, or to cause detriment to the company. There is no clear authority on the question as to when communications between nominee and appointor will amount to an improper use of information within the subsections. It is suggested, however, that the boundaries of proper disclosure will be determined by the equitable duty of confidence preventing fiduciaries from making improper use of confidential information acquired by virtue of their position.<sup>80</sup> This formulation of the limits of disclosure is tautologous but, it is suggested, inevitably so.

The Institute of Directors (U.K.) has adopted another formulation of the nominee director's entitlement to share information with his or her appointor. The Institute expresses the rule thus:

[t]he first principle here must be that information which is received in confidence must be treated in confidence. Information is part of the company's property, which directors must not misapply. The duty of confidence is plainly not absolute; many matters are discussed at board meetings which it is a director's right, and indeed often his duty, to disclose to third parties. The simple criterion is whether the disclosure is bona fide in the interests of the company. It is for the director concerned to prove that any disclosure is indeed bona fide. A director cannot be acting bona fide in the interests of his company if he fetters his discretion as to how he is to act. Thus if a nominee director agreed always to pass on to his nominator the management accounts of the company of which he is a director, that action alone would be a breach of his duty to act in good faith towards that company.<sup>81</sup>

Under this "simple criterion" the nominee's right to disclose corporate information to the appointor depends upon "whether the disclosure is bona fide in the interests of the company". The scope of the nominee's disclosure rights under this formulation depends upon the answer to the fundamental question posed in this article — within what limits may the nominee director identify the interests of the company with those of his or her appointor? The answer to that question lies at the heart of several others.

79 *Id.*, 293. See further J. Hill (1987) 61 ALJ 657 and "Inspection of Corporate Books and Documents by Directors and Shareholders" (1988) 12 *Sydney L Rev* (forthcoming).

80 See P.D. Finn, *Fiduciary Obligations* (1977) 142.

81 Note 27 *supra*, para. 17.