INSTITUTE OF LAW RESEARCH AND REFORM

VARIATION OF SHAREHOLDER RIGHTS

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I. INTRODUCTION

One of the more desirable goals for the draftsmen of modern corporate legislation is to attempt to strike a fair balance on those occasions where minority and majority interests clash. Although it is undoubtedly necessary to provide protection for minority shareholders whose rights are being unfairly prejudiced or adversely affected by the compa it is equally necessary to provide wide and flexible guidelines for the company so as to facilitate its efficient conduct of business in a modern corporate society.

This conflict manifests itself in the area of variation of shareholder and class rights. Although shares are basically regarded as property rights based on a contract between a company and the holder, this contract is, in Gower's words 'of a curious type', because it is variable at the option of one party who can always alter its original terms.

It will be the purpose of this paper to examine the ramifications and consequences of this curious contract. The basic issues to be discussed are first, the limitations on the holders of the voting shares to alter, amend or vary the share capital in a company, and second, the protections that are provided for shareholders to ensure that their share or class rights are protected. The examination will necessarily include a critical analysis of current Alberta legislation and the common law applicable to that legislation. The laws of other jurisdictions in Canada and around the world will also be canvassed. Special emphasis will be given to the new Canada Business Corporations Act which introduces several new concepts into the area.

The paper is subdivided into six major areas corresponding to the outline as found in the table of contents, although the two major considerations will be, generally, the procedures by which variations are made and the protections available to shareholders when those procedures are used. Conclusion and recommendations will close this paper.

II. DEFINING THE IMPORTANT CONCEPTS

Because this paper will be dealing in detail with certain basic concepts relating to shares and shareholders, this preliminary section will canvass the current law in order to derive some working definitions for use throughout this paper.

A. Shares

Only the Alberta Act in section 2(1)(31) and the Draft Ghana Code (in the first schedule) attempt to statutorize the definition of 'share'. Neither is useful in deliniating more fully the accepted common law definition. One of the classic definitions of a share at common law is derived from this statement of Farwell, J. in Borland's Trustee v. Steele Brothers and Company Limited:[1]

> A share is not a sum of money...but is an interest measured by a sum of money and made up of various rights contained in the contract, including the right to a sum of money of a more or less amount.

For purposes of this paper, the important feature to note is that a share confers upon a shareholder rights in a company as well as against it.

B. Classification of Shares

The diversity of interests and pressures affecting a company, the desire for various forms of protections, preferences and control and the need for flexibility in structuring share capital have lead companies to utilize more than one class of shares in organizing their share structure.

A lack of legislative definition has led to the use of the terms 'common' and 'preferred' to describe the various types of shares. The distinguishing feature of the preference share is that it confers on the holders some preference over other classes of shares, usually in respect of dividends or repayment of capital or both. Although the initial presumption of the law is that all shares confer equal rights and equal liabilities, in order to determine the particular preference of each share, it is necessary to examine the memorandum and articles of the company and the resolutions under which they were issued.[2] A company is entitled to issue shares with whatever types of preferences, restrictions, etc. it desires, subject only to corporate and security law, and the company's own bylaws.

Currently in Alberta, the Companies Act contains no definition of common or preferred shares although some sections of the Act do refer to preferred shares, notably section 68(1) and section 69. Only the Ontario and the Federal Acts are substantially different in approach from the remainder of the current Canadian Corporate Acts.

The Ontario Business Corporation Act is the only Act in Canada which attempts to define common and preferred shares.

26. (1) **Common shares.**—The common shares of a corporation shall be shares to which there is attached no preference, right, condition, restriction, limitation or prohibition set out in the articles of the corporation, other than a restriction on the allotment, issue or transfer.

(2) Classes of shares.—Except as provided in subsection (1) of section 37 where a corporation has one class of shares, that class shall be common shares and designated as provided in the articles.

[Subsec. (2) amended by 1972, c. 138, s. 8(1).]

(3) Idem.—Except as provided in subsection (1) of section 37 where a corporation has more than one class of shares, one class shall be common shares, designated as provided in the articles, and the other shares shall be special shares and may consist of one or more classes of special shares and shall have attached thereto the designations, preferences, rights, conditions, restrictions, limitations or prohibitions set out in the articles.

[Subsec. (3) amended by 1972, c. 138, s. 8(2).]

(4) Preference shares.—No class of special shares shall be designated as preference shares or by words of like import, unless that class has attached thereto a preference or right over the common shares. 1970, c. 25, s. 26.

27. (1) **Special shares.**—Each class of special shares may have attached to it preferences, rights, conditions, restrictions, limitations or prohibitions, including but not limited to,

(a) the right to cumulative, non-cumulative or partially cumulative dividends;

(b) a preference over any other class or classes of shares as to the payment of dividends;

(c) a preference over any other class or classes of shares as to repayment of capital upon the dissolution of the corporation or otherwise;

(d) the exclusive right to elect part of the board of directors;

(e) the right to convert the shares of that class into shares of another class or classes of shares;

(f) the right of the corporation at its option to redeem all or part of the shares of the class or the right of a shareholder at his option to require the redemption of all or part of his shares of the class.

[Clause (f) substituted by 1972, c. 138, s. 9.]

(g) the purchase for cancellation by the corporation of all or part of the shares of that class by agreement with the holder thereof;

[Clause (g) substituted by 1971, c. 26, s. 5.]

(h) conditions, restrictions, limitations or prohibitions on the right to vote at meetings of shareholders.

Section 26(2) reiterates the common law but section 26(3) introduces the concept of 'special' share into Ontario law and restricts the use of the 'preference' term to cases where there actually is a preference to that share over the common share. Except for a restriction in section 27 which prohibits preference shares to be convertible into securities, the preferences, rights, conditions, restrictions or prohibitions set out in the Ontario Act are unchanged in principle from those which could be attached to preference shares under the old Act. The changes in terminology are mainly for the purpose of clarifying the newer provisions of the Act.

In complete contrast to the complex Ontario approach is the simple approach of the new Federal Act. The Act abolishes the distinction between common and preferred shares

on the ground that they, as the Dickerson Committee argued, were not 'precise'. Section 24(3) allows a company to provide for more than one class of shares in the articles and the articles must set out any rights, privileges, restrictions and conditions attaching to the class. Section 24(4) provides that at least one class of shares must contain the accepted rights attributable to common shares--namely the right to vote and to share in the proceeds upon dissolution.

C. Shareholders Rights

The concept of shares and their classification leads us to the question of what rights attach themselves to shares. Normally, shareholders rights fall under three headings--dividends, return of capital on a winding-up (or authorized reduction of capital) and voting rights. As well, companies are free to allot any other right they desire,[3] subject of course to the law and the articles of the company. As noted earlier the law initially presumes all shares are equal so that unless there is some indication to the contrary in the articles all shares will confer the same rights in all cases. Section 51 of the Ghana Act goes so far as to statutorize the common law canons of constructions (with some changes) for interpreting rights of preference shares. In essence however, share rights are those rights attached to each class of shares affecting the holders of those shares in their interactions with the company.

D. Class Rights

Once the share structure in a company contains more than one class of shares, the concept of class rights arises. The accepted statement of what a class is, derives from Sovereign Life Assurance v. Dodd[4] per Browne L.J.:

> The word "class" is vague, and to find out what is meant by it we must look at the scope of the section, which is a section enabling the Court to order a meeting of a class of creditors to be called. It seems plain that we must give such a meaning to the term "class" as will prevent the section being so worked as to result in confiscation and injustice, and that it must be confined to those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest.

If all the shares are of one class, the only limitations on them are those which restrict the extent to which a company can effectively alter its memorandum or articles. Class rights arise only where one class of shares has rights different in some way from another class. All rights, not only the special ones, enjoyed by that class will then be regarded as special class rights to be protected if the company attempts to vary those rights. The procedure and protection of those class and shareholder rights will be the subject of future sections of this paper.

A problem arises in this area as to whether the rights of common shares are class rights thus qualifying them for the protection afforded to special classes of shares. There are no reported cases on this subject but there is one unreported case upon which we can draw some inferences. In Hodge v. James Howell and Company (December 12, 1958, see C.L.Y. 1958, 446), petitioner was an ordinary

shareholder in a company with two classes of shares. The voting class desired to create a second class of preference shares ranking behind the first class of preferreds but ahead of the common shares with regard to certain priorities. It was argued by the petitioner that the creation of the new shares constituted a variation of the rights and privileges of the ordinary shareholders and therefore required the use of a variation of rights procedure. The court dismissed the application and thereby inferred that no special class rights arose on the ordinary shares:

> "The memorandum and articles were designed to do no more with regard to the ordinary shares than attach to them the rights with which ordinary shares were commonly associated in the minds of persons dealing with such matters."

On this reasoning then, the rights of common shares do not seem to be included in the definition of special class rights. Support for this approach is found in the Federal Act, section 24(4) which requires a company to have at least one class of shares containing the usual rights associated with common shares. For purposes of this paper it will therefore be assumed that common shares do not contain special class rights.

III. POLICY CONSIDERATIONS

There are three questions which must be considered at the outset of this analysis. Each refers briefly to the basic policy determinations which are fundamental in our examination of this area.

(1) Why do companies desire to alter their capital structure?

The policy reasons behind the requirement for alteration of corporate structre are easily determinable. The facts of business life, i.e. business trends, tax considerations, etc., make it necessary that changes to a corporate share structure be easily made to ensure the greatest possible flexibility in dealing in the corporate world. A company requires an easily ascertainable share capital for purposes of voting and money payments and as an instrument to raise capital. In many companies, share capital can be an important element in determining and consolidating control of corporate management. The proper use of share capital represents an important function of a company in terms of economic and and business success.

(2) Why is it necessary to examine the rights of the shareholder in this area?

Keeping in mind the basic conflict between majority and minority shareholders noted earlier, corporation law must ensure that the rights of shareholders are protected from unfair or unwarranted alterations to their rights. Along these lines, it is necessary to investigate whether the current law, both the common law and statute law, have developed adequate procedures and protections for ensuring those rights. This examination is also necessary to ensure that the corporate entity remains an appealing vehicle both for purposes of carrying on a business in Alberta as well as investing in one.

(3) What approach should a corporate statute take in dealing in the area of variation of shareholder rights?

It is submitted that these issues of law should be dealt with in a concisely written, understandable corporate statute.

statute should be an enabling one and not regulatory and as noted by the authors of the Iacobucci Report:[5]

> The statute should reflect a permissiveness allowing businessmen to form and operate corporations as efficiently and as cheaply as possible, keeping regulatory or remedial aspects of the statute to that standard which sensibly takes account of the interests of shareholders, creditors, management and the public.

As will be seen, the area to be examined necessarily involves the role of the court. Therefore one of the major objectives of a statute will be to properly and effectively examine the rol the courts. The approach of this paper will be examine ways to limit the role of the courts in terms of the actual corporate decision-making process and to examine numerous alternatives for protecting rights and instituting remedies. The recommendations which will conclude this paper will hopefully reflect these objectives.

IV. PROCEDURE FOR ALTERING SHARE OR CLASS RIGHTS

It is the purpose of this section to examine the question of how share or class rights may be altered by the company. There are numerous procedures in use in Canada and other jurisdictions and examples of each type will be critically analysed. "It is perhaps surprising that what would seem to be of paramount importance to our economic life and of everyday occurrence should be hedged with uncertainty and doubt."[6]

There appear to be three different general procedures by which corporate legislation allows a company to vary share or class rights. Although the current Alberta legislation sanctions the use of only the first procedure,

all three procedures will be examined in detail in order to compare and contrast the available approaches.

Before proceeding into the main body of this section, it should be noted that although the terms 'alter', 'vary', etc., have been given strict technical interpretations by the courts (which will be examined in section V), the terms as they are used throughout this section indicate alterations to share or class rights which add, change or remove rights or privileges attached to shares.

A. The Act Itself Sets Out The Procedure

Under this first heading, the Act itself provides the procedure by which rights may be varied. Jurisdictions included in this classification are the current Alberta Act as well as the newer Canadian Companies Acts although the mechanics of the procedure differ in each case.

1. Variation to Share Rights (Shares are all of One Class)

Where only one class of share exists, no particular injustice can occur through variation in share rights because those changes will prima facie affect all shareholders in the same way.[7] Therefore the only question which arises is the actual procedure by which these changes are effected.

In all jurisdictions, variation to share rights are sanctioned primarily by the use of the special resolution. The defining section of the Alberta Act in section 2(1)(32) outlines the two basic requirements necessary for the successful authorization of a special resolution in all jurisdictions, namely, notice to those who have a direct interest and a vote on the subject matter and secondly a requirement for a majority in number larger than the simple

majority of 51%. These two requirements in themselves are designed as a protection for minority shareholders in a company to the effect that they have notice and information of the resolution and that a larger than usual majority is required to sanction it.

The percentage number required for a special resolution varies from not less than 66% in the Ontario and Federal Acts to 75% in Alberta. Note that the standards set out in the Ontario and Federal Acts indicate only minimum requirements which can be increased if the company so desires. Surprisingly however, brief examination of the approach of two American Company Acts, namely the New York State Business Corporation Act, section 803(a) and the U. S. Model Business Corporation Act, section 59(c) indicates that only a simple majority is required by the company to alter share rights. It should also be noted that the Federal Act, because of the effect given to unanimous shareholders agreements, could conceivably require 100% approval for any share variation.

If there is only one class of shares in an Alberta comp and the rights are set out in the memorandum of association, section 38 of the Alberta Act requires a further step in the procedure. Any reorganization of the share capital must be approved by the court as part of the positive variation procedure. However if the share rights are contained in the articles section 42 of the Alberta Act requires only a special resolution to alter or add to the articles so that conceivably share rights could be varied without requiring court approval. However this section must be read in conjunction with section 69 which does require court approval for variation. The requirement for approval by an outside body is also found in the British Columbia Companies Act. Section 247(2) of the B. C. Act requires that any resolutions affecting share rights of 'Reporting' companies must be approved by the Securities

Commission before they are valid.

One further difference found among the jurisdictions under this heading is in determining where the share rights may be placed. As noted above, in Alberta, share rights may be placed in either the articles or the memorandum of association. The Ontario Act, by virtue of section 189 allows the rights of shares to be placed only in its 'articles of incorporation' which correspond roughly to the memorandum of an Alberta company. Section 245 of the B. C. Companies Act allows alteration to either a company's memorandum or articles. For purposes of simplification, the new Federal Act requires all share information, including rights, to be included in the "articles of incorporation" which like the Ontario Act, is a charter document equivalent to the memorandum of association in an Alberta company.

2. Variation of Class Rights (more than one class of shares)

The procedures become much more complex when more than one class of shares is involved. Corporate acts which fall under this classification may only vary share or class rights pursuant to a set variation of rights procedure as detailed in the substantive provisions of the Act itself. In those jurisdictions, either the articles do not deal with the variations to share rights or if they do make provision for alteration, they must be consistent with provisions of the Act.

For purposes of effectively examining the procedure in question, it will be necessary to examine individually many of the procedures outlined in the various acts. This procedure, in general, requires that a valid alteration of rights can only become effective if a special resolution is

passed separately by all classes of shareholders whose rights are 'affected'. As well in Alberta, court approval is required. In most other jurisdictions, some mechanism is provided to allow dissenting shareholders to bring an application to the courts to have a variation resolution set aside.

The Alberta Companies Act

As we noted earlier, share rights in Alberta may be detailed in either the memorandum or the articles. This normally is explained by the fact that there is no provision in the Act indicating exactly where share rights should be outlined. Any alterations to the memorandum or the articles must be done in the mode and extent for which provision is made in the Act. If the rights of a class are conferred by the memorandum, it is possible that they not be varied at all unless the memorandum so provides. Usually however unless the alterations are illegal, contrary to public policy or to the express provisions of the Act, the company has the right to effect any alteration it deems 'in the best interests of the company'.

There are two sections in the Alberta Act, sections 38(1) and 69(2) which allow for the company to reorganize its share capital. Although section 38(1) expressly refers to the memorandum, section 69(2) refers to neither the memorandum nor the article.

> **38.** (1) A company having a share capital by special resolution confirmed by an order of the court,
>
> **(a)** may modify the provisions contained in its memorandum so as to reorganize its share capital in any way, and without prejudice to the generality of the foregoing power may modify or alter its memorandum so as to

> (i) consolidate shares of different classes, or
> (ii) divide its shares into shares of different classes, or
> (iii) vary the rights attached to any class of shares, or
> (iv) subject to section 68, convert shares of a fixed amount into shares without nominal or par value, or
> (v) convert shares without nominal or par value into shares of a fixed amount,
>
> but no preference or special privilege attached to or belonging to any class of shares shall be interfered with except by a resolution passed by a majority in number of shareholders of that class and holding three-fourths of the share capital of that class, and every resolution so passed binds all shareholders of the class, and

S.69(2) If at any time the share capital is divided into different classes of shares, the rights attached to any class, unless otherwise provided by the terms of issue of the shares of that class, may be varied by a special resolution confirmed by an order of the court, with the consent in writing of the holders of three-fourths of the issued shares of that class, or with the sanction of a resolution passed with such a majority as is required for the passing of a special resolution at a separate general meeting of the holders of the shares of the class.

Since it is reasonable to assume that section 69(2) was not included in the Act merely to duplicate the effect of section 38(1), it is submitted that section 69(2) refers to alterations in the articles, not the memorandum. The Alberta Corporation Manual indicates some support for this proposition: "It is not clear that section 69(2) can be used if the memorandum of the company was to be varied."[8] This position is reinforced by the rule of statutory interpretation which requires that in examining a statute, every provision is deemed to have been included in the statute for a definite and recognizable purpose.

The availability of these two alteration sections becomes important due to the fact that the procedures outlined in section 38(1) and section 69(2) are different in some aspects. Both require a special resolution to be confirmed by an order of the court. As well, both require some form of consent by those shareholders whose rights or privileges have been interfered with. The major difference

between the two is that in the case of section 69(2) the consent in writing of the holders of three quarters of the issued shares of the class may be obtained without holding a meeting. Under section 38(1)(a)(3) the resolution must be passed by not only the persons holding three quarters of the share capital, but also by an actual majority in number. As the actual numerical majority is not required by section 69(2), the standard for passage of a variation resolution is much easier under section 69(2). Not surprisingly, most of the special resolutions proposed in practice in Alberta use the procedure as outlined in section 69(2). However there is a definite uncertainty in this area of the law due to the ambiguities arising out of the two sections.

As noted earlier, unlike almost all other corporate statutes, the Alberta Act requires a second step in the variation procedure. The court must approve all variation resolutions before they become valid. Naturally the criteria used by the courts in approving such a resolution is a vital part of the procedure. Because however, the criteria used by the courts, both in terms of determining whether the actual alteration is valid, as well as whether it constitutes a 'variation' of rights, forms a major part of the protections available to the rights of shareholders, it is proposed to discuss these two points in the next section of this paper.[9] It is sufficient for our present purposes merely to note that court approval is a required positive step in the variation of rights procedure in Alberta. It should also be noted that the Alberta Act does not contain a specific section which allows dissenting class shareholders to appeal a variation resolution to the court.

The Ontario Business Corporations Act

The Ontario Act was the first of the new Canadian corporate legislation of the seventies and it has approached the variation of rights problem by providing for the procedure in the provisions of the Act. These types of amendments fall under the reorganization proceedings of the Act and as such require the sanction of a special resolution. However section 189(4) outlines additional protections if the amendment is in effect a variation of rights amendment.

> **189.** (4) **Additional authorization for variation of rights of special shareholders.**—If the amendment is to delete or vary a preference, right, condition, restriction, limitation or prohibition attaching to a class of special shares or to create special shares ranking in any respect in priority to or on a parity with an existing class of special shares, then, in addition to the confirmation required by subsection (2), the resolution is not effective until it has been confirmed,
>
> (a) by 100 per cent of the holders of the shares of such class or classes of shares in writing; or
>
> (b) in writing by at least 95 per cent of the holders of the shares of such class or classes of shares holding at least 95 per cent of the issued shares of such class or classes and after twenty-one days notice of the resolution and confirmation has been given by sending the notice to each of the holders of shares of such class or classes to his latest address as shown on the records of the corporation and only if at the expiration of twenty-one days none of the holders of such class or classes has dissented in writing to the corporation; or
>
> (c) if the articles so provide, by at least two-thirds of the votes cast at a meeting of the holders of such class or classes of shares duly called for that purpose or such greater proportion of the votes cast as the articles provide,
>
> and by such additional authorization as the articles provide.

It should be noted that the Lawrence Committee Report[1] which was the basis for the Ontario Act, did not deal with amendment to the articles or consider the topic with which we are dealing.

The Ontario Act puts a very strong onus upon the company to include in its articles a provision to the effect that the variation of rights procedure may be approved by a mere two thirds of the votes cast by the holders of the affected shares. Without this provision, the requirement of 100% consent in section 189(4)(a) or 95% written consent in section 189(4)(b) would be most difficult to obtain, in effect producing a situation where one class of shares would hold a potential veto power over the actions of corporate management--undoubtedly a severe restriction on the operatability of the corporation. However section 189(4)(c) provides the necessary 'out' which reduces the required consent even below that needed in Alberta to only two thirds of the votes cast at a meeting, providing of course the company puts this requirement in its articles. It should be noted that this requirement is again a minimum requirement and the articles may require higher standards of acceptance if the company so desires.

The Ontario Act, perhaps reflecting the attitude of the Lawrence Committee who rejected a section 210 approach[11] to relief against majority oppression, makes little use of the courts in the variation procedure. Special resolutions need not be approved by the courts prior to their validation as in Alberta. As well, the Act provides no section for allowing minority shareholders to question the validity of the variation. Thus, the only way an Ontario shareholder could get his action before the courts would be via a representative action on behalf of the corporation using section 99 or through an action on his common law rights that the alteration was not bona fide and in the best interests of the company. Failing those routes, once sanctioned under the rather lax terms of section 189(4), the resolution would appear to be valid. This position has been criticized:[12]

> ...The Select Committee seems to have confused the unremedied wrong done to the company which is cured by the derivative action and the wrong inflicted on the minority shareholder qua shareholder which is remedied in section 210... a widened section 210 would take care of the situation covered by the derivative action. But the converse is not true, as the Select Committee seemed to think. The problem of the oppressed minority shareholder is not adequately covered by a derivative action.

The B. C. Companies Act

The new British Columbia Companies Act sets out a detailed rigid procedure by which share or class rights may be altered. Changes to existing share structures are permitted under sections 245 and 246 which set out in express language that companies may alter so as to 'create', 'define', 'attach', 'vary' and 'abrogate' special rights to classes of shares. These alterations may be effected by a special resolution requiring three quarters majority.

The actual variation of rights procedure is outlined in section 247:

> **247.** (1) No right or special right attached to any issued share shall be prejudiced or interfered with under any provision of this Act or the memorandum or articles unless members holding shares of each class whose right or special right is prejudiced or interfered with consent thereto by separate resolution requiring a majority of three-fourths of the issued shares of the class.
>
> (2) No resolution to create, vary or abrogate any special right of conversion attaching to shares of a reporting company shall be submitted to a general meeting, or a class meeting, unless the Commission has first consented to the resolution.

Note the use of the words 'prejudiced or interfered with' in section 247(1). They are new words and it is arguable that they carry an even narrower restriction than the judicial interpretation of words such as 'affect'. This will be dealt with at length in the next section.

One of the major distinctions in the B. C. Act between a reporting and a non-reporting company is noted in section 247(2) in that the variation procedure for reporting companies requires the consent of the Securities Commission before such a resolution is even submitted to the general or class meeting. The rationale behind the 'reporting' company is that there was a 'need to know' in the classic sense in which that term is used, as enunciated in S. E. C. v. Ralston Purina (USSC) i.e. a need for giving shareholders the protection of the Companies Act in respect of such things as disclosure of financial information, share rights, etc. This changes the law in British Columbia as the old Act, in section 62, required court approval for any variation or abrogation of special rights or restrictions attached to any class of shares for all companies.

In contrast to the Ontario or Alberta Acts, the B. C. Act provides a framework in section 248, by which dissenting or affected shareholders may apply to court.

248. (1) The holders of

(a) not less than ten per cent of the shares of a company who voted, in person or by proxy, against a special resolution referred to in section 245 or 246; or

(b) not less than ten per cent of the shares of a class of shares of the company, whose rights are affected by a special resolution abrogating or altering special rights or restrictions attaching to any class of shares of the company, or approving of any arrangement, who did not, in person or by proxy, vote in favour of the resolution referred to in section 247;

other than as a proxy for a person whose proxy required an affirmative vote may, not more than fourteen days after the passing of the last resolution, apply to the Court to set aside the special resolution.

(2) The Court shall not hear the application referred to in subsection (1) unless notice thereof has been served upon the company and an affidavit of that service exhibiting the notice has been served upon the Registrar not later than fourteen days after the passing of the last resolution.

(3) The Court may direct that notice of the application be served upon any other person.

(4) Upon an application under subsection (1), the Court may

(a) set aside the special resolution and require a copy of the order to be filed with the Registrar;

(b) affirm the special resolution subject to such terms as the Court considers appropriate; or

(c) affirm the special resolution and require the company, subject to subsection (1) of section 257, or any other person, to purchase the shares of any member at a price and upon the terms to be determined by the Court,

and, in any case, the Court may make such consequential orders, including any order as to costs, and give such directions as it considers appropriate.

It should be noted that this section allows not only shareholders who actually voted against the resolution to apply to court, but allows application by shareholders whose rights have been affected by the resolution.[13] The court is given specific powers to either affirm or set aside a resolution and if they affirm it, they may require the company to buy up the shares of the dissenting shareholder, thereby eliminating him as a shareholder in the company. This is a significant change as it introduces in Canada for the first time the concept of 'appraisal rights'. However in British Columbia, the courts have the discretion to institute this remedy--it is not mandatory.

The Federal Act

The procedure outlined in the Federal Act is the broadest yet most refined procedure yet developed for variation of rights. Federal draftsmen classified an alteration to share rights as a 'fundamental change' and included it in that section of the Act. Sections in the Federal Act which expressly allow the corporation to vary share rights include sections 167(1)(e) to 167(1)(i).

> **167.** (1) Subject to sections 170 and 171, the articles of a corporation may by special resolution be amended to
>
> (*i*) authorize the directors to divide any class of unissued shares into series and fix the number of shares in each series and the rights, privileges, restrictions and conditions thereof;
>
> (*j*) authorize the directors to change the rights, privileges, restrictions and conditions attached to unissued shares of any series;

(*e*) create new classes of shares;

(*f*) change the designation of all or any of its shares, and add, change or remove any rights, privileges, restrictions and conditions, including rights to accrued dividends, in respect of all or any of its shares, whether issued or unissued;

(*g*) change the shares of any class or series, whether issued or unissued, into a different number of shares of the same class or series or into the same or a different number of shares of other classes or series;

(*h*) divide a class of shares, whether issued or unissued, into series and fix the number of shares in each series and the rights, privileges, restrictions and conditions thereof;

These provisions are much more explicit than the comparable sections in other Acts and provide for great flexibility on the part of the company. Procedures for varying share rights are found in section 170:

170. (1) The holders of shares of a class or, subject to subsection (2), of a series are entitled to vote separately as a class or series upon a proposal to amend the articles to

(*a*) increase or decrease any maximum number of authorized shares of such class, or increase any maximum number of authorized shares of a class having rights or privileges equal or superior to the shares of such class;

(*b*) effect an exchange, reclassification or cancellation of all or part of the shares of such class;

(*c*) add, change or remove the rights, privileges, restrictions or conditions attached to the shares of such class and, without limiting the generality of the foregoing,

(i) remove or change prejudicially rights to accrued dividends or rights to cumulative dividends,

(ii) add, remove or change prejudicially redemption rights,

(iii) reduce or remove a dividend preference or a liquidation preference, or

(iv) add, remove or change prejudicially conversion privileges, options, voting, transfer or pre-emptive rights, or rights to acquire securities of a corporation, or sinking fund provisions;

(*d*) increase the rights or privileges of any class of shares having rights or privileges equal or superior to the shares of such class;

(*e*) create a new class of shares, or make any class of shares having rights or privileges inferior to the shares of such class, equal or superior to the shares of such class;

(*f*) effect an exchange or create a right of exchange of all or part of the shares of another class into the shares of such class; or

(*g*) constrain the issue or transfer of the shares of such class or extend or remove such constraint.

(2) The holders of a series of shares of a class are entitled to vote separately as a series under subsection (1) only if such series is affected by an amendment in a manner different from other shares of the same class.

(3) Subsection (1) applies whether or not shares of a class or series otherwise carry the right to vote.

(4) A proposed amendment to the articles referred to in subsection (1) is adopted when the holders of the shares of each class or series entitled to vote separately

The usual pattern of requiring a special resolution of the separate class in a separate meeting is preserved by this section. In line with the desire of the federal draftsmen to overcome the current limitations of the common law in the area of interpreting the words 'variation' and 'alteration', the Act has dramatically broadened the provisions of this procedure so as to allow separate class votes for resolutions which "add, change, remove, change prejudicially, reduce, increase, create, etc. rights to shares." Section 170(3) is included to ensure that even though a share may be non-voting, it has a right to vote on a variation resolution and similarly section 170(4) expressly requires a separate vote for each class.

No court or other kind of administrative approval is required by the Federal Act. This is in line with the approach of the Dickerson Committee which favoured judicial non-interference with the actual business decisions of the corporation.[14] However the Federal Act does provide a very broad and easily accessible procedure by which shareholders may apply to court so as to allow him to opt out of the company under the supervision of the court.

184. (1) Subject to sections 185 and 234, a holder of shares of any class of a corporation may dissent if the corporation resolves to

(*a*) amend its articles under section 167 or 168 to add, change or remove any provisions restricting or constraining the issue or transfer of shares of that class;

(*b*) amend its articles under section 167 to add, change or remove any restriction upon the business or businesses that the corporation may carry on;

(*c*) amalgamate with another corporation, otherwise than under section 178;

(*d*) be continued under the laws of another jurisdiction under section 182; or

(*e*) sell, lease or exchange all or substantially all its property under subsection 183(2).

(2) A holder of shares of any class or series of shares entitled to vote under section 170 may dissent if the corporation resolves to amend its articles in a manner described in that section.

(3) In addition to any other right he may have, but subject to subsection (26), a shareholder who complies with this section is entitled, when the action approved by the resolution from which he dissents becomes effective, to be paid by the corporation the fair value of the shares held by him in respect of which he dissents, determined as of the close of business on the day before the resolution was adopted but in determining the fair value of the shares any change in value reasonably attributable to the anticipated adoption of the resolution shall be excluded.

The effect of this approach is that unless a shareholder wants to opt out of the company he is bound by a validly affected resolution. The Act specifically prohibits a situation where a shareholder may dissent in respect of less than all his shares so that he can compel purchase of part of his shares and retain the remainder. (This right is allowed in the U. S. Model Business Corporation Act.) If a shareholder does not wish to opt out of the company he is bound by the resolution unless he can fit himself within the confines of section 234 which allows him to apply to court to have the resolution set aside if he can show that the alteration is

"oppressive or unfairly prejudicial" to his rights.

The New York Business Corporation Act
The U. S. Model Business Corporations Act

For comparative purposes, it is interesting to briefly note the important components of the variation of rights procedure of two American Corporate Acts falling under the classification of Acts now being considered.

Section 801 of the New York Act provides very broad powers for a company to amend its certificate of incorporation. A simple majority however is all that is required to effect these changes (section 804). Like the Federal Act, this Act is quite explicit in detailing the exact situations where class rights are allowed a vote. The procedure for variation follows the normal pattern although again only a simple resolution is required from each class. By virtue of section 806(6), the holder of shares whose rights are affected has the right to dissent and receive fair compensation for his shares.

The New York Act is very similar to the U. S. Model Business Corporations Act. The same procedure is followed in sanctioning a variation of rights. However, there is no right for a dissenting shareholder to bring an action to compel the purchase of his shares unless the company plans a merger, consolidation or a sale or exchange of all the property or assets of the company not made in the usual or regular course of business.

B. The Articles of the Company Contain the Variation Procedure

The next two sections will examine the variation procedures in those jurisdictions where corporate legislation does not provide for a procedure in the provisions of the Act. In those cases two possibilities exist--that the articles of the corporation provide for a variation procedure or they do not. For purposes of this section, it will be assumed that any corporations within the jurisdiction in question do have some kind of variation procedure in its articles. Some of the Acts which fall under this classification are the U. K. Companies Act(1948), the Draft Ghana Code, the Australian Companies Act, and the Saskatchewan Companies Act.

Not only need we examine the actual procedures involved in these cases but a further question arises as to whether a company must follow the procedure as outlined in its articles in order to effectuate a valid alteration.

1. Legal Effect of the Articles

Before entering into an examination of the statutes in question, it is necessary to briefly examine the legal effect of the articles of a corporation as well as alterations to them.

The articles of association of a company set out in detail the manner in which the business and internal operations of the company shall be conducted. The effect of the articles is to bind the shareholder to the company on a contractual basis as exemplified by section 29(1) of the Alberta Act.

From time to time, business necessities will necessarily require alterations, elaborations or modification of the articles in order for the company to meet the demands of business. To facilitate these changes, a company is sanctioned by the Act to alter or add to its articles. Its power to do so cannot be limited by any provision in its memorandum or articles, nor can the memorandum or articles require the alteration to be made in any other way than by special resolution. The articles must be consistent with the memorandum so that if there is a conflict between any part of the altered articles and a provision in the memorandum, the articles are to that extent void.[15]

2. The Variation of Rights Procedure

(a) Variation of Share Rights

Where only one class of shares exist in a company, it is submitted that those rights are altered merely by a special resolution without the necessity of going through the variation procedure. Support for this proposition is found in the wording of the typical variation of rights clause. Article 4 of the U. K. Companies Act begins with these words: "If at any time the share capital is divided into different classes of shares..." and this indicates that the provision is not available where only one class exists. Further support for this proposition was noted in section II of this paper where the unreported case of Hodge v. James Howell inferred that the rights of ordinary shareholders were not special rights and thus not eligible for special protection offered by the variation of rights clause.

The usual method for altering the provisions of the articles is exemplified by section 42 of the Alberta Act which allows an alteration merely by special resolution.

Thus subject to any common law requirements, when there is only one class of shares and they are listed in the articles, they may be varied by a special resolution only. It should be noted however that the requirement of a special resolution where only one class of share exists is in effect the same procedure as is required by the variation of rights procedure where more than one class of sharer exists. The requirements of a separate class meeting and a special resolution are both met.

A proviso to the above must be noted: The articles are solely matters of internal management of the company and a company can provide for any variation procedure they desire. Thus a company could introduce a new variation procedure or indeed omit the procedure altogether. The second possibility will be examined in the next section of this paper.

We noted earlier that share rights could be included in the memorandum and this extends to corporations under the statutes to be examined in this section. However, section 23 of the U. K. Act appears to say that the power to alter the memorandum is not available in terms of authorizing a variation unless the memorandum itself provides a procedure for variation either expressly or by reference to provisions in accompanying articles.[16] In the absence of this power share rights cannot be varied even with the individual consent of each shareholder except under a scheme of arrangement approved by the court. Most companies however, realizing the need for allowing flexibility in the corporate share capital, have provided for some kind of variation procedure in the articles.

(b) Variation of Class Rights

(i) U. K. Companies Act

The U. K. Companies Act does not contain, in its substantive provisions, a procedure by which variation of rights may be affected. Indeed, the Act itself allows the company to provide for a variation procedure in its articles. Section 72 of the Act begins with the phrase:

> If...provision is made by the memorandum or articles for authorizing the variation of rights attached to any class of shares in the company...

The variation procedure usually takes the form of a variation of rights clause and is included in the articles in a manner similar to article 4 of Table A of the Act.

> 4. If at any time the share capital is divided into different classes of shares, the rights attached to any class (unless otherwise provided by the terms of issue of the shares of that class) may, whether or not the company is being wound up, be varied with the consent in writing of the holders of three-fourths of the issued shares of that class, or with the sanction of an extraordinary resolution passed at a separate general meeting of the holders of the shares of the class. To every such separate general meeting the provisions of these regulations relating to general meetings shall apply, but so that the necessary quorum shall be two persons at least holding or representing by proxy one-third of the issued shares of the class and that any holder of shares of the class present in person or by proxy may demand a poll.

The procedure in article 4 is very similar to the procedures outlined earlier. Note however that unlike the Federal Act, a class is not allowed to vote unless there is a direct variation to those class rights indicating that this is a much narrower provision than the Federal Act. Although article 4 of Table A is merely a guide for companies to use it appears that if companies and shareholders wish to avail themselves of the protection outlined in section 72 they must basically conform to the procedure as noted above.

72. Rights of holders of special classes of shares

(1) If, in the case of a company the share capital of which is divided into different classes of shares, provision is made by the memorandum or articles for authorising the variation of the rights attached to any class of shares in the company, subject to the consent of any specified proportion of the holders of the issued shares of that class or the sanction of a resolution passed at a separate meeting of the holders of those shares, and in pursuance of the said provision the rights attached to any such class of shares are at any time varied, the holders of not less in the aggregate than fifteen per cent. of the issued shares of that class, being persons who did not consent to or vote in favour of the resolution for the variation, may apply to the court to have the variation cancelled, and, where any such application is made, the variation shall not have effect unless and until it is confirmed by the court.

The primary use of section 72 is to provide a procedure for dissenting shareholders to apply to court to have a resolution set aside. Before an application can be heard 15% of dissenting shareholders must apply to the court. Once in the court, the court has but two choices--to confirm or disallow the resolution, there being no provision made for the purchase of a dissenting shareholder's interest. As well, the time for the application is shorter than the time allowed under the B. C. or the Federal Acts.

The effect of the British section is to place the power in the hands of the court to affirm or disaffirm variation resolutions. This has led to severe rigidity in these situations. From the company's point of view the efficient operation of the business can be interrupted or harmed by the interference of minority shareholders. From the dissenting shareholder's point of view, due to the high stand required by the Act in bringing an action, because they have but one option allowed to them by the Act, their rights are not well protected by this section.

The Saskatchewan Companies Act

For the most part, the Saskatchewan Act is based quite closely on its British counterpart. Procedure for variation is identical to that of the British Act. Table A of the Saskatchewan Act provides for a variation of rights procedure:

3. If at any time the share capital is divided into different classes of shares, the rights attached to any class (unless otherwise provided by the terms of issue of the shares of that class) may be varied with the consent in writing of the holders of three-fourths of the issued shares of that class, or with the sanction of a special resolution passed at a separate general meeting of the holders of the shares of the class. To every such separate general meeting the provisions of these regulations relating to general meetings apply *mutatis mutandis*, but so that the necessary quorum shall be two persons at least holding or representing by proxy one-third of the issued shares of the class, and that any holder of shares of the class present in person or by proxy may demand a poll.

The application to court section of the Act, section 60, is similarly comparable to section 72 of the U. K. Act, although the time for application is less. The only difference between the two sections is that the Saskatchewan Act allows the court to confirm the resolution "wholly or in part", while the English Act only allows the court to confirm the resolution as it stands. Therefore it is conceivable that the Saskatchewan court could make an alternative order to one which either confirms or disaffirms the resolution.

The Draft Ghana Code

Although the Ghana Act provides that the variation procedure must be in the articles of the company, the Act provides specific restrictions and guidelines on how the procedures should be set up. The Act also expressly requires by section 22(5) that alterations to class rights must be altered in accordance with the variation section, section 47.

(3) Except as provided in subsection (2) of this section a company may by special res tion alter its Regulations by inserting therein provisions regarding the variation of the rights of class or by modifying the terms of any such provisions, but any such alteration shall require prior written consent of the holders of at least three-fourths of the issued shares of each clas the sanction of a special resolution of the holders of the shares of each class and shall be deer for the purposes of subsections (5) to (8) of this section to be a variation of the rights of each cl.

In effect then the Act commands the regulations to follow the normal procedure requiring a special resolution and separate class vote of each class whose rights are altered. As regards any future issues of shares, section 72(4) removes the authority in the articles in effecting a variation and sets down its own guidelines, thus resembling in this instance at least the statutes discussed in Part A of this section.

The Ghana Act also provides for an application to court by dissenting shareholders but includes it as part of the procedure outlined in section 47. Procedures are similar to the British Act in section 72 except in three respects. The Ghana Act allows 60 days for an application unlike the 21 days allowed by the British Act. The Ghana Act allows an application to the court by a shareholder who has voted in favour of the resolution. This was designed to prevent hardships which might occur if shares were vested in nominees for a number of beneficiaries. The more important change is found in section 47(7) which sets out a new criteria for the court to use in examining the variation, namely, whether the variation would 'unfairly prejudice' the shareholders of any class. It is interesting to note that this criteria is the same as that used in the general 'remedy against opression' section 218(1)(b). In his commentary on that section, Gower explained that the applications were intended "to provide a remedy in the type of case where some transaction or resolution is sought to be enjoined on the ground that it is a fraud on the minority."[17] Presumably then, the same criteria applies to an application under section 47. As will be seen, this does not significantly expand the current law in the area.

A final point to note is that under the Ghana Code the court has authority merely to confirm or cancel the resolution.

There is no provision for dissenting shareholders to be bought out.

Note--although the Australian Companies Act fits under this classification, it does not contain any signficant changes from the Acts described above and therefore will not be examined in detail.

3. Is a Company Obligated to Follow the Variation Procedure as Outlined in its Articles?

Where a company's share rights are modified in accordance with a variation of rights clause, no problems regarding variation will arise. However an important question is raised in determining how far a company is bound to follow a prescribed procedure in altering its share rights. In short, must it follow the procedure as set out in its articles?

This problem of course does not exist in jurisdictions where the provisions of the Act set out the procedure, because the company is bound to comply with the standards set down in the Act. However in the case of the corporate legislation examined in this section potential problems may arise because the rights flowing from a company's articles, as between the shareholder and the company, are not entrenched. The company has, subject to some common law restrictions, an absolute right to amend the article in whatever way it so deems. Yet, as we have seen, corporate legislation has dealt with the issue of variation of share rights in such a way as to suggest that these rights require special protection--even to the point of allowing a court, in certain situations, to set aside a resolution. The conflicting approaches to this problem have provided difficulties for both the courts and the legislative draftsmen. The closest

this particular issue has come to be resolved is to be found in two conflicting Australian cases, Crumpton v. Morrine Hall Property Limited [1965] 82 W.N. (N.S.W.) 456 and Fisher v. Easthaven Limited [1964] N.S.W.R. 261, both cases of the Supreme Court of New South Wales.

Both cases dealt with companies incorporated pursuant to the Australian Companies Act and both companies had in their articles a variation of rights clause similar to article 4 of the U. K. Act. In both cases, the plaintiffs owned shares in a 'home unit company' which entitled them to certain rights in respect of their accommodation regarding parking facilities. In effect, plaintiffs owned all of the preference shares of their particular class in the company so that any attempt by the defendant company to use the requisite variation of rights clause to remove those special rights would have met with disaster. Therefore, defendant companies did not follow the procedure but merely attempted to effect the changes by amending its articles to deprive plaintiffs of their rights. Plaintiffs sought an injunction to invalidate the resolution. In the case which was decided first, Fisher, the court held for the defendant company by deciding that under section 65 (the Australian equivalent to section 72 of the U. K. Act), the right to appeal arose only if the procedure laid down by a variation clause was followed by the company. Else-Mitchell, J. also held that the section did not compel the company to follow the procedure laid down by the variation of rights clause:[20]

> I question whether it is proper to say that these sections create or confer in favour of the holders of a class of shares a right to object to an amendment which would affect the special rights attached to their shares. Such a right is certainly not given expressly by the statute...In short, I think that any attempt to apply the relevant sections to the many situations which can

> envisaged where class rights are sought to be effected seems to me to be beyond the capacity of a court called upon to construe a statute.

The Crompton case overruled the Fisher decision with regards to the variation issue. In the opinion of Jacob, J., the intention of section 65 and the variation procedure:[21]

> Is at least a recognition in the articles of association of the principle that there would be no variation of the rights attaching to a particular class of shares without the approval of a certain majority of the members of that class...I think that there is by implication a recognition in the articles that rights particularly attached to classes of shares cannot be altered except in accordance with the procedure laid down. For many years, it has been accepted by text writers and by the courts that such an article have such an effect.

The rationale behind the decision in the Fisher case was based on the proposition that a company has the fundamental right to alter its articles by following the procedure laid down in the Act:[22]

> ...old authorities of high standing... established that a company cannot deprive itself of the statutory right to alter its articles or make them unalterable... Once this conclusion is formed it is difficult to see what precise purpose was to be served by statutory provisions like section 65...These provisions are facultative inform and conserve but little purpose in resolving the rights of shareholders...

In support of this view, it is arguable that if a company wishes to prevent variations to their class rights by means of alteration to the articles, it always has the requisite power to make provision in the articles, i.e. that class rights shall only be modified subject to the terms and conditions in the variation of rights clause. Indeed, such a condition is, as we have seen, actually included in the provisions of the Ghana Act (section 47(4)) which requires that any variations to share or class rights must be affected subject to the procedures set down in that section.

The practical effects of the Fisher approach must also be noted. By virtue of this decision, the company would have an unfettered freedom to make any alteration to the company's articles as they desire, including changes to share capital and share rights. Although this might be a highly desirable goal in terms of allowing the company to efficiently conduct its business activities, it also provides no protection for the rights of minority shareholders who have invested in the company on the basis of their receiving certain benefits, only to have those benefits removed by the company with there being nothing the shareholder can do. It is doubtful that he can even sell out his shares for a fair compensation because the alterations effected by the company will undoubtedly lower the value of his shares.

Although the better academic approach to the problem would seem to be the Crompton position, it will be seen that this position is also unfavourable in practical terms.

The academic writers refer to in the judgment of Jacob, J. have centered on the wording of section 72 of the U. K. Act to support their contentions. As Gower argues:[23]

> It makes little sense to give this right where the variation has been pursuant to a variation of rights clause but to deny it when there is no provision for variation or, a fortiori, when there is such a provision but the company has disregarded it. The legislature must surely have assumed that in either of the latter cases there could be no variation. And since the power to alter the articles expressed by section 10 is expressly 'subject to the provisions of this act', it is subject to the implied limitation of section 72.

This position is supported by two other academic writers who have written articles on this subject.[24]

The case law on the subject of what a 'variation' is, provides further support for this position. Cases which have dealt with the interpretation of a variation of class rights have indicated that where they have found a true variation of class rights, and the articles have included a variation of rights clause, the rights can only be altered subject to the terms of that clause. Thus, in White v. Bristol Aeroplane [1953] Ch. 65 (C.A.) and Re John Smith's Tacaster Brewery [1953] Ch. 308, it was accepted without argument that the proposed changes could only be effected subject to a variation of rights clause. This indicates an acceptance by the courts of the fact that class rights can only be modified subject to the provisions of a variation of rights clause.

Not to be forgotten are the practical aspects of the Crompton approach, and it is here that the undesirability of this approach is apparent. Because the shareholders of each different unit holder were different, they constituted a special class of shares each with special class rights. Because it was unlikely that the shareholders in the above two cases would sanction a restriction on their own rights, no such alteration resoltuions would ever be passed. The

practical affect of this would be that the special class shareholders would hold a veto power over the company and the company would be effectively restrained from conducting its business or making the necessary changes to its corporate share structure--changes which indeed might be critical to the survival of the company.

It seems obvious therefore that both positions outlined above are not totally acceptable. Parts V and VI and this paper will examine this conflict in detail in hopes of deriving a more suitable solution to this problem.

One further related problem remains to be discussed in this section. Is it possible, instead of avoiding a variation of rights clause altogether, for a company to alter the variation of rights clause itself or perhaps even delete it from the articles?

There is no direct authority on this point although the reasoning used above would seem to suggest that any attempt to alter a variation of rights clause is itself a variation of rights and therefore requires the procedure to be complied with before such an alteration is effected. This particular problem is dealt with expressly in the Ghana Act in section 47(3) which entrenches the variation procedure in the provisions of the Act similar to the Alberta, Ontario and Federal Acts.

C. The Articles of the Company do not Contain the Variation Procedure

The courts have not had to directly consider the more difficult procedural problems which arise in jurisdictions where the variation procedure is provided for only in the articles, and the individual company does not include such a provision in its articles. How can share rights be

altered? There are at least two possible alternatives. The problems arise only if there is more than one class of shares. If only one class of shares exist in a company, those rights will always be alterable by special resolution--whether or not share rights are included in the memorandum or articles.

One approach, favoured by Gower[26] and other writers, is that once shares have been issued without a procedure for variation in the articles, then those rights cannot be altered except with the consent of all individual members or via a court authorized scheme of arrangement. Proponents of this approach rely on section 23 of the U. K. Companies Act for support.

23. Power to alter conditions in memorandum which could have been contained in articles

(1) Subject to the provisions of the last foregoing section and of section two hundred and ten of this Act, any condition contained in a company's memorandum which could lawfully have been contained in articles of association instead of in the memorandum may, subject to the provisions of this section, be altered by the company by special resolution:

Provided that if an application is made to the court for the alteration to be cancelled, it shall not have effect except in so far as it is confirmed by the court.

(2) This section shall not apply where the memorandum itself provides for or prohibits the alteration of all or any of the said conditions, and shall not authorise any variation or abrogation of the special rights of any class of members.

(3) Subsections (2), (3), (4), (7) and (8) of section five of this Act (except paragraph (*b*) of the said subsection (2)) shall apply in relation to any alteration and to any application made under this section as they apply in relation to alterations and to applications made under that section.

(4) This section shall apply to a company's memorandum whether registered before or after the commencement of this Act.

This section provides that if the rights attached to shares are included in the memorandum they cannot be varied by a special resolution but only by the procedure for variation expressed in the memorandum. If no such provision exists, no variation is possible.

There is also a Privy Council decision, Campbell v. Rofe [1932] A.C. 9, which implied a similar result at common law. In determining the rights of the directors in issuing certain preference shares, the court held:[27]

> If the memorandum prescribes the classes of shares into which the capital is to be divided and the rights to be attached to such shares respectively, the company has no powers to alter that provision by special resolution.

The second approach indicates that variations can be made by a direct alteration to the memorandum. When we considered the situation where a variation of rights procedure existed in the articles, it was argued that any direct alteration of the articles in question would in effect, constitute a variation of class rights and such a variation could only be effected subject to the terms of the variation of rights clause. However this argument will no longer apply where the variation of rights clause does not exist.

There is both statutory authority and case dicta to support the direct alteration proposition. Section 10 of the U. K. Companies Act provides that "subject to the provisions of this Act and to the conditions contained in the memorandum, the company may by special resolution alter its articles." As well, there is dicta in a series of cases arising out of the Andrews v. Gas Meter [1897] 1 Ch. 361 case to the effect that as long as the company has not

'entrenched' share rights (by expressly making them unalterable), they are variable merely by the passage of a special resolution. Restrictions upon this right are limited to the common law requirement that they must be bona fide and in the best interests of the company.

It is submitted however that the above approach is logically inconsistent. If this position is accepted, we are confronted with the paradoxical situation in which a shareholder is better protected where the articles contain a variation of rights clause than where they do not. A variation of rights clause can only be modified subject to the strict conditions of that clause which normally require that a specified majority of the shareholders of the class concerned consent to the resolution. A special resolution merely requires a three quarter majority in a general meeting of ordinary shareholders/who will usually not be the actual class concerned and may have interests either divorced or totally opposite from those of the affected class shareholders. The concluding inequitable effect of this position is that where the articles make no provision for the modification of class rights, a member of a particular class is in a worse position than he would be if the articles had in fact incorporated a typical variation of rights procedure.

Another argument for this view is suggested by the wording of section 72 of the U. K. Act. As noted earlier, it was suggested that the protection afforded by section 72 will only apply where a modification is made via the variation clause, and if no such clause exists, the safeguards of the section will be inapplicable. It seems illogical to believe that the legislature intended to give a minority better protection where there is a variation procedure than where there is not. This leads to the assumption that the

legislature did not contemplate that class rights would be modified merely by alteration of the articles.

There is another method by which class rights may be varied where the articles contain no variation procedure. No problems arise as to the allowability of this procedure, although from the company's point of view, it is more restricted. The method involves a two-step procedure by which the company first provides that a variation of rights clause is inserted into the articles by means of a special resolution and then the share rights are varied in accordance with that procedure. In the case of Re National Dwellings Society Limited (1898) 78 L.T. 144, the company followed such a procedure and that the court suggested that unless a variation of rights clause had first been inserted, the variation would not have been allowed.

The problems raised in this section indicate some of the uncertainty inherent in the laws of jurisdictions where the statute itself does not provide for the variation procedure. Obviously these shortcomings will have an important effect on the recommendations to be made later in this paper. It should be noted however that both the Ghana Code and the Saskatchewan Act have attempted to solve these problems in their Acts, leaving only the English Act in the unfortunate position of having this area of the law undecided. The Jenkins Committee[28] did recommend that where there was no variation of rights clause in the articles of a company, the articles should be deemed to include a provision similar to article 4 of Table A. The Committee also recommended that special share rights should not be varied except with the consent of the prescribed majority of the holders of the shares concerned. To date however these recommendations have not been implemented into the Act.

The Ghana Code provides in section 47(1) that the regulations must contain provision as to variation of rights although it is possible for the regulations to entrench those share rights. If such a provision does appear and the company in the future wishes to alter its share rights, section 47(4) sets out a variation procedure in which this may be accomplished.

Section 61 of the Saskatchewan Act also deals with this problem:

> **61.**—(1) Where a company has heretofore issued or hereafter issues any shares with special rights or restrictions attached thereto, and no such provision as is mentioned in section 60 is made by the memorandum or articles authorizing the variation of such special rights, the company by special resolution may vary such special rights or restrictions, and may enter into an arrangement with its members or any class of them with respect to any shares or class of shares held by them:
>
> Provided that no special right attached to any class of shares shall be interfered with unless a resolution agreeing to the variation or arrangement is passed at a separate meeting by, or a consent in writing to the variation or arrangement is signed by, members holding not less in the aggregate than three-fourths of the shares of that class and the special resolution is confirmed by the court wholly or in part.

Unlike the Ghana Act, the Sasktachewan section does not direct the company to place a variation procedure in its articles, but simply provides a variation procedure in the Act itself by which a company may make the changes. The section makes it clear that it provides the same protections for dissenting shareholders in this situation as in a situation where a variation of rights clause exists. This is not expressed in the Ghana Act although it is assumed that the same protections would apply there as well.

An important point to note about the Saskatchewan Act, which is not part of the Ghana approach, is that the

resolution is not valid until it is confirmed by a court. Thus in Saskatchewan, where no variation procedure is included in the articles, the company may vary, but the conditions for successful passage of the resolution are much more stringent for two reasons: First, a company must follow the procedure as outlined in section 61 and has no power to vary that procedure; second, court approval is required. The effect of this section is to be harsher on a company for not including a variation of rights procedure in its articles. There does not seem to be any good reason why preliminary court approval is required, especially because the Act expressly allows for an application to the courts by a shareholder who wishes to do so. This issue will be examined in more detail in later sections of this paper.

D. Who Should Make the Alterations?

A current position in Canadian corporate jurisdictions is that alterations to the memorandum or articles are a matter of 'internal management' of the company, and that directors alone may adopt or alter the articles or memoranda subject only to confirmation by the shareholders (see: Kelly v. Electrical Construction Company (1908) 16 O.L.R. 232). Thus only the directors have the power to institute variations of either share or class rights whether those rights appear in the articles or memorandum.

The new Federal Act however has instituted what the Dickerson Committee called a major change in the present law, by conferring on the shareholder the right to propose an amendment to either the articles of association (which corresponds to the memorandum of an Alberta company) or the bylaws (which correspond to the articles of an Alberta company). This right is found in section 169(]) and seems

to be based directly on the Dickerson recommendations.[29]

> **169.** (1) Subject to subsection (2), the directors or any shareholder may in accordance with section 131 make a proposal to amend the articles.

What is the effect of this change? There is no doubt that it broadens the scope of those who can play a role in controlling the operation of the company. The Act allows 'any' shareholder to propose such an alteration so that any shareholder, no matter what rights are attached to his shares seemingly has this power. One of the major effects of this change will be that there will be more protection allowed to minority shareholders in protecting their share rights. Not only will they be allowed only to sanction resolutions designed to alter or vary their rights but they will now have the use of this right in order to propose alterations which could strengthen or entrench their share rights. Although it remains to be seen how practically effective this remedy will be due to the fact that most companies incorporated in Alberta are small private companies and the majority shareholder has de facto control of the directors anyway, the right does present a useful alternative to a shareholder who under the Federal Act does not want his right varied but also does not want to sell out to the company. Using this right, he may still have a way to protect his share rights so that he can remain a shareholder in the company.

V. PROTECTION OF CLASS AND SHARE RIGHTS IN THE ALTERATION PROCEDURE

To this point we have examined the nature of share and class rights, why a company might require to alter those rights and the procedures involved in the actual variation.

This section completes the examination by looking at the protections available to shareholders whose rights are being affected. In practical terms this is the area of greatest importance because the law and the courts have been deeply involved in these questions. Indeed in this section the conflict between the desire for corporate efficiency versus the desire to protect the rights of minority shareholders plays a fundamental role. It will remain for us to examine how successful the various protections have been in coping with this conflict.

It is submitted that there are three kinds of protection available for shareholders to protect their share or class rights and this section will examine each of those protections in detail.

A. The Procedure Itself

As we have seen, the actual variation of rights procedure, whether it is contained in the Act or in the articles, provides for some protection of the rights of a shareholder. As our examination in Part IV revealed, although the approach of jurisdictions may vary, there are some common features basic to all.

Except for the American jurisdictions examined, all Acts provide that a special resolution be passed in a separate meeting of the class whose rights are affected. Features of the special resolution include a requirement that a majority be 50 percent and that the company is obligated to give some of notice to the shareholders of the proposed resolution. These features are inherently designed to provide greater protection for shareholders as compared to the features of the ordinary resolution indicating that these kinds of alterations have traditionally

been considered by the courts and the legislators as sufficiently important enough to require special protection. The requirement of a separate class meeting as well adds to the protection afforded to shareholders because it allows them to make their decision unfettered by any pressures which may be exerted on them by other shareholders at a general meeting.

A second protection is included in the variation procedure in Alberta as well as British Columbia and Saskatchewan in some cases. Before a variation resolution is valid, it must first be approved by the courts in Alberta. The same holds true for a company under the Saskatchewan Act which has not included a variation of rights clause in its articles. In British Columbia a reporting company must get the approval of the B. C. Securities Commission.

All other jurisdictions provide a mechanism by which a dissenting shareholder may apply to court. However those appeal procedures are not part of the positive variation procedure. In other words, unlike Alberta, the court cannot examine the validity of the resolution until the requisite number of shareholders decide to bring the necessary application to the courts. Without such action on the part of the shareholders, the court has no jurisdiction to examine the resolution. Nevertheless, in both situations it is presumed that the court is bound by the same common law and statutory guidelines in making its assessment as to the validity of the resolution. It is those guidelines which bring us to an examination of the second and third types of protection available to shareholders.

B. The Common Law Guidelines

The question to be discussed in this section is whether the voting or majority shareholders are bound by any common law duties in proposing alterations to the articles or memorandum which will affect share or class rights. As will be seen, the majority shareholder does have such a common law obligation. He must show that when he voted in favour of the alteration he acted 'bona fide for the benefit of the company as a whole' or as Gower puts it--"just as the fiduciary duties of directors impose upon them certain objective restraints to which they are subject irrespective of subjective good faith on their part, so it seems due the so-called fiduciary obligations of the controlling shareholders."[31] Is there a general test or principle by which we can examine those guidelines placed on the majority shareholders?

The first restriction on the class shareholder is ironically the class itself. In a case where an individual holds more than one class of shares and the variation of one class will have the effect of benefitting his overall personal interest in the company although not necessarily benefitting the affected class, the Privy Council has held that:[33]

> No doubt he was entitled in giving his vote to consider his own interests. But as that vote had come to him as a member of a class he was bound to exercise it with the interests of the class itself kept in view as dominant...

The major common law restriction on the rights of the majority shareholder is, to quote the leading case in the area:[34]

> ...The power must be exercised not only in the manner required by law, but also bona fide for the benefit of the company as a whole.

Although the above may appear as a concise statement of the law, there have been numerous conflicting interpretations of the above Allen statement. Both the courts and academic writers have applied various criteria to the dicta in attempting to formulate tests which have had no other effect but to confuse this area of the law. However all the tests which have developed are based primarily on an examination of two factors: (a) The majority must bona fide believe the alteration to be beneficial to the company. (b) There is a requirement that there be some other limitation placed on the majority power by the courts.

The Court of Appeal in Greenhalgh v. Arderne Cinemas [1951] Ch. 286 attempted to formulate a conclusive test on the subject and clear up the confusion. Eversheds M.R.'s famous dicta from the case is as follows:[35]

> " Certain principles, I think, can be safely stated as emerging from those " authorities. In the first place, I think it is now plain that ' *bona fide* for the " benefit of the company as a whole ' means not two things but one thing. " It means that the shareholder must proceed upon what, in his honest " opinion, is for the benefit of the company as a whole. The second thing " is that the phrase, ' the company as a whole ', does not (at any rate in such " a case at the present) mean the company as a commercial entity, distinct " from the corporators: it means the corporators as a general body. That is " to say, the case may be taken of an individual hypothetical member and it " may be asked whether what is proposed is, in the honest opinion of those " who voted in its favour, for that person's benefit.
>
> " I think that the matter can, in practice, be more accurately and pre- " cisely stated by looking at the converse and by saying that a special " resolution of this kind would be liable to be impeached if the effect of it " were to discriminate between the majority shareholders and the minority " shareholders, so as to give the former an advantage of which the latter " were deprived. When the cases are examined in which the resolution " has been successfully attacked, it is on that ground. It is therefore not " necessary to require that persons voting for a special resolution should, " so to speak, dissociate themselves altogether from their own prospects and " consider whether what is thought to be for the benefit of the company as a " going concern (*sic*). If, as commonly happens, an outside person makes " an offer to buy all the shares, *prima facie*, if the corporators think it a fair " offer and vote in favour of the resolution, it is no ground for impeaching " the resolution that they are considering their own position as individuals."

However the confusion which Evershed, M. R. hoped to alleviate is still apparent in that at least three tests have been derived from his interpretation of the Allen test. Can we attempt to formulate some conclusions as to the duties on the majority shareholder? Clearly, the position based on the Greenhalgh case and the interpretations placed on it, indicate a subjective test. In the first instance, if the majority shareholder himself believes an alteration is bona fide, a strong presumption is raised that the alteration is in fact valid. However, there seem to be a number of factors which will the court will examine. They include the proper purpose of the alteration, whether there is any discrimination of the minority shareholder, and what a 'hypothetical member' would do. In examining these factors, the court will apply a more objective determination based on what a reasonable shareholder would have done in the circumstances. However the court will in almost all cases reject an alteration solely on the basis that the court itself thinks it an improper alteration. The courts have been quite loathe to get involved in the actual business of running a company.

For comparative purposes, it is interesting to note an American approach in this subject area. American courts have also had a difficult time in applying the proper criteria to this problem. A test, as applied in some American jurisdictions including California, known as the Ballantine Test, is as follows:[36]

> Changes in the rights of outstanding shares may be valid if they can be justified as an exercise of fair business discretion in meeting the needs and exigencies of the corporate enterprise. The more urgent the need or the emergency the more drastic the amendment or adjustment which fairness will permit.

Under the Ballantine Test the burden is upon the proponents of the change (usually the management) to demonstrate (1) the business need or exigency requiring the change, (2) the fact that the amendment would appear to help or meet the need or exigency, and (3) the fact that adoption of the amendment would appear to be an exercise of fair business discretion in meeting such need. The important point to note is that the factors noted above seem to take more into account the business realities of the situation than does the current Canadian position. The current Canadian position suggests that in most cases, the majority shareholders will be able to affect most of the changes they desire. As far as protection of the minority shareholder go therefore, the courts, in their desire to maintain a position of judicial non-interference, have utilized both a subjective approach and have formulated tests, such as the 'hypothetical member' test, which are very difficult to apply in practice. In contrast we noted an American approach which takes into consideration more of the business realities of such an alteration. The concluding effect is that, faced with an alteration which has an actual discriminatory effect in terms of practical business realities on the minority shareholder rights, protection provided by the common law is minimal.

C. Statutory Protections Available to Dissenting Shareholders

1. Statutory Appeals Sections

Many of the statutes which we have examined contain an appeals provision by which dissenting shareholders may apply to have the court to set aside a variation application. In other jurisdictions, the court must approve all variation resolutions before they become valid. Unfortunately, none of the Acts set out the conditions under which the courts should sanction an alteration to the articles. "The statute

itself gives no guidance and imposes no limit as regards the grounds on which the judicial discretion is to be exercised."[37]

It appears that there are two separate occasions when a shareholder would want to invoke these appeal sections and those occasions will be dealt with in this section.

(a) Judicial Interpretation of the Terms 'Vary', 'Alter', etc.

The first occasion and perhaps the most important one, where a shareholder would want to invoke these procedures, is when the shareholder claims that the proposed alteration is a variation of his rights and wants the court to so determine. If the court does decide that it is a variation it has a discretion to set it aside. Thus it is necessary for the shareholder to first prove that the proposed alteration is a 'variation' or 'alteration' as per the clause in the variation procedure, whether it be located in the Act or in the articles. Note that this also applies to an Alberta shareholder, because the court, in examining whether the resolution falls under section 38(1) or section 69(2), therefore requiring court approval, will have to decide whether the resolution is a 'variation' as per section 38(1)(a)(iii) or section 69(2).

If there is but one class of shares in a company, they will necessarily be voting shares and as we have seen, no special rights will attach to them. Any variation to those rights will require a company to propose a special resolution because it involves an alteration to the articles or memorandum. Thus the protection for minority shareholders will always be provided.

When, as in the usual case, the company provides for more than one class of shares, different rights are naturally attached to each class, and the rights of the preference or non-voting shares will be recognized as requiring the protection of a variation of rights procedures when certain of those rights are proposed to be altered. There are two possible situations in which the interpretation of the words 'variation', 'alteration', etc. must be examined: (1) Where the voting shareholders desire to vary the rights of the non-voting or special shares. (2) Where the voting shareholders desire to vary their own rights which will then have an indirect effect on the rights of the preference or non-voting shareholders.

(1) An examination of this type must first begin with a perusal of the wording used in the various Acts we have discussed. The Alberta Act, in sections 38 and 69 talk in terms of 'varying' the rights attached to shares. Other older Acts use the words 'variation or abrogation' and many Acts include a section similar to section 72(6) of the U.K. Act:

> (6) The expression "variation" in this section includes abrogation and the expression "varied" shall be construed accordingly.

The proposed variation of rights clause found in the articles contains words such as 'vary', 'modify', 'affect', and so on.

The situation to be dealt with in this section, namely a variation proposed by the voting shareholders on the non-voting shares, is the typical kind of variation procedure. Indeed, all the cases that have dealt with this issue are on this point. The newer corporate Acts have to some extent attempted to remove themselves from the restrictions which we will see have developed due to the limited interpretation placed on these words by the courts. Those

sections will be dealt with after the case law has been examined.

The first major case dealing with the interpretation of the words 'altered, modified, dealt with or affected in any manner whatsoever', was Re MacKenzie and Company Limited [1916] 2 Ch. 450. The voting shareholders wished to reduce its capital and make it a ratable deduction on all shares both ordinary and preferred. The practical effect of this was to reduce the dividend of the preferred shares. However the court held that this attempted reduction did not fall into the category of an action requiring a variation of rights procedure to be followed. To quote from the case headnote:[37]

> Where under the memorandum and articles preference shareholders have no priority as to capital and no voting power...and the company has power to reduce capital, the ratable reduction on all shares, preference and ordinary, though diminishing the actual preference dividend, is not an alteration of the rights of the preference shareholders so as to require their sanction under an ordinary modification of rights clause.

The next important case considered by the court was Greenhalgh v. Ardene Cinemas [1946] 1 All. E.R. 512, C.A. The court considered the effect of a variation of rights clause using the term 'vary'. The court held that a proposal to subdivide 10s 0d.shares so as to make their voting power five times as great and thus be able to outvote shares held by the plaintiff, did not involve a variation of his rights:[38]

> The effect of this resolution is of course, to alter the position of the 1941 2s. shareholders. Instead of Greenhalgh finding himself in a position of control, he finds himself in a position where the control has gone, and to that extent the rights of the 1941 2s. shareholders are affected as a matter of business. As a matter of law, I am quite unable to hold that, as a result of the transaction, the rights are varied, they remain what they always were...

Note the distinction made by the court between matters of business and matters of law. By using this approach, the courts cannot give affect to alterations which are in fact serious interferences with the business rights of non-voting shareholders.

In the leading case on point, White v. Bristol Aeroplane Company Limited [1953] Ch. 65, the variation of rights clause in question included these words: "All or any of the shares may be affected, modified, varied, dealt with or abrogated..." The voting ordinary shareholders desired to increase both the common and preferred shares by issuing both common and preferred shares to the current ordinary shareholders. This would have given the ordinary shareholders a majority of the preferred votes on matters which were solely the matter of that class of shares. In effect therefore, by issuing the new preference shares, the ordinary shareholders could control the non-voting shares.

The court was asked to consider this plan in terms of whether it 'affected' the rights of the preference shareholders who argued that 'affect' was a:[39]

> word of the widest importance must be taken to cover a transaction which though not in any modifying or varying rights, would in some way otherwise affect them.

However the court rejected this contention. After examining the article in question 'as a matter of construction', Evershed, M. R. rejected the wide use of the word 'affect' and went on to formulate a very strict test in outlining the limits to which interpretation of the word 'affect' could take:[40]

> It is necessary first to note that what must be affected are the rights of the preference shareholders. The question then is--are the rights 'affected' by what is proposed?...No, they are not; they remain exactly as they were before; ...It is no doubt true that the enjoyment of, and the capacity to make effective, those rights is in a measure affected...The existing preference shareholders will be in a less advantageous position...but there is to my mind a distinction between an affecting of the rights, and an affecting of the enjoyment of the rights...

This strict test was reiterated by the same court in the same year in In Re John Smith's Tadcaster Brewery Company Limited [1953] Ch. 308.

The question arises as to the actual import of the use of the variation of rights clause in terms of protection of the non-voting shareholder. Gower has called the results of the above cases 'shocking' and it seems apparent that notwithstanding any of the words which are traditionally used in these kinds of clauses, or in the statutory provisions, courts will place a very restricted and impractical interpretation on them.

The courts do however give us an insight as to the perspective used by the courts in examining the situations. Evershed, M. R. in the White case said:[41]

> I have no doubt, that what is here suggested will affect the preference shareholders as a matter of business...But we are concerned with the question whether the rights of the preference shareholders are 'affected' not as a matter of business, but according to the articles, that is according to their meaning construed under the rules of construction and as a matter of law.

Again in Re John Smith's Tadcaster Brewery Company Limited, Evershed, M. R. said:[42]

> It is to be noted that the court...decided that the word 'affect' in articles of this kind is not to be given so broad a sense as to mean or cover anything in a business sense.

The approach by the courts is therefore, quite obviously, an approach which takes no account of the business realities of an apparent alteration of the rights of non-voting shares. In all the above cases, the rights of the non-voting shareholders 'affected' or 'varied' in a true business sense in that the value of their shares has been lowered due to some adjustment of one of their special rights affecting those shares. And althougn the courts are quite willing to admit that this kind of variation exists, they have not felt the need to apply their discretion to prevent it.

The courts indicate that they are unwilling to open the 'floodgates' in this area:[43]

> Carried to its fullest extent, the argument must mean that any activity on the part of the directors in pursuance of their powers which may in any way affect or touch the value of any of the privileges attached to the preference shareholders, would be rendered ineffective save with the prior sanction of a special meeting of the preference shareholders. Such a conclusion obviously runs counter to the ordinary conception of the relationship between preference and ordinary shareholders in a company of this character.

At least one writer agrees with this position:[44]

> In fact, there are few acts done by a company which do not affect the value of its shares to some extent, however small, so that the wide interpretation of the requirements of a class consent would result in the preference shares becoming a second Board of Directors with a power of veto over the decisions of the duly constituted Board.

It is submitted however, that the 'ordinary conception of the relationship between preference and ordinary shareholders' involves more of a realization of the business realities of the situation than the courts are prepared to assume. The protection currently afforded the non-voting shareholders in attempting to force the voting shareholders to invoke the variation procedure will arise only it seems where there is a direct interference with their rights. Any other alteration, whether it affects actual business rights or not, will not be protected by the courts. On the other hand, Professor Pennington's argument has some merit. To allow non-voting or preference shareholders the right to, in effect veto a company's action is a severe restriction on the effective management of the company and is quite undesirable. It is perhaps for this reason that the courts have developed such a strict interpretation of the law in this area.

The failure of the courts to provide necessary protection in this area has led to some alterations in the new corporate Acts. In the Ghana Code, Professor Gower has attempted to abrogate the effect of this line of cases. The approach he uses deals more with the specific situations which have arisen out of the cases:

> 2. There is also the problem of what amounts to a " variation of rights ". It seems that n increase in the size of one class (*e.g.*, on a sub-division of the shares of another class or a pitalisation issue to another class) does not amount to a variation notwithstanding that it ay materially affect the voting ratio of the two classes: *Greenhalgh v. Arderne Cinemas Ltd.* 1946] 1 All E.R. 512, C.A.; *White v. Bristol Aeroplane Co.* [1953] Ch. 65, C.A.; *Re John Smith's ddcaster Brewery Co.* [1953] Ch. 308, C.A. Again in the shocking case of *Re MacKenzie & Co.* 1916] 2 Ch. 450, where preference shares were entitled to a dividend expressed as a percentage f the par value but shared equally with the ordinary shares on a winding up, it was held that rateable reduction in the capital of both classes did not " vary " the rights of the preference hareholders notwithstanding that its effect was to cut their fixed dividend to the advantage of he ordinary shares. Nor, probably, is an increase in the number of shares of a class regarded s a variation, notwithstanding that if the new shares are issued to other people it clearly lters the financial and voting ratio of the existing shareholders of that class.
>
> **(5) Any resolution of a company the implementation of which would have the effect diminishing the proportion of the total votes exercisable at a general meeting of the company the holders of the existing shares of a class or of reducing the proportion of the dividends or d tributions payable at any time to the holders of the existing shares of a class, shall be deemed be a variation of the rights of that class.**
>
> Finally, by subsection (5), the types of transactions referred to in paragraph 2 require class consents. For example, it will not be possible to increase the number of issued Ordinary shares, unless the Preference shareholders consent, if the latter's voting power is thereby decreased. To my mind this imposes no hardship; all that will be necessary is to increase the number of the votes attaching to their shares so as to preserve the existing balance of power.

Although this will undoubtedly clear up in the specific areas as noted in this section, it might not be general enough to cover a situation which might arise in the future.

Neither of the two newer provincial Corporate Acts, in Ontario or B. C., have adopted an approach which would abrogate the current restrictions on the interpretation of the terms used in the variation procedure. The Ontario Act uses the words 'delete' or 'vary' while the B. C. Act talks in terms of rights 'prejudiced or interfered with'. It is uncertain how the courts will interpret the new British Columbia phrase although it is arguable that the new terminology will not have a significant effect on the case law on this subject.

The new Federal Act, in incorporating these kinds of variations into their 'fundamental change' section has made a very significant alteration in the law. Based on the Dickerson Committee proposals which were designed to abrogate the principles as formulated from the White case and give practical effect to the business realities of the situation, section 14.03(1) of the Dickerson Report was drafted as follows:

14.03

(1) The holders of shares of a class or, subject to subsection **(2),** of a series are entitled to vote separately as a class or **series** upon a proposed amendment to the articles that **would**

(a) increase or decrease any maximum number of authorized shares of such class, or increase any maximum number of authorized shares of a class having rights or preferences prior or superior to the shares of such class,

(b) effect an exchange, reclassification or cancellation of all or part of the shares of such class,

(c) change the designation, rights, privileges, restrictions or conditions attached to the shares of such class, and, without limiting the generality of the foregoing, that would

(i) cancel or vary prejudicially rights to accrued dividends or rights to cumulative dividends,

(ii) attach, cancel or vary prejudicially redemption rights,

(iii) reduce a dividend or liquidation preference,

(iv) cancel or vary prejudicially conversion privileges, options, voting, transfer, or pre-emptive rights, or rights to acquire securities of a corporation, or sinking fund provisions,

(d) increase the rights or privileges or any class of shares having rights or privileges equal, prior or superior to the shares of such class,

(e) create a new class of shares, or make any class of shares having rights or privileges subordinate or inferior to the shares of such class, equal, prior or superior to the shares of such class, or

(f) effect an exchange or create a right of exchange of all or part of the shares of another class into the shares of such class.

This section has become part of section 170(1) of the new Federal Act. As noted, the section is very detailed in setting out all the possible situations in which a class of shares may vote with respect to an alteration of rights. This removes any uncertainty from the law so that all shareholders will know when a variation of rights procedure must be instituted and when it need not be. The Federal Act goes as far as allowing a series of shares of a class to vote separately as long as the series is effected in a manner different from other shares of the same class.

(2) Shareholders desire to vary rights to voting shares which will affect the rights of non-voting shares.

This area does not seem to have been discussed in any great detail in either the case law or in the text books. The situation in this section usually arises where the common and preferred shares, or more than one class of preferred shares, are owned by the same people who desire to vary the rights of the common or voting shares, and this will in some way reduce the value of the rights attached to the preferred shares. The question is--do the non-voting shares have a right to invoke the variation of rights procedures when their rights are in some way affected by the variation to the voting class of shares.

There is no reported case law on this subject. All the cases relevant to this discussion seem to have been decided on the basis that some right of the preferred share was being devalued, for example, a diminishing of the proportion of total votes exercisable or a reduction of the proportion of the dividends or distributions payable, by an alteration to the preferred shares themselves. None of the cases examined dealt with an alteration to the common shares or

to other class of preference shares which would in effect devalue the rights of yet another class of preferred shares.

An unreported case which we examined earlier, Hodge v. James Howell, does indicate one opinion on this subject. In that case the voting shares attempted to vary their rights with regards to winding up by creating a new class of preferred shares which would rank ahead of the ordinary shares but behind existing preference shares. Thus although the rights of the first class of preference shares were not directly or even indirectly affected, and this was not a case where the variation was being made to the voting shares themselves, the court did make the statement which has some bearing on the issue at hand:[45]

> It was to be open to the company, having issued ordinary shares, to issue preferred shares ranking in priority to the ordinary shares, provided that the rights attached to those preference shares were subordinate to the rights attached to the original preferred shares...

The inference to be drawn from that statement is that the rights of the new preferred class, because they rank behind the existing preferred class, will not result in an interference with the existing preferred shares. Only if the rights of the new or preferred class were created equally to or in priority of the existing preferred class, would an action arise. However this statement must be read in the context of the cases which we have examined earlier. There does not seem to be any reason why the principles enunciated in those cases do not apply to the situation at hand. The test as enunciated in the White case would suggest that even if a new preferred class of shares were created so as to rank equal to or in priority of an existing class of preferred shares, this could not constitute a

variance of rights only perhaps a variation of the enjoyment of those rights, with no right to protection. Only a direct interference with rights would allow the courts to invoke the protection of the appeals section and by definition, there could never be a direct interference with rights in the situation we are discussing here, because the variation is being made not to the rights of the objecting class but to the rights of the voting class of shares. Therefore, common law would seem to have provided little or no protection for shareholders in the situation under discussion in this section.

It appears however that the newer corporate Acts have either intentionally or inadvertently, provided some opportunity for protection in this area. For example, section 248(1)(b) of the B. C. Companies Act allows not only those shareholders who voted against a special variation resolution to apply to court, but it allows ten percent of the shares of the class of shares of the company whose rights are affected by special resolution which alters or abrogates special rights of 'any' class of shares in the company. It appears therefore that this definition is broad enough to cover the situation where a variation is made to either a voting or other preferred class of shares and a preference shareholder wishes to challenge the validity of the resolution. However the major roadblock of the section is that it speaks in terms of 'abrogating or altering', which immediately involves an interpretation of those words by the courts and as we have seen, the interpretation of those words would make it unlikely that a preference shareholder could garner much protection from this section.

Section 189(4) of the Ontario Act requires the variation procedure to be invoke if an amendment varies a preference 'attaching' to a class of shares ranking 'in any

respect in priority to or on parity with an existing class of special shares'. This section suggests at least in the situation where the affected share rights are in priority to or an a parity with an existing class of shares, the preferred shareholders are entitled to invoke the procedure. Note that this position is similar to the position as noted in the James Howell case.

By far the greatest number of modifications have occurred in the new Federal Act. Like the Ontario Act, the Federal Act allows a class of preference shareholders to vote separately on a special resolution to increase the rights or privileges of any other class of shares having rights equal or superior to the aforementioned shares (section 170(1)(a) and 170(1)(d)). However the Federal Act goes further in providing protection in two other instances.

> 3.204(3) A corporation may liquidate and dissolve by special resolution of the shareholders or, where the corporation has issued more than one class of shares, by special resolutions of the holders of each class whether or not they are otherwise entitled to vote.

This section provides that if the corporation proposes a voluntary liquidation and dissolution of the company, it must be sanctioned by a resolution of each class of shares. More importantly however the converse situation seems to provide each class with a veto power to hold over the corporation in a case where the corporation desires to wind up. The Dickerson Report does not contain any information on this subsection. One possible source of the provision is section 49(2)(d) of the Ghana Act which is very similar to section 204(3). The main purpose of the Ghana section was to protect against the evil effects of non-voting and of weighted voting shares and to prevent voting being weighted in favour of

certain classes of shares. It was not therefore, primarily based on allowing some kind of special protection for preference shareh in terms of dissolution of the company. It would seem more advantageous to ensure that the rights of non-voting or preference shareholders are not prejudiced in any way if the company decides to wind up. But to give them an effective veto control over a decision which may have been made without prejudice and in the best interests of the company, seems to be a power which is too prohibitive on the company in terms of carrying on business. Such a right as is presently accorded shareholders in the Federal Act could easily turn into a powerful veto weapon.

The broadest protection afforded to non-voting or preference shareholders is the power given to shareholders of any class by virtue of section 184(2) of the Federal Act to dissent on any fundamental change.

> **184.** (1) Subject to sections 185 and 234, a holder of shares of any class of a corporation may dissent if the corporation resolves to
>
> (*b*) amend its articles under section 167 to add, change or remove any restriction upon the business or businesses that the corporation may carry on;

Note that this right is available only to preference shareholders who are allowed a vote under section 170. This means in effect that only those shareholders falling into the category represented by sections 170(1)(a) and 170(1)(d) will be allowed to dissent and therefore opt out of the company by requiring the company to buy their shares from them at a price determined by the court. However this right is not extended to any other class of shareholder.

Returning to the position as it now is in Alberta, the question arises as to the position of the courts if they in fact determine that a variation resolution is a 'variation' of a share or class right. If the courts find a variation has occurred, they then have a discretion to approve or disaffirm the resolution. The criteria to be used by the courts is not expressed in the Alberta Act, although as we noted earlier, the U. K. Act uses the 'unfairly prejudicial criteria'. Although there is no reported case law on the subject, it is submitted that an Alberta court as well as any other court in the jurisdictions we have considered would use similar guidelines in determining whether the alteration was bona fide and in the company's best interest. Indeed, it appears that basically the same criteria used in determining common law guidelines examined in Part B of this section, would be utilized by the courts under a statutory appeal, with perhaps special emphasis as to whether the proposed alteration constituted a fraud on the minority or was unfairly prejudicial to their rights. As we noted earlier, the case law in this area suggests that only in the cases of extreme oppression or fraud will the court overturn a decision reached by the majority of the shareholders in a company.

Mr. H. Shandling, in an article[45a] has compiled a short list of some of the considerations used by the courts in approving a resolution (which is the position in Alberta regarding variation resolutions due to section 38(1) and section 69(2)). This list is reproduced in Appendix A of this paper.

(b) Ensuring the Variation Procedure is Followed by the Company

The second way in which a shareholder can use the statutory appeal section is to ensure that the majority

shareholders have properly and carefully studied the variation procedure. Assuming that the company desires to 'alter' or 'vary' class rights in such a way as to fall under the court's interpretation of what those words mean, the shareholder is entitled to rely on the protection afforded him by the procedure itself i.e. a separate class vote and a special resolution of the affected class. If the company has not followed that procedure, a shareholder in a jurisdiction where the appeal section is set out in the Act, can definitely apply to a court to have the resolution set aside on the basis that the company has not adhered to the statutory requirements of that section. If the shareholder brings an action in a jurisdiction where the variation procedure is set out in the articles, on the authority of the Crompton decision as well as the other arguments noted earlier, the court would also have the power to set aside that resolution.

It should be noted that this appears to be strictly a procedural remedy and there is nothing to stop a majority from reintroducing the resolution at a later time and if the proper procedure is followed, it will become valid at that time. However in situations like the Fisher case, the non-voting shareholders would be protected. As well, the costs of losing a court action might persuade the majority shareholder that such a resolution is not worth the expense or in the best interests of the company.

2. The Statutory Remedy for Oppressive and Unfairly Prejudicial Conduct

In some jurisdictions, a minority shareholder whose rights have been affected in a manner which he believes amounts to oppressive or prejudicial conduct, has a special remedy which allows him to apply to the courts for a wide range of judicial relief. These sections are based upon

section 210 of the U. K. Companies Act which itself was based upon recommendations of the Cohen Committee.[46]

210. Alternative remedy to winding up in cases of oppression

(1) Any member of a company who complains that the affairs of the company are being conducted in a manner oppressive to some part of the members (including himself) or, in a case falling within subsection (3) of section one hundred and sixty-nine of this Act, the Board of Trade, may make an application to the court by petition for an order under this section.

(2) If on any such petition the court is of opinion—

(*a*) that the company's affairs are being conducted as aforesaid; and

(*b*) that to wind up the company would unfairly prejudice that part of the members, but otherwise the facts would justify the making of a winding-up order on the ground that it was just and equitable that the company should be wound up;

the court may, with a view to bringing to an end the matters complained of, make such order as it thinks fit, whether for regulating the conduct of the company's affairs in future, or for the purchase of the shares of any members of the company by other members of the company or by the company and, in the case of a purchase by the company, for the reduction accordingly of the company's capital, or otherwise.

(3) Where an order under this section makes any alteration in or addition to any company's memorandum or articles, then, notwithstanding anything in any other provision of this Act but subject to the provisions of the order, the company concerned shall not have power without the leave of the court to make any further alteration in or addition to the memorandum or articles inconsistent with the provisions of the order; but, subject to the foregoing provisions of this subsection, the alterations or additions made by the order shall be of the same effect as if duly made by resolution of the company and the provisions of this Act shall apply to the memorandum or articles as so altered or added to accordingly.

(4) An office copy of any order under this section altering or adding to, or giving leave to alter or add to, a company's memorandum or articles shall, within fourteen days after the making thereof, be delivered by the company to the registrar of companies for registration; and if a company makes default in complying with this subsection, the company and every officer of the company who is in default shall be liable to a default fine.

(5) In relation to a petition under this section, section three hundred and sixty-five of this Act shall apply as it applies in relation to a winding-up petition, and proceedings under this section shall, for the purposes of Part V of the Economy (Miscellaneous Provisions) Act, 1926, be deemed to be proceedings under this Act in relation to the winding up of companies.

Section 210 and its Canadian counterparts, section 221 of the B. C. Act and section 234 of the Federal Act provide a flexible tool for use in protection of the minority shareholder. They allow a court to apply general standards of fairness in order to achieve a solution in a

conflict between minority shareholders and the company without ordering cessation or severe restrictions on the affairs of the corporation. The courts however are firm in their belief that judicial interference should occur only when there is some particular abuse of minority rights and only to the extent necessary to protect those rights.

It is outside the scope of this paper to examine in depth the development, use, rationale or criticisms of these general remedy sections. Suffice it to say that if a minority shareholder can fit his case within the confines of the Act, the courts have a very broad discretion to make an order to protect those rights.

The Alberta Act does not contain a section similar to section 210 so this remedy obviously does not apply in Alberta for provincially incorporated companies. Section 221 of the British Columbia Companies Act provides for relief from 'oppressive or unfairly prejudicial conduct'. The broadest section of this kind is found in section 234 of the Federal Act. It has incorporated all of the major recommendations of the Jenkins Committee Report, each of which was designed to alleviate restrictions found in the original British section. The Lawrence Committee recommended against the inclusion of such a provision in the Ontario Act, expressing dissatisfaction with section 210, indicating that the

> Underlying philosophy of section 210 has an air of reservation and defeatism about it as if the legislature was unable to offer any solution to the plight of minority shareholders other than abandoning the problems to the judiciary to be dealt with ad hoc...

As a result the Ontario Act does not contain this provision.

With regards to shareholders rights, the inclusion of this kind of section tends to reinforce the protection of minority shareholders. Note that the wording of section 72 of the British Act is quite similar to the wording of section 210 of that same Act. In the Federal sphere, section 234 offers an alternative method to minority shareholders who do not wish to opt out of a company but instead desire to have their rights protected by an order of the court. If they qualify for protection under the Act, the court has the wide and flexible power to protect rights in contrast to the single remedy the shareholder has under a dissent provision in the Federal Act, namely, the power to opt out of the company.

VI. CONCLUSIONS AND RECOMMENDATIONS

After having canvassed the law as it is applied in Alberta and other jurisdictions, we are now confronted with the task of deriving conclusions and proposing recommendations for improvements in the law with regard to share and class rights. It is apparent from the previous discussion that many aspects of both the procedures for variation and the protections afforded variation are less than adequate in many cases.

Conclusions and recommendations will be examined in terms of the following three questions:

(1) How should corporate legislation provide for the definitions of shares, share rights, etc.?

(2) What are the most effective procedures for allowing a company to vary their rights of shares or specific classes of shares?

(3) What are the most effective ways of providing protection for the rights of shareholders affected by the variation procedures?

1. Corporate Legislation

Only the Ghana Act attempts a substantive definition of "share" in a corporate act and as was noted earlier, this definition adds little to the current common law position as to what a share is. Similarly, the Ontario Act outlines detailed definitions of 'common', 'preferred' and 'special' shares. An even more complex system is found in the North Carolina Business Corporations Act, sections 55 to 71 which require a designation on each class of shares to distinguish one series from another series. The Federal Act, in contrast, utilizes a simple system which abolishes such terminology for types of shares and allows a company to provide for as many types and classes of shares as they desire. All the Acts which have been examined do provide, either expressly or impliedly, that companies be allowed to structure their capital in any way they want, subject only to restrictions in the Act and the company articles. At least one class of shares in any company must be voting shares.

When determining how this problem of share definition is to be handled in an act, care should be taken to note the practical aspects of the situation. In Alberta, it is possible that the concepts of common and preferred shares have been ingrained into society, not only among trained lawyers or experienced business men, but among the general investing public as well. Any attempt to alter these concepts or eliminate them, must be carefully considered.

It should also be noted that although the approaches of the various acts differ with regards to classification of shares etc., none of those acts actually advocate any major reforms to the concepts of 'snares' or 'classes of shares'. That is, the concept of what rights are delineated in either ordinary or preferred shares has not been altered--only broadened and in some of the acts, significantly simplified.

Keeping in mind the objectives of simplicity and flexibility discussed in section 3, an approach similar to the Federal Act is favourable. With the impact of other legislation requiring full disclosure of the nature of shares in public companies (Securities Act), there would seem to be less concern with the requirements for disclosure of classes of shares by name. Most corporations in Alberta are small private companies. The designation of types of shares would not be a major problem in private companies either however because potential shareholders would surely inform themselves of the nature and rights of the shares they were contemplating purchasing. It is therefore recommended that this approach be adopted for use in Alberta. Corporations should be allowed to provide for any number of class of shares, with any conditions, restrictions, rights or privileges attached to those shares as the company so desires. Subject to a determination that terms such as 'common' and 'preferred' could be eliminated from use in the Act without harming the effectiveness of the system, it is recommended that revisions to the Alberta Act do not contain explicit references to classes of shares by such imprecise terms as common, preferred, special and so on.

It is accepted law that at least one class of shares in a company must contain, at minimum, a right to vote and a right to a distribution of the assets upon winding up. All other classes of shares may contain those rights plus any other preferences,

conditions or rights as the company so desires. For the first time in Canadian corporate law, the Dickerson Committee recommended that all shares automatically contain the right to vote and put the onus on the company to remove this right or provide restrictions upon it, providing at least one class has a vote in election of directors and of the auditor of the company. The Federal draftsmen did not accept this proposal and have provided that only one class of shares be required to have a vote and to participate in the winding up of the company. This is in effect a statutory requirement for a class of common shares (section 24(4)).

The provisions of the Ghana Act should be noted in this regard. Preference shareholders are given the right to attend general meetings and vote at all times in the following cases:

> **(2) Notwithstanding any provision in the Regulations any preference shares issued after the commencement of this Code shall carry the right to attend general meetings and on a poll thereat to at least one vote per share in the following circumstances, but not otherwise, that is to say—**
>
> **(a) upon any resolution during such period as the preferential dividend or any part thereof remains in arrear and unpaid, such period starting from a date not more than 12 months, or such lesser period as the Regulations may provide, after the due date of the dividend; or**
>
> **(b) upon any resolution which varies the rights attached to such shares; or**
>
> **(c) upon any resolution to remove an auditor of the company or to appoint another person in place of such auditor; or**
>
> **(d) upon any resolution for the winding up of the company or during the winding up of the company.**

These sections were included in the Act to deter the principle of the non-voting share and to prevent voting from being weighted in favour of certain classes. They apply only to preference shares which are narrowly defined in the Ghana Act as shares which "do not entitle the holder thereof to any right to participate beyond a special amount in any distribution." However with the inclusion of this section in the Act it in effect provides specific classes of shares

with an automatic right to vote. We must examine these rights in light of the situations provided for in the Ghana Act.

Section 49(2)(b) deals with the topic that this paper is primarily based upon. It is inherent that when rights of a class are varied, shareholders of that class should have a right to vote.

The other three circumstances which allow preference shareholders to vote deal with topics which are basically outside the framework of this paper. It will not be necessary to examine in detail each case.

From the point of view of classifying share rights, however, there does not seem to be any good reason to automatically provide for voting rights on all classes of shares, subject to the removal of them or restrictions placed upon them by the company. Often, voting rights are not considered a 'selling point' from the potential investor's point of view, who wishes to invest in the company for reasons other than a right to play a role in the management or control of the company. As well, companies could easily remove the right to vote by amendment to their articles or perhaps provide for voting rights only in certain circumstances and then ensure that those circumstances never occur. In either case, the non-voting shareholder has gained no advantage and perhaps has even suffered a detriment. There should however be an express provision in the Act to ensure that at least one class of share contains voting rights and the right to participate in a winding up. All other share and class rights, subject perhaps to restrictions such as are placed in the Ghana Act, should be left up to the individual companies themselves.

2. Discussion of the Variation Procedures

In this section we will examine the ways in which the company may alter share rights in an efficient, flexible, simple manner, having regards both to requirements of the company and the various class rights of its shareholders.

The first consideration should be to determine exactly where share rights or class rights should be set out. Currently, many jurisdictions including Alberta, provide that these rights may be set out in either the articles or the memorandum. The memorandum/article dichotomy is followed in most other jurisdictions, although the nomenclature differs. Both the Federal and the Ontario Acts require that share rights be included in the articles of incorporation which are similar to the memorandum in Alberta. Although it is beyond the scope of this paper to undertake an examination of the merits of the relationship between the articles and the memorandum, it is strongly recommended that details of capitalization, including share and class rights, should be found in only one place. Alberta companies have widely utilized the practice of including share rights in the articles while placing the actual capitalization details in the memorandum. An important consideration in deciding this question is not only the current practice in Alberta but the degree of entrenchment of the rights. For example, should share rights go into the articles even though the company could make them virtually unalterable by requiring majorities of up to one hundred percent for alteration?

Currently of course, alterations to the articles can be effected much more simply than alterations to the memorandum. However this is basically a problem of procedure and mechanics and not one of share or class rights. For example, the Federal Act has significantly streamlined and

and simplified its procedure for a corporation which allows for alteration to the incorporating documents to be effected very simply and quickly. If such a practice is adopted in Alberta, it is recommended that share rights be included in the memorandum of the company or its equivalent. This recommendation is also based on a recommendation to be made later in this section which suggests that the variation procedure be included in the substantive provisions of the Act. Because the procedure itself will be contained in the Act, there will be no special advantage in placing share rights in the articles. Another advantage of placing all share rights in the memorandum would be uniformity both within the province and with other jurisdictions.

Section IV of this paper outlined two possible places where the variation procedure itself can be placed--in the actual provisions of the Act, or the articles of association. We must now examine the location where the variation procedure would be most effective.

The modern trend of corporate statutes provides for a variation procedure in the actual provisions of the Act, either by actually including the procedure in the Act as per the Federal, Ontario or B. C. Acts, or by making a variation clause a requirement of the articles, as per the Ghana Act. On the other hand, the Saskatchewan and U. K. Acts make provision for a variation procedure in the articles only. This means that a company need not include such a procedure in its articles thus leaving in doubt the question as to how a variation will be validly executed in those situations. The situations arise where a variation clause exists in the company's articles and conversely where such a procedure does not exist. Another problem which may arise under the Saskatchewan or U. K. Acts occurs if the class rights are defined not in the articles

or memorandum, but by resolution passed by the directors or a general meeting pursuant to a power in the articles. It is uncertain what procedure must be adopted to vary them if the articles and the resolution make no provision in that respect. It is arguable that the variation might be affected by an ordinary resolution in general meeting, since all powers of the company which are not delegated to the directors and are not required to be exercised by special resolution, may be exercised in that way. The counter argument, as noted earlier is that the company should be required first to install a variation of rights procedures in the articles, and then follow that procedure. The Fisher decision gave affect to the proposition that a company may alter share rights in exactly the same way as any other alteration to the articles. In contrast, the Crompton decision, the various academic writers, and the Jenkins Committee have favoured the requirement that the company, in altering share rights, have a super added burden to follow a variation proceeding. Where the company's articles do not contain a variation procedure, the issue is undecided although our earlier discussion noted two positions, namely, that if no procedure exists no rights can be altered unless a variation procedure is first inserted into the articles, and the opposite positions, that either a direct alteration to the article is required or that a company must first insert a variation of rights clause and then very pursuant to that clause.

Leaving the details of the actual variation procedure to be examined in the next few pages, it is recommended that the variation procedure should be set out in the substantive provisions of the Act. By requiring the procedure to be outlined in the Act, many of the very serious and undecided issues outlined earlier in section IV will be avoided. For example, under the Australian Act we noted the

two extreme positions which result when the variation is wholly contained in the articles. The Crompton case puts a severe restraint on corporate flexibility to make share alterations because the shareholders hold a potential veto power over the directors. In contrast, the Fisher position provides the necessary flexibility for the company, but severely limits the amount of protection a dissenting shareholder has.

The concept of share and class rights is much too important to be left to the company to decide whether a variation procedure must be included. It should be a fundamental basis of shareholder protection that such a procedure be set out in the Act. If the shareholders of the company wish to entrench the variation procedure requirements, this should be provided for in the provisions so that in effect the variation procedure would detail only minimum requirements to be followed. This would effectively provide for the same flexibility as is given in the Ghana Act which tells the company that they must include a variation procedure in their articles, but does not detail what the procedure should be. As well, the above recommendation has the advantage of uniformity, by setting minimum requirements for the variation procedure, especially in a private company, where considerable abuse can occur without there being any scrutiny on the activities of the corporation.

What should the variation procedure consist of? The first consideration must be to refer to the policy positions outlined earlier in this paper. Basically we must again note the conflict between minority and majority rights which has been developed throughout this paper. We must examine the proposed elements of the variation procedure in light of those policy positions.

The accepted concept of the variation procedure involves the requirement of a separate vote by each class of shareholders whose rights are to be affected. These separate class votes require a greater than a simple majority vote to be passed. As well most procedures provide for a mechanism by which a dissenting shareholder can apply to court for some kind of legal remedy.

No injustice can occur through variations in the share rights if only one class of shares exist in the company, save for the possibility of fraud on the minority. Shareholders are all affected in the same way. An alteration to the articles or memorandum may be affected by a special resolution only and there does not seem to be a need for anything more in the variation procedure.

When more than one class of shares exists the procedure is more complex. A primary requirement should be a separate class vote by each class whose rights are affected. The Federal Act goes even further and allows a separate vote for different series of classes of shares if the right series are themselves altered. A separate class vote will allow the shareholders to make a decision which hopefully will be based on what is best for that class of shares and any pressure exerted on those shareholders by other classes of shareholders will be reduced to a minimum.

The next requirement in a variation procedure is that of a special resolution. The concept of the special resolution itself inherently provides for protection of minority rights by requiring notice by the company to the shareholders specifying the intention to propose a resolution, and by requiring a majority greater than 51 percent. There seems to be no good reason to disregard the value of the special resolution. If enough of the minority shareholders

object to the resolution, they can effectively defeat it. Otherwise it will be validly passed. Currently in Alberta, there is confusion as to the actual majority required due to the ambiguities resulting from section 69(2) and section 38(1). Along these lines, it should be noted that the highest standard required for a special resolution is found in Ontario Act where section 189(4)(a) requires one hundred percent approval of the holders of the shares or classes of shares, and the lowest standard required is in the Federal Act where a two thirds majority is the required figure. It is submitted that the proper standard to be adopted should be one based on section 189(4)(c) of the Ontario Act except that the two thirds requirement should be replaced by the current three quarters of seventy-five percent required majority for Alberta shareholders.

> **(c) if the articles so provide, by at least two-thirds of the votes cast at a meeting of the holders of such class or classes of shares duly called for that purpose or such greater proportion of the votes cast as the articles provide,**
>
> **and by such additional authorization as the articles provide.**

This section should also provide for the same majority to sanction the vote if those votes are in writing. The advantage of this kind of section is that it is very similar, but much clearer to the current requirements in section 69(2) which is the standard now used in most of the share alterations proposed in Alberta companies. It also clears up the uncertainty now existing in the Alberta Act and is a section similar to other sections throughout Canada therefore having the advantage of uniformity. As well, the section talks in terms of minimum requirements so that the company may increase the numerical requirement if it so desires.

(c) Turning now to the actual wording to be used in the variation procedure, we note that the current state of the law with regards to the interpretation with words such as 'vary', 'alter', etc. is very restricted. These limitations, as illustrated by our examination of the White, Greenhalgh and MacKenzie cases, have led to severe inequities in providing protection for dissenting shareholders whose rights have been materially affected from a business point of view. As Gower argues:[48]

> The distinctions which the court have drawn are over-subtle and unsuited to matters of practical business as opposed to abstract journalism.

An objective of effective corporate legislation should be to give regard to practical situations as well as legal rights. In practice, changes by the voting shareholders to the non-voting shares often affect more than the mere 'enjoyment' of those rights--they can effect a serious financial depreciation of the share value in the market place. Therefore these alterations should not be allowed by a company without reference to the consent of the affected shareholders. As is argued in the Iacobucci Report:[49]

> It is therefore necessary for effective protection to provide for separate class votes not only where the class rights are altered directly but also where there is an indirect effect upon these rights as the result of an action in relation to the shares of another class, for example, upstream conversion into the class or leap-frogging of one class over another.

It is therefore submitted that the current common law restrictions which currently are in force in Alberta be

abrogated by changes to the provisions of the variation procedure.

As we noted earlier, the newer Canadian acts have made various changes in their procedures. While the older acts, such as the Alberta and Saskatchewan Acts talk in terms of 'variation and alteration', the new British Columbia Act in section 247(1), employs the term 'prejudiced or interfered with'. This term has not yet been judicially interpreted, and it is uncertain as to the effect the courts will give to these words although it is arguable that the words could be interpreted as narrowly as the words now used in the Alberta Act. The Ontario Business Corporation Act has required its variation procedure to be invoked via section 189(4) where the amendment is to 'delete or vary a preference, right, condition, restriction, limitation or prohibition attaching to a class of special shares'. These provisions are broader than the Alberta Act but could still be bound by current restrictions of judicial interpretation. The approach of the Ghana Code in section 47(5) attempts to remove the restricted interpretations effecting the case law by dealing with specific situations which have arisen in the cases i.e. 'reduction of the proportion of the dividends or distributions payable to the holders'. The limitation of this approach however is that it is confined to the situations which appear in the Act and does not provide the required protection for all possible situations where business rights will be involved.

Only the Dickerson Committee recommendations, which were accepted by the Federal draftsmen, have seemingly removed many of the common law restrictions by expressly detailing situations where the procedure is to be invoked.

170. (1) The holders of shares of a class or, subject to subsection (2), of a series are entitled to vote separately as a class or series upon a proposal to amend the articles to

(*b*) effect an exchange, reclassification or cancellation of all or part of the shares of such class;

(*c*) add, change or remove the rights, privileges, restrictions or conditions attached to the shares of such class and, without limiting the generality of the foregoing,

(i) remove or change prejudicially rights to accrued dividends or rights to cumulative dividends,

(ii) add, remove or change prejudicially redemption rights,

(iii) reduce or remove a dividend preference or a liquidation preference, or

(iv) add, remove or change prejudicially conversion privileges, options, voting, transfer or pre-emptive rights, or rights to acquire securities of a corporation, or sinking fund provisions;

(*d*) increase the rights or privileges of any class of shares having rights or privileges equal or superior to the shares of such class;

(*e*) create a new class of shares, or make any class of shares having rights or privileges inferior to the shares of such class, equal or superior to the shares of such class;

(*f*) effect an exchange or create a right of exchange of all or part of the shares of another class into the shares of such class; or

These provisions set out in detail the possible situations where separate class votes are required and as a result, any restrictions which existed at common law have been abrogated. It should be noted that the Federal Act provides not only the protection of the variation procedure for non-voting shares where their rights are changed as per the new wording of the Act, but also provides some protection where voting shares have been altered which indirectly have an effect on the non-voting shares. This will be examined in detail in the next section. The effect of this section will be to delineate in clear terms when a proposed variation by the company require the procedure to be invoked and where it does not, instead of leaving it up to the courts to try and interpret the meaning of words and phrases of general, imprecise meanings.

It can be argued that the effect of these provisions is to broaden the protection for minority shareholders at the expense of the effective operation of the company. It is submitted however that the changes only give effect to practical business realities which have always existed but have yet to be recognized by the courts as requiring protection. The corporation is not saddled with such a harsh burden due to these requirements. Indeed, by invoking it, the corporation is merely fulfilling its obligations to the shareholders to effect all changes in the best interests of the company as a whole. As well, as we shall note, the variation procedure in the Federal Act does provide the required flexibility because of the single remedy available to a minority shareholder...the appraisal right. It is therefore recommended that provisions similar to the above noted Federal provisions be adopted in Alberta.

We must now examine the role that the courts should play in the variation procedure. At present, there are

basically two approaches available in which the machinery of the court may be invoked. In two instances, the court plays a positive step in the variation procedure--the courts are required to approve a variation resolution before they become effective in the Saskatchewan Act where the articles do not contain a variation of rights clause, (section 61(1)), and in the Alberta Act for all variation resolutions under section 38(1) and section 69(2). Along these same lines, before a resolution of a British Columbia reporting company is sanctioned, it must be approved by the B. C. Securities Commission.

At this point, it is not necessary to examine the criteria which the court is using in examining these resolutions. That point has been dealt with in earlier discussion. The main issue is whether or not the courts should be utilized as they now are in Alberta. Based on the following reasons, it is suggested that the current procedure in Alberta be discontinued.

From my investigation into this area, which included a discussion with the Deputy Registrar of the Companies Branch of Alberta, and several practitioners in the City of Edmonton, it appears that court approval as required by section 169 and section 138 does not play an effective role either as a part of the variation procedure or as a mode of protection for minority shareholders. When these resolutions are brought before the courts, the usual procedure for an uncontested ex parte application is for them to be approved automatically without any kind of investigation into the merits of the resolution or whether it has adversely affected the rights of minority shareholders. It appears that in practice, the more senior the counsel the easier the applications will go through. Only if the action is contested will the courts conduct an investigation. Yet the lack of any reported case law on this

subject indicates that these instances are rare and that dissenting sharenolders have a difficult task ahead of them. Compare this procedure to the second way in which the courts may be utilized as exemplified by section 72 of the U. K. Act, an appeals section by which a dissenting shareholder may apply to court for judicial relief. There has been a substantial amount of case law under those sections, delineating the rights of shareholders in those jurisdictions. One should also note the complex technical procedure which is currently in use in Alberta as well as the general cost in acquiring court approval/which seem both of to denegrade from the objectives of simplicity and ease desired for corporate legislation.

Even if the court does review an application for a variation of rights, the criteria which binds them, i.e. alterations to articles must be 'bona fide for the benefit of the company as a whole', are uncertain and unlikely to provide a great deal of protection to shareholders. Undoubtedly,more effective use of the courts can be achieved in other ways.

The British Columbia recommendations in this area are based on the concepts of reporting and non-reporting companies. This is one of the few cases in the area under examination where the treatment varies for different types of companies. In Alberta, as in all other jurisdictions, private companies are not subject to any extra restrictions in this area. On the other hand, private companies are not subject to a great deal of scrutiny, and it is quite possible that abuse could be more prevalent in these types of companies. Although it is outside the scope of this paper to examine in depth the rationale behind the use of the reporting company concept, we noted earlier that the general rationale was a

'need to know' by the governing authorities over the actions of a reporting company, i.e., a company where there is no 'community of interest ' among the shareholders in the company.

Companies should be free to reorganize their share structures unfettered by any outside administrative controls of their power to do so. It is hoped that both the procedure for variation of rights outlined in this section and the protections to be proposed in the next section will supply the shareholder with adequate safeguards, so that the company cannot unfairly or prejudicially alter a shareholder's rights without allowing the shareholder some form of protection. With regards to public companies in Alberta, any regulation of corporate activities should probably be dealt with in securities legislation and not in corporate legislation. Private companies on the other hand, do not need any of this kind of 'supervisory' protection because the 'community of interest' exists in a private company. It is comprised of a small group of shareholders all of whom are in intimate contact one with the other and as such, should be fully aware of all rights and privileges attached to shares as well as the right of the majority to vary those shares if the proper procedure is followed.

Having rejected the use of the courts or an administrative tribunal as a positive step in the variation procedure, it now falls on us to decide in exactly which way the shareholders should be allowed to utilize the facilities of the courts.

The usual provision is in the form of a statutory appeal section which allows a certain percentage of shareholders to apply to the court within a certain time, asking the court to use its powers to either affirm or set aside the resolution, or as in the Federal Act, to value the rights

of the dissenting shareholder. It is recommended that this approach be adopted so as to allow any shareholder (not a minimum ten or fifteen percent of a class) of a class of shares whose rights are varied as per the broad Federal provisions in section 170 to apply to the court after notice has been given to the company within certain defined time limits. Exactly what rights the courts should have will be outlined in Part (3) of this section.

The last point to be examined in this section is the related question as to who should be allowed to propose alterations to the memorandum, which based on an earlier recommendation will now include the share rights. The current law limits this right to the directors only, but we noted that the Federal Act extended this right to include shareholders as well. The Dickerson Report argued that in their streamlined method of structuring a corporation, such a right corresponds to the right of a shareholder to propose an amendment to the bylaws of the company.

By extending this right to shareholders, it provides them with an additonal protection to their share rights. They are now able to take some kind of positive action to protect their share or class rights, rather than being forced to protect their rights by either garnering enough support to defeat a special resolution or by opting out of the company altogether. On the other hand, the right of proposing amendments to the memorandum has always been termed a matter of internal business to which the directors are most qualified to handle.

Obviously the determination to this question involves much more than the variation of rights issue, and in fact, in the Federal scheme,is one of the major components of the concept of fundamental change. If such a concept is

to be examined for a future Alberta act, this change would obviously be an important consideration. However, it is impossible to make a recommendation on such a major proposal within the narrow confines of the topic under discussion. However, the fact that such a reform does provide an extra right for shareholder protection will undoubtedly be one of the major considerations when this question is examined in depth.

3) Most Effective Means of Protection

We now come to the final consideration of this paper--that of attempting to derive proper protections for shareholders whose rights are being varied by the company. It is again important to note that any effective protection must not place undue restrictions on the company, either by the courts or by the shareholders exercising a veto power. Conversely, protection must be provided for the basic rights and remedies of shareholders, one of which is a protection of the rights that attach to shares which undoubtedly played a la role in influencing the investment in the first place. In this light, we come to evaluate the current protections available for shareholdrs.

The common law has attempted to provide some protection in the area of alteration to the articles. Not only do the directors of a company have imposed upon them certain common law duties when proposing alterations to the articles, but the majority shareholders as well are bound by the duty to act bona fide for the benefit of the company as a whole. However concise this duty may be stated, the courts have had a great deal of difficulty in formulating accurate and realistic tests for guidelines for implementing it. As the Dickerson Committee argued:[50]

> Judging from the reported cases, the present state of the common law is at best unsatisfactory, at worst downright unjust.

As we have seen, from our earlier discussion, in terms of protecting the rights of shareholders where alterations are proposed, including alterations to share and class rights, we cannot look to the common law for any significant amount of protection.

An earlier recommendation with regards to the wording to the actual variation of rights procedure has hopefully overcome another problem in this area caused by narrow and restrictive judicial decisions. We noted in section IV that an action under the statutory appeals sections such as section 72 of the U. K. Act, resulted in the courts distinguishing between a variation affecting 'rights' and a variation affecting 'enjoyment' of those rights. The effect of these decisions has been to provide protection only in circumstances where those rights are altered directly, while providing no protection for indirect alterations which from a business point of view have the same practical effect on the shareholder. It was therefore recommended that the broad provisions of the Federal Act be applied to abrogate those principles. By setting out in detail the exact situations where variation of share or class rights required a procedure to be invoked, both the company and the individual shareholder will know when rights are to be protected by using this procedure. The major advantage of these changes will be to give effect to the requirement that these rights need protection from a practical business point of view. An attempted variation of share rights, even though indirect, could have the effect of lowering the value of those shares in the market place If that alteration falls within the confines of the suggested provisions, the affected shareholder will have the protection

of the variation procedure at his disposal. As to the argument that this will in effect make the preference shareholders, as Pennington called them a second board of directors with a power of veto over the directors, it is submitted that a variation in any of the situations outlined in the Federal Act would be substantially important enough to the value of the shares to warrant the requirements of the procedure. Note also that no veto power is actually in question under the Federal Act because the courts have no authority to set aside or vary the resolution.

It is submitted that the actual variation procedure itself recommended in Part II of this section, will provide the basic framework of a protection for shareholder rights in the following ways:

(1) The entire procedure for a variation of share or class rights is contained in the substantive provisions of the Act, and not the articles.

(2) The nature of the procedure itself provides fundamental protection by way of the requirements for separate class voting and a special resolution.

(3) Every type of alteration which will require the variation procedure to be invoked is detailed in the procedure (as per section 170(1) of the Federal Act).

The above procedure will provide the basic protection for minority shareholders. However because it has been concluded that the other protections currently available in Alberta for shareholders are not wholly effective or desirable, it is submitted that a new approach must be adopted, one that is not restricted by the current law, and provides protection for the business rights of the minority

shareholder as well as protection of his legal rights, but yet is not so broad as to put restrictive clamps on the effective operation of the company. Such an approach, it is submitted, is found in the Federal Act concept of 'fundamental change'.

The concept of fundamental change refers to changes by the company to its articles of a fundamental nature by the majority shareholders. It is designed to establish new standards of fairness for minority shareholders, and to remove such alterations from the confines of the common law:[51]

> The law is ambiguous...the application of such a standard [i.e. the common law standards relating to alterations discussed in section IV] is very difficult. Judging from the reported cases, the present state of the common law is at best unsatisfactory, at worst downright unjust...

As a replacement for these common law standards, the Dickerson Committee recommended this major policy change:[52]

> Instead of relying on common law standards to restrict the conduct of majority shareholders who propose to make a fundamental change, the provisions in this part confer upon a shareholder who dissents from the fundamental change privilege of opting out of the company and demanding fair compensation for his shares...in short, if the majority seeks to change fundamentally the nature of the business in which the shareholder invested, and if the shareholder dissents from the change, he may demand that the corporation pay him the

as determined by an outside appraiser.

The effect of this change means that a minority dissenting shareholder has one major protection from the company--to opt out of the company with no prejudice to the monetary value of his shares. The minority shareholder is therefore no longer at the mercy of the majority shareholder who proposes alteration schemes such as those successfully carried out in the White and Greenhalgh cases. However, assuming that the variation procedure has been validly followed, the minority shareholder has no power at all to set aside the resolution, unless he can garner enough votes to block the special resolution or prove some sort of fraud on the minority. Otherwise it is a valid alteration. This will ensure that the company can carry on business unfettered from any potential veto threat by the minority shareholder.

A major change in this approach is this elimination to a large extent of the positive role of the courts in the variation procedure. In all other jurisdictions, the courts have been charged with the duty of balancing the rights of the majority and minority interests while attempting to maintain a policy of judicial non-interference. The Dickerson recommendations have removed this dilemma from the courts and their new responsibility is to ensure that a dissenting shareholder's rights are properly and fairly appraised.

This approach, at first glance, appears somewhat harsh with respect to the rights of the minority dissenting shareholder. However, their rights under a fundamental change are supplemented by their rights under the 'unfairly prejudicial or oppressive' relief sections. This section applies in the case where a minority shareholder feels his rights have been oppressed or prejudiced by the majority shareholder

or there has been a "visible departure from the standard of fair dealing and a violation of the condition of fair play on which every shareholder who entrusts his money to a company is entitled to reply."[53] In such a case, the Federal Act provides a very broad discretion for the courts to make any order it deems fit. Note that the Federal section has incorporated all the major recommendations of the Jenkins Committee Report so as to provide the widest possible protection. Thus a minority shareholder does have an avenue available to him to remain in the company as a shareholder if he has been aggrieved and falls under the protection provided in section 234.

As well, the minority shareholder does have the protection of the actual procedure which the company must follow. One should note the very broad provisions in the pro procedure which ensures that it be invoked in almost all cases where the voting shareholders attempt to vary the rights of the non-voting or preference shares. If the company does not follow the procedure, the alteration is invalid. As well, the company might be wary of making any such class alterations due to the cost it might incur in paying off dissenting minority shareholders.

Nevertheless, the protections available for minority shareholders must not hinder the effective operation of the company. Under this approach, the majority shareholders can, if they go through the proper formalities, effect almost any fundamental change with impunity. As Dickerson concluded:[54]

> The result is a resolution of the problem that protects minority shareholders from discrimination and at the same time preserves flexibility within the enterprise, permitting it to adapt to changing business conditions.

The Federal approach has much to recommend it, although to make it effective would require the adoption of both the variation procedure suggested above and some kind of oppressive and unfairly prejudicial remedy relief section. The adoption of such a relief section encompasses many more considerations than have been mentioned in this paper and it is outside the scope of this paper to examine in detail the arguments for and against such a section. However such a section does appear to complement the notion of fundamental change, and indeed, with regards to variation of share or class rights, adds a great deal of protection to the rights of the minority shareholder.

We have noted that the concept of appraisal rights is a new one in Canada and there will undoubtedly be problems in deriving a procedure for the valuation of shares. The remedy has been widely used in American jurisdictions and numerous problems have developed. The American statutes generally establish strict requirements for its use, such as requiring a negative vote on the proposal to which the shareholder objects and notice to the corporation within a stipulated time; as a result many holders lose their appraisal remedy by failure to learn of it in time or failure in following the statutory procedure (note that these two requirements are part of the Federal procedure). Also, much controversy has arisen over the proper method of valuation of the dissenters' shares. The task can be very difficult especially where the corporation involved is a closely held one whose shares have no recognized market value. Moreover, the existence of a right of appraisal may limit the equitable remedies that would otherwise be available. Furthermore, the probability that the minority shareholder will be remitted to his appraisal remedy adds temptation to the majority to attempt a freeze-out, since buying out the minoritys' shares

may be precisely the majority's objective. As well, one should expect technical and procedural problems by corporations in adjusting to a new system.

One further point remains to be examined: In the light of the above recommendations, should any protection be allowed for non-voting shares when the voting shareholders alter their own rights or rights to another class of shares and those alterations have an effect on other non-voting shares?

As noted earier, the common law does not indicate much willingness to extend this kind of protection to the non-voting shareholders. Only the Ontario and Federal Acts in Canada have altered this common law position by providing protection where the class of shares altered are shares having rights and privileges equal or superior to the shares of the affected class. These protections are justifiable on the basis that alterations of this type are in the nature of alterations which have a very real effect on the business value of the non-voting shares because their rights are being watered down or leap-frogged over. When the alterations to the voting shares do not affect rights in this way, no protection is provided.

There is a further right extended by the Federal Act to all shareholders, including non-voting shareholders, whose rights are affected by a variation to voting or another class of non-voting shares. This is the right to dissent if the shareholder is entitled to vote pursuant to section 170 (1)(a) or 170(1)(d). It is recommended that this same right be applied in similar circumstances to shareholders in Alberta. However, classes of shares whose rights are in no way affected by the proposed alteration should not be placed in a preferred position by having the right to opt out of the company at any time.

We also examined a right given to any shareholder by both the Ghana Act and the Federal Act (section 204(3)) to a separate class vote when the company proposes to voluntarily wind up. This effect of this right is that one class of shares can effectively veto a proposal to wind up the company, even if that share normally would not carry a vote, or whether the desire to wind up was a bona fide business decision made in the best interests of the company. This kind of right seems to fly in the face of the desire to allow companies to make corporate decisions with the greatest possible flexibility. If, by proposing a winding up, a shareholder of a particular class can show that the voting shareholders are perpretating some kind of fraud on the minority or are oppressing or prejudicing their rights, the non-voting shareholders can apply to the court to have the resolution set aside if there is a section similar to section 234 of the Federal Act. In all other circumstances, there is no reason to attach this unwarranted right to the non-voting shares.

With regards to the situation now under discussion, we should note section 47(7) of the Ghana Code:

(7) An application to the Court under subsection (6) of this section shall be made within 60 days of the date on which the variation was effected and may be made on behalf of the shareholders entitled to make the application by such one or more of their number as they may appoint in writing. If such an application is made the company shall forthwith deliver to the Registrar for registration notice in the prescribed form of that fact. The Court after hearing the applicant and any other persons who apply to the Court to be heard and appear to the Court to be interested in the application shall if it is satisfied that the variation would unfairly prejudice the shareholders of any class, cancel the variation and shall, if not so satisfied, confirm the variation.

Under this section, the court has power to cancel a variation which would unfairly prejudice the shareholders of 'any' class. The crux of the matter will be interpretation of 'unfairly prejudicial'. If this term is to be given a broad interpretation, it is possible that a court could set aside a variation resolution in many more situations than is contemplated by the Federal or Ontario Acts. However the Ghana approach has basically the same effect as sections similar to section 234 of the Federal Act, except that it is specifically designed to deal with the variation of rights problem. If we are to assume that section 234 of the Federal Act covers this situation as well, then the provision in the Ghana Act appears redundant. However, if a section similar to section 234 is rejected for inclusion in a corporate act, as it was in Ontario, then this kind of provision, i.e., one dealing only with the variation of rights issue, becomes necessary and important to complement the rights given to the dissenting shareholders to opt out of the company. Without this kind of right, the minority shareholder is restricted to one remedy if the company proposes to vary his share rights--to opt out of the company. This would be the case even if the alteration unfairly prejudices or is oppressive to the minority share rights. Thus, if a general oppression remedy is rejected in Alberta, it is recommended that a section similar to section 47(7) of the Ghana Code be included in the variation of rights procedure.

VII. CONCLUSION

A concluding remark is in order at this point. This paper has attempted to examine the various aspects involved in the variation of shareholder and class rights and to make recommendations as to how the problems in this area should be dealt with in corporate legislation. Many of the recommendations made in this paper have been largely based on the Dickerson Committee recommendations. These recommendations were not easily reached however and not without a thorough examination of all the approaches currently in use as well as proposed changes in other jurisdictions. The philosophy of the Dickerson recommendations seem well suited to the problem at hand. They attempt to abrogate several common law principles which have not been effective in providing the necessary balance between the interests of the company in the name of the majority shareholders on the one hand, and the rights of the minority shareholders on the other. The Federal approach provides the necessary flexibility required in this situation. The majority will have an unfettered power to restructure share capital and alter share rights. A dissenting shareholder has no rights to challenge the validity of a valid alteration, but can opt out of the company and receive fair compensation for his shares. However, any shareholder can apply to court for a judicial remedy if a variation unfairly prejudices or oppresses his share rights. It is hoped that this examination on the variation of share rights and the recommendations made will aid in developing some worthwhile guidelines for the law in this area.

VIII. FOOTNOTES

1. [1901] 1 Ch. 279.

2. See Gower, The Principles of Modern Company Law (3d. ed.), p. 367 for his 'Canons of Construction' as to the interpretation of preferential rights when a company has more than one class of shares.

3. One of the 'rights' which some acts allow is the non-voting common share. Although it is outside the scope of this paper to examine that complex question, it is to be noted that the Ontario Act in section 112(2) outlaws non-voting common shares, while the new Federal Act provides for them. The Alberta Act presently allows non-voting common shares.

4. [1892] 2 Q.B. 573 at p. 583.

5. Selected Topics in Canadian Company Law Reform (Iacobucci Report) July 1975, p. 3.

6. D.G.R. Rice, Problems on the Variation of Shareholders Class Rights, 22 Conveyancer 126.

7. It should be noted that even where there is only one class of shares, some acts allow a minority shareholder to apply to court to set aside a resolution if it is 'unfairly prejudicial' or 'oppressive' to the rights of the minority shareholder. See section 234 of the Federal Act.

8. The Alberta Corporations Manual, (Deboo) p. 3512.

9. See Part V, sections C and D.

10. The Interim Report of the Select Committee on Company Law (1967) Ontario.

11. Section 210 of the U. K. Companies Act (1948) allows an action to be brought to the courts by a minority shareholder on the basis that the company is conducting its affairs in a manner oppressive or would unfairly prejudice a member's rights. The Lawrence Committee rejected the use of such a provision in the Ontario Act on the grounds that section 210 was "objectionable on the ground that it is a complete dereliction of the established principle of judicial non-interference in the management of companies." (Para. 7.3.12.)

12. Stanley M. Beck Canadian Corporation Law Vol. 1 (Ziegel, ed.) p. 597.

13. This concept will be dealt with in detail in Part V.

14. Note this quotation from the Dickerson Report which gives us an indication of how they viewed the role of the courts in their Draft Act:

> We think that the best means of enforcing a corporation law is to confer reasonable powers upon the alleged aggrieved party to initiate legislation to resolve his problem, making the Draft Act largely selfenforcing, ...we have established only very broad quality standards of conduct, permitting the courts to determine whether there has been failure to comply with those standards. (Para. 476.)

15. See Ashbury v. Watson (1885) 30 Ch. 376.

16. See Re Welsbach Incandescent Gas Light [1904] 1 Ch. 87 C. 8. The court held that if the articles contain a power of variation and the articles are filed contemporaneously with the memorandum, alterations may take place.

17. Final Report of the Commission of Enquiry into the Working and Administration of the Present Company Law of Ghana--para. 8 section 218 p. 161.

18. Deleted.

19. Deleted.

20. Fisher v. Easthaven Limited [1964] N.S.W. p. 261 per Else-Mitchell J. at p.

21. Crumpton v. Morinne Hall Property Limited [1965] 82 W.N. (N.S.W.) per Jacob J. at p.

22. Supra n. 20 at p.

23. See Gower, p. 509.

24. See Trebilcock, The Effect of Alterations to Articles of Association (1967), 31 Conveyancer (M.S.) 95; Baxt, The Variation of Class Rights (1968), 41 A.C.J. 490.

25. Delete.

26. Supra n. 23 at p. 464.

27. Campbell v. Rofe (1932) 48 C.L.R. 258 at p. 264.

28. Report of the Company Law Committee (1973) Cmnd. 1749 para. 198.

29. Proposals for a New Business Corporations Law for Canada, (Dickerson Report) Vol. 1 para. 353 and para. 195, Vol. 2 section 1402(1).

30. Fogler v. Norcan (1964) 47 W.W.R. 257 (Alberta C.A.) per Porter J. A.

31. Supra n. 23 at p. 570.

32. (1966) 4 Alta. Law Review p. 395.

33. British American Nickel Corporation v. O'Brien [1927] A.C. 369 at p. 378.

34. Allen v. Gold Reefs of West Africa [1900] 1 Ch. 656 (C.A.) at p. 671.

35. [1951] Ch. 286 C.A. at p. 291.

36. H. Ballantine and G. Sterling, California Corporations Law section 294 (4h. ed. 1962).

37. In Re MacKenzie and Company Limited [1916] Ch. 450 at p. 450. Note this quote from the case of Greenhalgh v. Ardene Cinemas Limited [1946] 1 All E. R. 512 at p. 517:

> "The effect of this resolution is, of course, to alter the position of the 1941 2s. shareholders. Instead of Greenhalgh finding himself in a position of control, he finds himself in a position where the control has gone, and to that extent the rights of the 1941 2s. shareholders are affected as a matter of business. As a matter of law, I am quite unable to hold that, as a result of the transaction, the rights are varied; they remain what they always were..."

39. White v. Bristol Aeroplane Company Limited [1953] Ch. 65 at p. 73.

40. Ibid. at p. 74.

41. Ibid. at p. 80.

42. In Re John Smith's Tadcaster Brewery Company Limited [1953] Ch. 308 at p. 316.

43. Ibid. at p. 316.

44. Pennington, Company Law, (1973) at p. 198.

45. Hodge v. James Howell and Company (December 12th, 1958) C.L.R. at p. 446.

** 46. Report of the Committee on Company Law Amendment, Cmd. 6659 (1945) (The Cohen Report).

47. Supra n. 10 at para. 7.3.12.

48. Supra n. 23 at p. 513.

49. Supra n. 5 at p. 179.

50. Supra n. 29 at para. 346.

51.

52. Ibid. at para. 347.

53. Supra n. 56.

54. Supra n. 29 at para. 347.

**45a. Corporate Freezeouts and the Protection of Minority Shareholders in Alberta Companies (1966) 3 Alta. L. R. 395.

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22. Special One Day Programs - Ontario B.C.A. 1970. Conducted by LSUC.

23. Symposium - The Proposed Michigan B.C.A. (1972) 18 Wayne L.R. 912.

24. Trebelcock, The Effect of Alterations to Articles of Association (1967) 31 Conv. (N.S.) 95.

APPENDIX A

The following are some of the principles on which courts have acted when required to approve a vote:

1. The Court must be satisfied that the statutory procedure has been followed. Where a member's property is being taken from him, for example under a take-over in terms of section 138, the court must be satisfied that the act has been strictly complied with.[30] Once the majority have discharged this onus, however, it has been held that the dissentient is faced "with the very difficult task of discharging an onus which is undoubtedly a heavy one—of showing that he, being the only man in the regiment out of step, is the only man whose views ought to prevail."[31]
2. It must be clear that an intelligent and honest man would vote for it[32] and sensible business men would approve.[33]
3. The court must examine the scheme and see if it is fair and reasonable.[34]
4. The court must scrupulously regard the rights of minority shareholders.[35] Thus, in *Re Provincial Apartments Ltd.*,[36] the court refused to sanction a scheme depriving preference shareholders of certain rights, holding that it would not allow the common shareholders to "feast on the rights" of the preference shareholders.
5. The shareholders must have been given accurate and adequate information so as to arrive at an informed decision,[37] and the

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28 Amalgamation and compromise schemes (*ante*, n. 20) alteration of class rights, enlargement of objects and reduction of capital, require this sanction. In section 138 take-over schemes, the court can intervene.

29 (1964), 47 W.W.R. 257 (Alta. C.A.). Reversed on further appeal, but on other grounds. Reported *sub. nom.*, *Norcan* v. *Gridoil*, 49 W.W.R. 321.

29a *Id.* at 263.

30 In *Re Brazilian Traction Light, etc., Co. Ltd.*, [1947] O.R. 791; *Fogler* v. *Norcan Oils, ibid*; *In Re Alabama, New Orleans, Texas and Pacific Ry.*, (1891] 1 Ch. 213 (C.A.); *Re Dairy Corporation of Canada Ltd.*, (1934] O.R. 436; *Rathie* v. *Montreal Trust Co.*, [1953] 2 S.C.R. 304.

31 Per Vaisey, J. in *Re Sussex Brick Co. Ltd.*, [1960] 1 All E.R. 772 (Ch.). He also says that the scheme must be unfair to "the meanest intelligence." This is cold comfort for a minority.

32 In *Re Brazilian Traction*, etc., *ante*, n. 30.

33 *Re Western Canada Flour Mills*, [1945] 1 D.L.R. 589 (Ont. H.C.); *Re National Grocers Ltd.*, [1938] O.R. 123.

34 *Re Langleys Ltd.*, [1938] O.R. 123; *Re Dorman Long & Co. Ltd.*, [1934] Ch. 635.

35 Re *Langleys Ltd.*, *ante*, n. 34). *Re National Grocers Ltd.*, *ante*, n. 33.

36 [1936] 3 W.W.R. 327 (Sask. K.B.).

37 *Fogler* v. *Norcan Oils*, *ante*, n. 29; *Rathie* v. *Montreal Trust Co.*, *ante*, n. 31; *In re St. Lawrence Corporation & Mayr*, [1948] 2 D.L.R. 107 (Que. S.C.); but see *In re Evertite Locknuts*, [1945] Ch. 220, where inadequate information was considered insufficient to persuade the court to intervene on behalf of the minority in a section 138 type of scheme.

directors must honestly put forward to the best of their skill and ability a fair picture of the company's position.[38]

6. At the same time the court will be guided by the majority decision, an approach which effectively casts an onus on the minority to show why the scheme should not be approved, rather than on the majority to justify it. This attitude is exemplifeid by observations of the following type: the court will pay the greatest attention to what business people who are concerned with the transaction decide;[39] what is fair from a business standpoint can generally best be judged by the opinion of businessmen rather than judges;[40] shareholders acting honestly are better judges of the advantage to the company than the courts;[41] the court must be guided by the voice of reasonable businessmen who understand the nature of business,[42] and, where a very large majority desire a certain procedure the court should give effect to it.[43] This reluctance to interfere is perhaps an abdication of the duty specifically imposed on the courts by the legislature. By relying on the majority decision the freezeout protection envisaged is nullified. As will be illustrated by the rule in *Foss* v. *Harbottle*,[44] the courts are reluctant to sit in judgment on the decisions of shareholders; but here they have been specifically charged so to do. There is no mystique in the management of companies that is beyond the understanding of the courts. It displays an unjustified modesty to suggest that shareholders, by the mere act of acquiring a share, are in a better position to decide on the efficacy of a scheme than a judge. If one takes account of the realities of a corporate decision, it will often be revealed as a mere rubber-stamping of a decision placed before a meeting rather than the considered and informed opinion of businessmen-shareholders.[44a]

7. The courts have considered the situation where a member may hold shares in more than one class. He may vote to surrender privileges in one class because he will get a greater benefit as a member of another class. Such a shareholder will not be considered as truly disinterested, and the courts will take this into account in deciding whether to give their approval. In deciding whether the necessary 90% acceptance of an offer has been obtained in section 138 procedures, the courts have taken into account analogous conflicts of interest. In the *Esso case*,[45] Esso Petroleum had made an offer to purchase all the shares in International Petroleum Co. Ltd. A 90% acceptance was obtained, but a substantial part of this 90% consisted of shares owned by a subsidiary of the offeror Esso, which would obviously be in favour of the scheme. The Supreme Court of Canada held that there had not been a disinterested 90% and agreed that the minority could not be compelled to accept the offer.

[38] *Re Dorman Long & Co. Ltd.*, *ante*, n. 34.
[41] *Carruth* v. *Imperial Chemical Industries*, [1937] A.C. 707 (H.L.).
[42] *Sidebottom* v. *Kershaw, Lesse & Co.*, *ante*, n. 18.
[43] *Re Bailey Cobalt Mines Ltd.* (1920) 47 O.L.R. 13.
[44] (1843), 2 Hare 461, 67 E.R. 189. See *post*.
[44a] Porter, The Vertical Mosaic 49 *et. seq.* (University of Toronto Press 1966) gives an interesting account of the timidity of shareholders.
[45] *Ante*, n. 22, and see also *Re Canadian Breweries Ltd.*, [1964] C.S. 600 (Que.), which indicates that the 90% cannot be obtained piecemeal over a period but must result from a single offer.