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The Shifting Balance of Power between Shareholders and the Board: News Corp's Exodus to Delaware and Other Antipodean Tales

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Abstract

NOTE: The research in this Working Paper was subsequently published in the form of the following articles: (i) Jennifer G. Hill, "Subverting Shareholder Rights: Lessons from News Corp's Migration to Delaware", 63 Vand. L. Rev. 1-51 (2010) (available at http://papers.ssrn.com/abstract=1541644) (examining News Corp's shift in domicile from Australia to the United States as a case study, or natural experiment, to assess fundamental differences in traditional shareholder rights in the US, compared to other common law jurisdictions, such as the United Kingdom and Australia. The article also explores the lessons of News Corp's reincorporation for current US reforms increasing shareholder rights, and for the anti-reform claim that if shareholder empowerment were efficient, it would already have existed in the marketplace). (ii) Jennifer G. Hill, "The Rising Tension Between Shareholder and Director Power in the Common Law World", 2010, 18 Corporate Governance: An International Review, pp. 344-359 (2010) special issue on Shareholder Activism (available at http://papers.ssrn.com/abstract=1582258) (examining key arguments in the US shareholder empowerment debate, and the increasing tension between shareholder and director power in common law jurisdications). The balance of power between shareholders and the board of directors is a contentious issue in current corporate law debate. It also lay at the heart of a controversy concerning the re-incorporation of News Corporation (News Corp) in Delaware. News Corp has recently been the subject of intense media attention due its successful bid to acquire Dow Jones & Company. Nonetheless, News Corp's move to the US, which paved the way for this victory, was neither smooth nor a fait accompli. Rather, the original 2004 re-incorporation proposal prompted a revolt by a number of institutional investors, on the basis that a move to Delaware would strengthen managerial power vis-a-vis shareholder power. The institutional investors were particularly concerned about the effect of the re-incorporation on shareholder participatory rights, and the ability of the board of directors to adopt anti-takeover mechanisms, such as poison pills, which are not permissible under Australian law. It was this latter concern, which ultimately led a group of institutional investors to commence legal proceedings in the Delaware Chancery Court in UniSuper Ltd v News Corporation (2005 WL 3529317 (Del Ch)). The News Corp re-incorporation saga highlights a number of important differences between US and Australian corporate law rules relating to shareholder rights, and provides a valuable comparative law counterpoint to the recent US shareholder empowerment debate. Other recent Australian commercial developments discussed in the article show a tension between legal rules designed to enhance shareholder power, and commercial practices designed to readjust power in favor of the board of directors. These developments are interesting because they demonstrate how some Australian companies have tried to create a de facto corporate governance regime, which mimics certain aspects of Delaware law.

Keywords: corporate governance, comparative corporate governance, News Corporation, Liberty Media, Rupert Murdoch, John Malone, institutional investors, shareholders, shareholder empowerment, managers, directors, boards, stakeholders, corporate charters, charter amendments, shareholder meetings, mergers

JEL Classifications: D70, G30, G32, G34, G38, K22, K33, K40, K42, M14

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Introduction

> "[I]f there are sufficient basic similarities to make a comparison possible, there are, equally, sufficient differences to make it fruitful."
>
> L.C.B. Gower[1]

The dominant issue in comparative corporate governance debate at the turn of the decade was whether international corporate laws would converge,[2] or whether differences between common law and civil law jurisdictions would persist.[3] An embedded assumption on both sides of this debate was that there exists a unified and stable Anglo-American model of corporate governance representing the common law side of this divide.[4] This article discusses some developments and events which

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* Professor of Corporate Law, Sydney Law School; Visiting Professor, Vanderbilt University Law School. I am grateful to Sandy Easterbrook and Megan McIntyre for providing me with access to a number of important background documents in relation to the discussion in Parts 3 and 4 of the article. Thanks also to John Armour, Emma Armson, Andrew Black, Bill Carney, Deborah DeMott, David Friedlander and Ron Masulis for helpful comments and references. Finally, particular thanks go to Alice Grey and Michael Rawling, as well as to Alexander Giudice and Fady Aoun, for excellent research assistance in connection with various aspects of this article. All errors are my own. Funding for this research was provided by the University of Sydney and the Australian Research Council.

1 L.C.B. Gower, "Some Contrasts Between British and American Corporation Law" (1956) 69 *Harv L Rev* 1369, 1370.

2 For example, at this time, Professors Hansmann and Kraakman famously stated "[t]he triumph of the shareholder-oriented model of the corporation over its principal competitors is now assured…" Henry Hansmann and Reinier Kraakman, "The End of History for Corporate Law" (2001) 89 *Geo LJ* 439, 468.

3 A voluminous literature on the "convergence-divergence" debate emerged at the turn of the last decade. For a recent synthesis of the issues in that debate, see Jeffrey Gordon and Mark Roe (eds), *Convergence and Persistence in Corporate Governance* (2004).

4 See, for example, Gordon and Roe (eds), *ibid*, which poses the question "Is the Anglo-American model of shareholder capitalism destined to become standard or will sharp differences persist?"

challenge this assumption of a cohesive common law governance model in relation to the balance of power between shareholders and the board of directors/management.

One such event was the 2004 decision by News Corporation ("News Corp") to move from Australia to Delaware. News Corp has recently been the subject of intense media attention, as a result of its successful bid to acquire Dow Jones & Company, publisher of the Wall Street Journal, and bring it under the aegis of News Corp's $70 billion global media empire.[5] Nonetheless, News Corp's migration to the US from Australia, which paved the way for this recent victory, was neither smooth nor a fait accompli. Rather, the original re-incorporation proposal in 2004 prompted a revolt by a number of institutional investors, on the basis of corporate governance concerns.

The 2004 News Corp re-incorporation saga highlights some crucial differences in the balance of power between shareholders and management under current Australian and US corporate law regimes. This article discusses the News Corp re-incorporation controversy against the backdrop of two other developments, which also reveal corporate governance fissures within the common law world. First, international corporate collapses, epitomized by Enron, prompted a wave of reforms in common law jurisdictions, such as the US, UK, Canada and Australia.[6] While these reforms tackled similar corporate governance concerns, they demonstrated interesting differences in relation to shareholder participatory rights and interests.[7] Secondly, corporate theory concerning the role of the shareholder is back on the agenda in US

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5 The success of the bid seemed assured after News Corp finally secured support from the majority of the Bancroft family, which had controlled Dow Jones & Company since 1902 and held 64% of its voting shares. See generally "Mogul's Dream: Murdoch Wins His Bid for Dow Jones – News Corp.'s Success Follows Delicate Dance Between Suitor, Target", *The Wall Street Journal*, 1 August 2007, A1; Richard Perez-Pena and Andrew Ross Sorkin, "Dow Jones Deal Gives Murdoch a Coveted Prize", *The New York Times*, 1 August 2007, 1. Formal approval for the acquisition was given on 13 December 2007, when 60.2% of Dow Jones shareholders voted in favor of the deal. See Joshua Chaffin, "Dow Jones Now With Murdoch", *Financial Times*, 14 December 2007, 21; Richard Perez-Pena, "News Corp. Completes Takeover of Dow Jones", *The New York Times*, 14 December 2007, 4.

6 See generally, Jennifer G. Hill, "Regulatory Responses to Global Corporate Scandals" (2005) 23 *Wisconsin Int'l LJ* 367.

7 *Id*, 392.

corporate law. The shareholder empowerment debate[8] and the Interim Report of the Committee on Capital Markets Regulation (the "Paulson Committee Report")[9] raise shareholder participation rights as a significant issue for corporate law reform. These developments suggest that US law relating to the balance of power between shareholders and management may itself be fluid and evolving at this time.

Much recent regulatory debate has focused on the effect of legal rules. Yet, commercial norms and practices may be equally, or more, important.[10] The article concludes by discussing a tension, which has recently emerged in Australia, between legal rules designed to enhance shareholder participation in corporate governance, and commercial attempts to curb such involvement and shift power away from shareholders towards management. These commercial developments are interesting because they demonstrate how some Australian companies have tried to create a de facto corporate governance regime, which mimics certain aspects of Delaware law. These developments show that commercial practices may in some instances effectively subvert legal rules and generate their own convergence pressures.

1. Evolving Visions of the Shareholder in Corporate Law

> "[I]t is the courts that are relegating shareholders to the questionable role of bystanders".
>
> Richard M. Buxbaum[11]

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8 The debate is played out in a 2006 and 2007 Special Issue of the *Harvard Law Review* and *Virginia Law Review* respectively.

9 The Paulson Committee recommended strengthening of shareholder rights in a number of areas. See Committee on Capital Markets Regulation, *Interim Report of the Committee on Capital Markets Regulation* (30 November 2006, revised version released 5 December 2006), xiii; 5. For progress on the Committee's recommendations, see Hal S. Scott, "What is the United States Doing About the Competitiveness of its Capital Markets" (2007) 22(9) *Journal of International Law and Regulation* 487, 480-490.

10 See generally Melvin A. Eisenberg, "Corporate Law and Social Norms" (1999) 99 *Colum L Rev* 1253.

11 Richard M. Buxbaum, "The Internal Division of Powers in Corporate Governance" (1985) 73 *Cal L Rev* 1671, 1683.

> "[I]f the principal economic function of the corporate form [is] to amass the funds of investors, *qua* investors, we should not anticipate their demanding or wanting a direct role in the management of the company".
>
> Henry G. Manne[12]

The controversy concerning News Corp's 2004 re-incorporation in Delaware centered on the issue of shareholder rights in contemporary corporate governance. Institutional investors claimed that the shift from Australia to Delaware would seriously affect the role and rights of shareholders.

A range of different visions of the relationship between shareholders and the corporation can be discerned across time and jurisdictions in corporate theory. These images lie on two distinct axes – first, the appropriate level of shareholder participation in corporate governance and secondly, the status of shareholder interests. Within this schema, the shareholder is variously presented as an owner/principal; beneficiary under a trust; bystander; participant in a political entity; investor; gatekeeper; or managerial partner.[13]

The level of shareholders' participatory rights, and the status of their interests, varies considerably across this spectrum of possible images. Under the classic nexus of contracts theory of the corporation, for example, the shareholder is viewed as an investor with restricted participatory rights, but preeminent interests.[14] Collectivist theories, such as team production theory, go one step further, by challenging not only

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12 Henry G. Manne, "Our Two Corporation Systems: Law and Economics" (1967) 53 *Va L Rev* 259, 261.

13 For a detailed analysis of these images underlying corporate law doctrine, see Jennifer G. Hill, "Visions and Revisions of the Shareholder" (2000) 48 *Am J Comp L* 39, 42*ff*.

14 See, for example, Jonathan R. Macey, "An Economic Analysis of the Various Rationales for Making Shareholders the Exclusive Beneficiaries of Corporate Fiduciary Duties" (1991) 21 *Stetson L Rev* 23. See generally William W. Bratton, "The 'Nexus of Contracts' Corporation: A Critical Appraisal" (1989) 74 *Cornell L Rev* 407, 427*ff*; David Millon, "Theories of the Corporation" [1990] *Duke LJ* 201, 229-231.

strong participatory rights for shareholders, but also any assumed primacy of their interests over the interests of other corporate constituencies.[15]

The image of shareholders has been reevaluated in recent times, following the international corporate scandals and demise of the dotcom boom. Ambivalence emerged concerning the role of shareholders in these events. On one interpretation, gatekeepers, such as auditors and boards of directors, bore most responsibility for the scandals,[16] with shareholders seen as innocent bystanders or victims. On another interpretation, however, shareholders were far from blameless. The latter interpretation has focused on the perceived short-term interests of many shareholders,[17] particularly investors such as hedge funds,[18] viewing them not as victims, but as potential threats to the corporate enterprise.[19] There is also increasing

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15 Margaret M. Blair and Lynn A. Stout, "A Team Production Theory of Corporate Law" (1999) 85 *Va L Rev* 247.

16 See, for example, John C. Coffee, "Understanding Enron: 'It's about the Gatekeepers, Stupid'" (2002) 57 *Bus Law* 1403; John C. Coffee, "What Caused Enron? A Capsule Social and Economic History of the 1990s" (2004) 89 *Cornell L Rev* 269; Jeffrey N. Gordon, "What Enron Means for the Management and Control of the Modern Business Corporation: Some Initial Reflections" (2002) 69 *U Chi L Rev* 1233.

17 See, for example, Roberta S. Karmel, "Should a Duty to the Corporation be Imposed on Institutional Shareholders?" (2004) 60 *Bus Law* 1, 4-9 (arguing that institutional investors must take a share of the blame for defective financial analysis and aggressive pursuit of a shareholder primacy norm, which encouraged earnings manipulation and excessive executive pay); Vice Chancellor Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harvard L Rev* 1759, 1764, 1772-1773 (suggesting, from the perspective of the corporate law traditionalist, that quarter-to-quarter earnings of mutual and pension funds helped to fuel the pre-Enron environment, and noting the failure of institutional investors to detect the "obvious rot" at firms like Enron (at 1766)). See also William W. Bratton, "Enron and the Dark Side of Shareholder Value" (2002) 76 *Tulane L Rev* 1275, 1284 (condemning the short-termism associated with a commercial norm of shareholder value maximization); Antoine Rebérioux, "Shareholder Primacy and Managerial Accountability", *Comparative Research in Law and Political Economy Working Paper No. 1/2007* (January 2007, available at http://ssrn.com/abstract=961290), 2-3, 18-24 (suggesting that a shareholder primacy norm, rather than gatekeeper failure, was the main driving force in the corporate scandals); Patrick Bolton, José A. Scheinkman and Wei Xiong, "Executive Compensation and Short-Termist Behavior in Speculative Markets" (2006) 73 *Review of Economic Studies* 577 (positing a reinterpretation of compensation practices in a bubble market).

18 See Iman Anabtawi, "Some Skepticism About Increasing Shareholder Power" (2006) 53 *UCLA L Rev* 561, 582-584. There is also, however, ambivalence concerning the role of hedge funds in corporate governance. See, for example, Geert T.M.J. Raaijmakers and Rene H. Maatman, "Hedge Funds in Company Law: Virus or Vaccine?" [2006] *Ondernemingsrecht* 256 (available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=931884).

19 See generally Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harv L Rev* 1759, 1764.

concern about the phenomenon of "empty voting", involving a disjunction between voting rights and economic interests in the company.[20] Ambivalence about the role of the shareholder is reflected in a shift in much contemporary corporate law scholarship from traditional discourse about protection *of* investors, to discourse about protection of the corporation *from* investors.[21]

The international corporate scandals, epitomized by Enron, elicited a range of regulatory responses from common law jurisdictions, including the US, UK, Canada and Australia.[22] Although these reforms tackled similar problems of corporate legitimacy, they varied in terms of focus and structure.[23] The reforms also had a distinctly local flavor, often tracking the contours of national issues and political pressures.[24] While similar motivations underpinned the various reforms, their long-term effects are unlikely to coincide, due to inevitable differences in compliance and

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20 See Henry T.C. Hu and Bernard S. Black, "The New Vote Buying: Empty Voting and Hidden (Morphable) Ownership" (2006) 79 *S Cal L Rev* 811; Marcel Kahan and Edward B. Rock, "Hedge Funds in Corporate Governance and Corporate Control", *U of Penn. Inst for Law & Econ Research Paper No. 06-16; NYU Law and Economics Research Paper No. 06-37* (July 2006, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=919881).

21 Professor Robert Clark, Opening Comments, Sixth Annual Law and Business Conference, *Corporate Separateness*, Vanderbilt University, 31 March 2006. For reflections of this trend, see, for example, Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733 and Iman Anabtawi, "Some Skepticism About Increasing Shareholder Power" (2006) 53 *UCLA L Rev* 561 (discussing the dangers of shareholder opportunism and self-interest); Margaret M. Blair, "The Neglected Benefits of the Corporate Form: Entity Status and the Separation of Asset Ownership from Control" in Anna Grandori (ed), *Corporate Governance and Firm Organization: Microfoundations and Structural Forms* (2004), 45 (discussing the need for mechanisms to lock in capital and prevent asset stripping by investors); Henry Hansmann, Reinier Kraakman and Richard Squire, "Law and the Rise of the Firm" (2006) 119 *Harv L Rev* 1333 (discussing the role of "entity shielding" as the flip side of limited liability).

22 See generally, Jennifer G. Hill, "Regulatory Responses to Global Corporate Scandals" (2005) 23 *Wisconsin Int'l LJ* 367.

23 See Jennifer G. Hill, "Evolving 'Rules of the Game' in Corporate Governance Reform" in Justin O'Brien (ed), *Private Equity, Corporate Governance and the Dynamics of Capital Market Regulation* (2007), 29.

24 See Larry Ribstein, "Market vs. Regulatory Responses to Corporate Fraud: A Critique of the *Sarbanes-Oxley Act* of 2002" (2002) 28 *J Corp L* 1; Jennifer G. Hill, "Regulatory Responses to Global Corporate Scandals" (2005) 23 *Wisconsin Int'l LJ* 367; Eilis Ferran, "Company Law Reform in the UK: A Progress Report", *ECGI Working Paper No. 27/2005* (March 2005, available at http://ssrn.com/abstract=644203), 25.

enforcement.[25] Also, regulatory stringency can itself engender push-back from the business community. The Paulson Committee Report, which stresses the need to protect shareholders from excessive regulation, is an example of this kind of commercial backlash.[26]

Shareholder protection was a common goal in the various post-scandal reforms in common law jurisdictions. Nonetheless, the reforms differ in the way in which they seek to achieve this end, with an interesting dichotomy emerging between strengthening of shareholder participatory rights versus protection of shareholder interests.

Strengthening shareholder participatory rights was an explicit theme in the post-scandal reforms of both Australia and the UK, suggesting that legislators viewed increased shareholder power as a valuable check on abuse of managerial power and a potential antidote to future corporate collapses.[27] It appears to be a premise of these reforms that shareholders were victims of the corporate scandals, rather than complicit in creating the conditions that produced them. In Australia, the Explanatory Memorandum to the *CLERP 9 Act* 2004[28] contains numerous references to the desirability of improving shareholder participation,[29] increasing shareholder

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25 See, for example, Donald C. Langevoort, "The Social Construction of Sarbanes-Oxley", (2007) 105 *Mich L Rev* 1817, arguing that a gap exists between motivations and long-term effects, which depend on compliance and enforcement decisions, in relation to the *Sarbanes-Oxley Act* 2002.

26 *Interim Report of the Committee on Capital Markets Regulation* (30 November 2006, revised version released 5 December 2006), *id*, xi. For a summary of the Committee's recommendations, see Hal S. Scott, "What is the United States Doing About the Competitiveness of its Capital Markets" (2007) 22(9) *Journal of International Law and Regulation* 487.

27 *Cf* Lynn A. Stout, "The Mythical Benefits of Shareholder Control" (2007) 93 *Va L Rev* 789, 808, asserting that "[l]ack of shareholder power did not contribute to Enron's fall".

28 *Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Act* 2004 (Cth). The *CLERP 9 Act*, Australia's main legislative response to the international corporate scandals, was passed on 25 June 2004. The majority of the Act's provisions commenced operation on 1 July 2004.

29 See, for example, Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003, *Explanatory Memorandum*, paras [4.271]-[4.280], "Shareholder Participation and Information". According to the Explanatory Memorandum:-

activism,[30] and enabling shareholders to "influence the direction of the companies in which they invest".[31] Similarly, the UK reforms were accompanied by strong governmental rhetoric concerning the need to encourage greater shareholder democracy and activism.[32]

This theme of shareholder participation underpinned Australian and UK reforms in the area of executive remuneration.[33] Thus, for example, the Australian *CLERP 9 Act* 2004 permitted greater shareholder involvement in remuneration issues by requiring shareholders to pass a non-binding resolution at the annual general meeting approving the directors' remuneration report.[34] An analogous provision was introduced two years earlier in the UK.[35]

> Shareholders can and should play a key role in promoting good corporate governance practices by influencing the management of corporations through participating at general meetings ... It is sought to increase the practical opportunities for shareholders to assess and influence the performance of the board by effectively participating in general meetings of corporations" (*Id*, paras [4.271] - [4.272]).

30 See, for example, *id*, para [1.4], stating that "[t]he underlying objective of the reforms is to improve the operation of the market by promoting transparency, accountability and shareholder activism". See also *id*, para [4.71].

31 *Id*, para [4.174].

32 See Oliver Morgan, "Labour Fosters Investor Revolt: Manifesto Pledge to Encourage Shareholder Activism", *The Observer*, 4 April 2004, 1. See generally Eilis Ferran, "Company Law Reform in the UK: A Progress Report", *ECGI Working Paper No. 27/2005* (March 2005, available at http://ssrn.com/abstract=644203), 27-28. For example, the Secretary of State for Trade and Industry applauded a "welcome increase in the level of shareholder activism on the issue of directors' remuneration" (DTI, *Rewards for Failure*, Foreword, 5, cited in Ferran, *id*, 28).

33 Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003, *Explanatory Memorandum*, paras [5.415], [5.435]. See generally Jennifer G. Hill, "Regulating Executive Remuneration: International Developments in the Post-Scandal Era" (2006) 3 *European Company Law* 64, 67-68.

34 See ss 250R(2) and 249L *Corporations Act* 2001 (Cth). See generally Larelle Chapple and Blake Christensen, "The Non-Binding Vote on Executive Pay: A Review of the CLERP 9 Reform" (2005) 18 *Aust J Corp L* 263.

35 The Directors' Remuneration Report Regulations 2002, S.I. 2002/1986 (UK). The provision requiring shareholder approval of the directors' remuneration report is now found in section 439 of the recently enacted UK *Companies Act* 2006. See generally Eilis Ferran, "Company Law Reform in the UK: A Progress Report", *ECGI Working Paper No. 27/2005* (March 2005, available at http://ssrn.com/abstract=644203), 28. Evidence from the first three years of operation of the non-binding vote in the UK suggests that it has had an effect on remuneration practices and excessive compensation. See Kym Sheehan, "Is the Outrage Constraint an

In spite of its non-binding status, the explicit goal of the Australian shareholder remuneration resolution is to facilitate more active shareholder involvement in compensation issues and to permit shareholders to express their opinion collectively.[36] The Explanatory Memorandum to the *CLERP 9 Act* envisages greater consultation and information flow between directors and shareholders, stating that it is essential for directors to communicate with shareholders to ensure that appropriate remuneration policies are adopted.[37] The reform seeks to constrain excessive remuneration by censure and "shaming",[38] and from this perspective may be a potentially powerful governance mechanism.[39] In the light of these reforms, it has been claimed that "enhancing shareholder participation is now undoubtedly a legitimate corporate governance objective" in Australia.[40]

The US post-scandal reforms present an interesting contrast to Australia and the UK in this regard. Protection of shareholder interests was a clear priority and part of the legislative intent of the reforms;[41] enhancement of shareholder participatory rights

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Effective Constraint on Executive Remuneration? Evidence from the UK and Preliminary Results from Australia" (March 2007, available at http://ssrn.com/abstract=974965).

36 Corporate Law Economic Reform Program (Audit Reform and Corporate Disclosure) Bill 2003, *Explanatory Memorandum*, paras [5.434]-[5.435].

37 *Id*, para [4.353]. According to the Explanatory Memorandum, although it is normally the board's function to determine executive remuneration, "[i]n performing their function, boards need to be accountable for their decisions and shareholders need to be in a position to exercise their rights in an active and informed way". *Id*, para [5.413].

38 See generally David A. Skeel, "Shaming in Corporate Law" (2001) 149 *U Pa L Rev* 1811.

39 See Jennifer G. Hill, "Regulating Executive Remuneration: International Developments in the Post-Scandal Era" (2006) 3 *European Company Law* 64, 69-71. For preliminary evidence regarding the use of the advisory vote on executive pay in Australia following its first year of operation, see Kym Sheehan, "Is the Outrage Constraint an Effective Constraint on Executive Remuneration? Evidence from the UK and Preliminary Results from Australia" (March 2007, available at http://ssrn.com/abstract=974965), 24-29.

40 James McConvill and Mirko Bagaric, "Towards Mandatory Shareholder Committees in Australian Companies" (2004) 28 *Melb U L Rev* 125, 131.

41 The preamble to the *Sarbanes-Oxley Act* appears to confirm this focus, stating that it is an Act "[t]o protect investors by improving the accuracy and reliability of corporate disclosures made pursuant to the securities laws, and for other purposes". See generally Roberta S. Karmel, "Should a Duty to the Corporation be Imposed on Institutional Shareholders?" (2004) 60 *Bus Law* 1, 2, arguing that the *Sarbanes-Oxley Act* 2002 reinforces shareholder primacy norms in corporate law. *Cf* Donald C. Langevoort, "The Social Construction of *Sarbanes-Oxley*"

was not.[42] Commentators have described the refusal of the *Sarbanes-Oxley Act* 2002 to grant shareholders greater governance power and participatory rights in, for example, the director election process, as notable[43] and potentially "the forgotten element" of the US reforms.[44]

2. The Great Debate - Shareholder Empowerment and US Corporate Law

> "There's a battle outside and it's ragin'".
>
> Bob Dylan[45]

In spite of its absence from the US 2002 reforms, the theme of investor participation has taken center-stage in the recent US corporate law debate on shareholder empowerment and in several reform proposals. This debate has drawn attention to differences between US law relating to shareholder rights and analogous principles in the UK and Australia. These differences also lay at the heart of the revolt concerning News Corp's re-incorporation.

Instigating the controversial shareholder empowerment debate, Professor Bebchuk has advocated readjusting the balance of power between management and shareholders in some key areas of US corporate law, including the corporate election

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(2007) 105 *Mich L Rev* 1817, 1828*ff*, arguing that although the *Sarbanes-Oxley Act* is, by its terms, about investor protection, the long-term effect of the Act may be less about protection of investor interests than about public accountability.

42 Jennifer G. Hill, "Regulatory Responses to Global Corporate Scandals" (2005) 23 *Wisconsin Int'l LJ* 367, 392; Langevoort, *id*, 1829.

43 Langevoort, *ibid*.

44 See William B. Chandler and Leo E. Strine, "The New Federalism of the American Corporate Governance System: Preliminary Reflections of Two Residents of One Small State" (2003) 152 *U Pa L Rev* 953, 999.

45 Bob Dylan, *The Times They are A-Changin'* (1964).

process ("the corporate election issue")[46] and amendment of the corporate constitution ("the constitutional amendment issue").[47]

Shareholder involvement in corporate elections became a live topic when the SEC recommended in its 2003 Staff Report[48] that there should be increased shareholder participation in the US director nomination process, via use of the company's proxy statement to conduct a contested board election. This was by no means a new debate in US corporate law; the issue has periodically emerged for at least fifty years.[49] In the debate's most recent iteration, Bebchuk urges reform on the basis that the supposed power of shareholders to replace directors is illusory under the current corporate election system.[50] In spite of the SEC's initial enthusiasm for such reform, the issue of allowing shareholders increased participation in the director nomination process was subsequently described as "moribund".[51]

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46 See Lucian A. Bebchuk, "The Myth of the Shareholder Franchise" (2007) 93 *Va L Rev* 675, 696-697; Lucian A. Bebchuk, "The Case for Shareholder Access to the Ballot" (2003) 59 *Bus Law* 43.

47 See Lucian A. Bebchuk, "Letting Shareholders Set the Rules" (2006) 119 *Harv L Rev* 1784; Lucian A. Bebchuk, "The Case for Increasing Shareholder Power" (2005) 118 *Harv L Rev* 833.

48 SEC Staff Report, *Review of the Proxy Process Regarding the Nomination and Election of Directors*, Division of Corporate Finance, 15 July 2003. The SEC issued proposed proxy rules on 14 October 2003. The SEC had earlier announced that it was reviewing its policies on elections for corporate boards and shareholder proposals under Securities Exchange Act Rule 14a-(8) to increase shareholder democracy, following an SEC ruling, which permitted Citigroup to exclude shareholder nominations for board elections. See SEC, *Press Release No 2003-46*, 14 April 2003; Deborah Solomon, "SEC Plans Comprehensive Look at Rules for Proxy Exclusions", *The Wall Street Journal*, 15 April 2003, C9.

49 The issue was first addressed by the SEC in 1942. For a history of the debate, see Lewis J. Sundquist, "Comment: Proposal to Allow Shareholder Nomination of Corporate Directors: Overreaction in Times of Corporate Scandal" (2004) 30 *Wm Mitchell L Rev* 1471, 1473*ff*. See also Richard M. Buxbaum, "The Internal Division of Powers in Corporate Governance" (1985) 73 *Cal L Rev* 1671, 1682-83, expressing frustration in the mid-1980s with the "jawboning" of the SEC and NYSE, but ultimate lack of progress on the issue at that time.

50 See Lucian A. Bebchuk, "The Case for Shareholder Access to the Ballot" (2003) 59 *Bus Law* 43, 45; Lucian A. Bebchuk, "The Myth of the Shareholder Franchise" (2007) 93 *Va L Rev* 675. See also Vice Chancellor Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harv L Rev* 1759, 1782, arguing that reform of the current "incumbent-biased election process" in the US would accord legitimacy to directors and justify corporate law's deference to their autonomy and power.

51 See Vice Chancellor Leo E. Strine, *id*, 1776-1777.

Some recent developments, however, breathed further life into the corporate election issue. The Paulson Committee Report, for example, sought to reactivate it,[52] in conjunction with another contentious reform proposal - the introduction of majority, rather than plurality, voting for the election of directors.[53] The SEC also re-entered the fray, with the release of two conflicting proposals. The first had the effect of preventing shareholder participation in the director election process.[54] This proposal came in reaction to a federal appeals court decision[55] which adopted a liberal interpretation of Securities Exchange Act Rule 14a-8(i)(8), potentially providing an indirect method for increased shareholder participation in the director nomination process.[56] In contrast, the second SEC proposal would have allowed shareholders with five per cent of a company's voting shares to include in that company's proxy materials proposals for bylaw amendments regarding the nomination of directors.[57]

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[52] See Committee on Capital Markets Regulation, *Interim Report of the Committee on Capital Markets Regulation* (30 November 2006, revised version released 5 December 2006), 33, 106, calling on the SEC to "address and resolve, in its upcoming hearings, appropriate access by shareholders to the director nomination process".

[53] *Id*, 105; Hal S. Scott, "What is the United States Doing About the Competitiveness of its Capital Markets" (2007) 22(9) *Journal of International Banking Law and Regulation* 487, 490; Lucian A. Bebchuk, "The Myth of the Shareholder Franchise" (2007) 93 *Va L Rev* 675, 702-704. In June 2006, the American Bar Association's Committee on Corporate Laws adopted amendments to the *Model Business Corporation Act* to facilitate adoption of majority voting by shareholders (although plurality voting remains the default standard under the Act): see ABA Committee on Corporate Laws, News Release, "Committee on Corporate Laws Adopts Amendments to the Model Business Corporations Act Relating to Voting by Shareholders for the Election of Directors", 20 June 2006 (available at http://www.abanet.org/buslaw/committees/CL270000pub/nosearch/mbca/amendments/release.pdf); Kaja Whitehouse, "Bar Association Releases New Rules on Director Elections", *Dow Jones Newswires*, 20 June 2006. In addition, ss 141(b) and 216 of the Delaware General Corporation Law were amended in 2006 to permit shareholders to adopt a majority voting norm, and to prevent management from amending or repealing any majority voting bylaws adopted by shareholders: see Richard P. Swanson and Darlene F. Routh, "Shareholders Ready for Battle: Second Circuit Ruling, Along with Other Changes, Portends a Wave of Proxy Rights", *New York LJ*, 20 November 2006, 9.

[54] SEC, *Shareholder Proposals Relating to the Election of Directors: Release No. 34-56161*, 27 July 2007 (available at http://www.sec.gov/rules/proposed/2007/34-56161.pdf).

[55] *American Federation of State, County and Municipal Employees, Employees Pension Plan v American International Group, Inc* 462 F.3d 121 (2d Cir. 2006).

[56] The court limited the election exclusion under Securities Exchange Act Rule 14a-8(i)(8) to proposals relating to a particular election. The court held that proposals which established the procedural rules governing elections generally (such as a procedure permitting shareholder-nominated candidates to be included on the corporate ballot), would not fall within the scope of the election exclusion. *Ibid*.

[57] SEC, *Shareholder Proposals: Release No. 34-56160*, 27 July 2007 (available at http://www.sec.gov/rules/proposed/2007/34-56160.pdf). Some investor groups were highly

Internal disagreement among commissioners at the SEC explains the release of these two separate, yet opposing, proposals.[58] In late 2007, the SEC voted to maintain the status quo and adopt the first proposal, restricting shareholder participation in the director election process.[59]

Bebchuk's second set of reform proposals involves increasing US shareholder powers to initiate and effect change to governance structures by, for example, alteration to the corporate charter.[60] The ability of shareholders to effect corporate change through constitutional amendment is extremely limited in the US. Under both the Delaware General Corporation Law ("Delaware Code") and the Model Business Corporation Act ("MBCA"), shareholders are precluded from initiating changes to the corporate charter.[61]

At first sight, the potential for shareholders to achieve corporate governance change via a company's bylaws appears more promising, since both the Delaware Code and the MBCA grant shareholders power to initiate and to effect changes to the bylaws.[62] Since these statutes explicitly permit the bylaws to contain provisions relating to the business of the corporation and the conduct of its affairs, this would appear to give US shareholders significant powers with respect to constitutional change. There is,

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critical of the proposed five per cent threshold: see Judith Burns, "SEC Proxy Access Proposal Draws Fire from Investors", *The Wall Street Journal*, 11 July 2007, D2.

58 Two Democratic commissioners voted in favor of the proposal affording greater participation rights to shareholders. Two Republican commissioners voted in favor of the converse proposal. Rather than supporting one proposal alone, Chairman Christopher Cox voted both ways. See Kara Scannell, "SEC's Solomon? Cox Splits Vote on Proxy Access – Chairman Backs Change and the Status Quo; Buying Time to Fix Rule", *The Wall Street Journal*, 26 July 2007, C1; Stephen Labaton, "A Public Airing for Proposals on Shareholders", *New York Times*, 26 July 2007, 3.

59 See SEC, *SEC Votes to Codify Longstanding Policy on Shareholder Proposals on Election Procedures: Release 2007-246*, 28 November 2007 (available at http://www.sec.gov/news/press/2007/2007-246.htm).

60 See Lucian A. Bebchuk, "The Case for Increasing Shareholder Power" (2005) 118 *Harv L Rev* 833.

61 See Del. Code Ann, tit 8, s 242(b); Model Bus. Corp. Act s 10.03.

62 See Del. Code Ann, tit 8, s 109; Model Bus. Corp. Act s 10.20. Under the MBCA provision, shareholders have concurrent power with directors to amend the bylaws, however, under the Delaware provision, directors will only have concurrent power to amend the bylaws if such power is conferred in the company's certificate of incorporation.

however, a Catch 22-like twist. It is in the form of the statutory qualification to the effect that no provision in the bylaws can be inconsistent with US state law or with the corporation's charter.[63] The Delaware Code vests power to manage the corporation's business in the board of directors, except as is otherwise provided by the statute or the certificate of incorporation.[64] The absence of any reference to the bylaws in this qualification dilutes the efficacy of bylaw amendment as a tool for reallocation of power between shareholders and management.

US corporate law is strikingly different to UK and Australian corporate law in relation to the ability of shareholders to alter the constitution. Under traditional English and Australian law principles, the constitution[65] is freely alterable[66] by special resolution of the shareholders.[67] The board's managerial powers are expressly constrained by any powers reserved to the shareholders in general meeting, either by statute or the company's constitution.[68] Any provision attempting to contract out, or deprive, the shareholders of their inherent power to alter the constitution would be invalid under

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63 See Del. Code Ann, tit 8, s 109(b); Model Bus. Corp. Act s 10.20.

64 Del. Code Ann, tit 8, s 141(a). See also Model Bus. Corp. Act s 8.01.

65 Early UK and Australian corporate law recognized two distinct constitutional documents: the memorandum of association and the articles of association. The division between the memorandum and articles is retained in the recently introduced *Companies Act* 2006 (UK), however the memorandum is now largely of historical significance and contains only basic information. It will no longer be possible to amend the memorandum of a company formed under the new Act: *Explanatory Notes to Companies Act 2006* (available at http://www.opsi.gov.uk/ACTS/en2006/2006en46.htm), paras [33] and [65]. The articles of association are now the sole constitutional document: *id*, para [34]. Companies may also choose to adopt any or all of the 'model articles' as prescribed by the Secretary of State (s 19). Australian law abolished the requirement for a constitution in 1998, and companies may instead adopt "replaceable rules" under s 135 of the *Corporations Act* 2001 (Cth).

66 See also *Walker v London Tramways Co* (1879) 12 Ch D 705; *Allen v Gold Reefs of West Africa Ltd* [1900] 1 Ch 656 (especially the comments of Lindley MR at 671); *Peters' American Delicacy Co Ltd v Heath* (1939) 61 CLR 457.

67 Section 136(2) *Corporations Act* 2001 (Cth); s 21 *Companies Act* 2006 (UK). Under 136(3) *Corporations Act* 2001 (Cth), it is possible, however, for the company's constitution to provide that a further requirement or condition be met before the alteration is effective. In the UK, s22 of the *Companies Act* 2006 (UK) permits members, in more limited circumstances than its Australian counterpart, to 'entrench' certain provisions by agreeing to additional conditions that must be met for amendment to succeed.

68 See, for example, s 198A(2) *Corporations Act* 2001 (Cth).

UK or Australian law, as contrary to statute.[69] Shareholders may initiate amendment to the constitution, by proposing a resolution at the annual general meeting or by convening a special shareholders' meeting. The power of shareholders to convene meetings under current Australian law is particularly generous, by international standards.[70]

The US rules relating to charter alteration, and shareholder voting generally, reflect a governance model in which directors are essentially cast in the role of gatekeeper,[71] and shareholders in the role of supplicant.[72] This relationship is alien to traditional UK and Australian principles of corporate law, which until recently did not recognize precatory or advisory resolutions by shareholders.[73] Rather, UK and Australian principles on allocation of power appear to be based on a constitutional model of separate and autonomous spheres of authority for directors and shareholders.[74]

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69 See, for example, *Allen v Gold Reefs of West Africa Ltd* [1900] 1 Ch 656, 671; *Peters' American Delicacy Co Ltd v Heath* (1939) 61 CLR 457, 479. Nonetheless, there are several techniques, such as weighted voting, entrenchment clauses or shareholder agreements, whereby free alterability of the constitution can effectively be reduced or subverted. See, for example, *Bushell v Faith* [1970] A.C. 1099; *Russell v Northern Bank Development Corp Ltd* [1992] 3 All ER 161.

70 As discussed in detail later in the paper, shareholders with at least 5% of votes or 100 members by number may requisition a shareholder meeting (s 249D *Corporations Act* 2001 (Cth)) or propose a resolution (s 249N *Corporations Act* 2001 (Cth)). In contrast, the basic rule under UK corporate law is that only shareholders with at least 10% of voting shares may direct the board to convene a meeting (s 303(3) *Companies Act* 2006 (UK)).

71 See Charles O'Kelley and Robert B. Thompson, *Corporations and Other Business Associations: Cases and Materials* (5th ed, 2006), 145; Stephen M. Bainbridge, "Unocal at 20: Director Primacy in Corporate Takeovers" (2006) 31 *Del J Corp L* 769, 771.

72 See, for example, *Continental Securities Co v Belmont* 206 NY 7, 16-17; 99 NE 138, 141 (1912), stating that any action by shareholders is "necessarily in the form of an assent, request or recommendation".

73 See, for example, *NRMA v Parker* (1986) 6 NSWLR 517, 522; *Winthrop Investments Ltd v Winns Ltd* [1975] 2 NSWLR 666, 683 (adopting the view that advisory resolutions by shareholders were not recognized in law and could have no effect). The recent introduction of a non-binding shareholder vote in relation to executive pay in the UK and Australia therefore diverges from tradition in these jurisdictions. See above n33*ff*.

74 See, for example, *John Shaw & Sons (Salford) Ltd v Shaw* [1935] 2 KB 113, 134 stating "[a] company is an entity distinct alike from its shareholders and its directors … [The shareholders] cannot themselves usurp the powers which by the articles are vested in the directors any more than the directors can usurp the powers vested by the articles in the general body of shareholders". See also *Automatic Self Cleansing Filter Syndicate Co, Ltd. v Cuninghame* [1906] 2 Ch 34; *Howard Smith Ltd v Ampol Petroleum Ltd* (1974) 3 ALR 448, 457.

This paradigm difference between US and UK law, which directly affects the balance of power between shareholders and management, arguably derives from deep historical differences in the evolution of corporations in these jurisdictions[75] and constitutes an interesting example of path dependence in operation.[76] Whereas US corporate law evolved out of state-based charters, the same was not true of UK companies, whose origins can be traced to joint-stock companies, which were unincorporated partnerships. Historically, these different origins meant that UK company law was more firmly based on partnership law and contractual principles than US corporate law, resulting in greater freedom and flexibility for participants themselves to allocate power within UK companies.[77] These divergent origins have significant implications for a wide range of contemporary issues in corporate law, such as shareholder rights,[78] and hostile takeovers.[79]

Bebchuk's constitutional amendment reform proposals would, by allowing shareholders to initiate and make constitutional alterations to the corporate charter, significantly alter the balance of power between shareholders and management under US corporate law. The proposed reforms would shift US law away from its

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75 See generally L.C.B. Gower, "Some Contrasts Between British and American Corporation Law" (1956) 69 *Harv L Rev* 1369.

76 See generally Mark J. Roe, "Path Dependence, Political Options and Governance Systems", in Klaus J. Hopt and Eddy Wymeersch (eds), *Comparative Corporate Governance: Essays and Materials* (1997), 165.

77 See generally L.C.B. Gower, "Some Contrasts Between British and American Corporation Law" (1956) 69 *Harv L Rev* 1369, 1371-1372.

78 See, for example, Jonathan Rickford, "Do Good Governance Recommendations Change the Rules for the Board of Directors?" in Klaus J. Hopt and Eddy Wymeersch (eds), *Capital Markets and Company Law* (2003), 461, 474, who states, "[w]hile the focus in the UK has been on attracting capital, the focus in the US has been on attracting managers…" (cited in Deborah A. DeMott, "The Texture of Loyalty" in Joseph J. Norton, Jonathan Rickford and Jan Kleineman (eds), *Corporate Governance Post-Enron: Comparative and International Perspectives* (2006), 23, n13).

79 See John Armour and David A. Skeel, "Who Writes the Rules for Hostile Takeovers, and Why? The Peculiar Divergence of U.S. and U.K. Takeover Regulation" (2007) 95 *Geo LJ* 1727, arguing that while self-regulation of takeovers in the UK led to a regime benefiting institutional investors, judicial regulation in the US benefited management. See also Paul Davies and Klaus J. Hopt, "Control Transactions" in Reinier Kraakman et al (eds), *The Anatomy of Corporate Law: A Comparative and Functional Approach* (2004), 157, 172.

traditional "board as gatekeeper" model and towards the constitutional model favored in the UK and Australia.

Bebchuk has advanced the shareholder empowerment reform proposals on the basis of an efficiency, rather than a shareholder democracy, rationale.[80] The presumed efficiency gains include a reduced need for outside intervention by legislators and regulators, with the mere threat of shareholder participation acting as a disciplinary mechanism for managerial decisions.[81]

Issues relating to the balance of power between shareholders and management permeate several other recent US developments. The Paulson Committee Report, for example, argued that the US post-scandal reforms were overly stringent by international standards, resulting in reduced competitiveness of US markets.[82] As a concomitant to this argument, the Committee recommended increased shareholder rights and participation as an alternative regulatory technique.[83] Contrary to the assumption in the influential "law matters" hypothesis that US corporate law provides

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80 Lucian A. Bebchuk, "The Myth of the Shareholder Franchise" (2007) 93 *Va L Rev* 675, 678. James McConvill considers it ironic that advocates from both sides of the shareholder empowerment debate adopt the same view regarding the place of shareholder participation, perceiving it as a means to enhance corporate performance rather than as an end in itself. See James McConvill, "Shareholder Empowerment as an End in Itself: A New Perspective on Allocation of Power in the Modern Corporation" (2007) *Ohio Northern University Law Review* (forthcoming, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=943907), 2, 11-18.

81 Lucian A. Bebchuk, "The Case for Increasing Shareholder Power" (2005) 118 *Harv L Rev* 833, 838-839.

82 Committee on Capital Markets Regulation, *Interim Report of the Committee on Capital Markets Regulation* (30 November 2006, revised version released 5 December 2006), xi. The Paulson Committee Report was followed by another report, McKinsey & Company, *Sustaining New York's and the U.S.' Global Financial Services Leadership*, Report to MR Bloomberg & CE Schumer (2007), which addressed similar concerns.

83 Key proposals of the Committee on Capital Markets Regulation relating to enhancement of shareholder rights included:- (i) the requirement that classified boards gain the approval of shareholders prior to implementing a poison pill (ii) the adoption of majority, rather than plurality, voting for board directors (iii) clarification of the rights of shareholders with respect to gaining access to the company proxy to nominate directors for election (iv) enhancing shareholders' ability to access alternative means of dispute resolution (Paulson Committee 2006, xii-xiii, 93-114). For subsequent developments concerning these proposals, see Hal S. Scott, "What is the United States Doing About the Competitiveness of its Capital Markets" (2007) 22(9) *Journal of International Banking Law and Regulation* 487, 489-490.

strong minority shareholder protection,[84] the Paulson Committee Report considered that, in fact, "lack of shareholder rights" was affecting the level of investment in US companies.[85] While an efficiency/firm value justification underpins much of the Paulson Committee's discussion, there are some statements suggesting that the fundamental power imbalance between management and shareholders is an independent justification for stronger shareholder rights.[86]

The Paulson Committee also contemplated granting US shareholders an advisory vote on executive remuneration,[87] similar to the post-Enron reforms introduced in the UK and Australia. A reform proposal to this effect later become the subject of Democrat-instigated congressional consideration.[88] In April 2007, the House of Representatives overwhelmingly passed a Bill that would accord US shareholders an advisory vote on executive remuneration,[89] however, ultimate translation of the Bill into legislation is in doubt, due to White House opposition.[90]

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84 See, for example, Rafael La Porta, Florencio Lopez-de-Silanes, Andrei Shleifer and Robert Vishny, "Law and Finance" [1998] 106 *J Political Economy* 1113, 1128, 1130; Rafael La Porta, Florencio Lopez-de-Silanes & Andrei Shleifer, "Corporate Ownership Around the World" (1999) 54 *J Fin* 471.

85 See Hal S. Scott, "What is the United States Doing About the Competitiveness of its Capital Markets" (2007) 22(9) *Journal of International Banking Law and Regulation* 487, 489.

86 According to the Paulson Committee, "[w]hen firms have a choice of legal regime, any policy proposal should adopt as a default the option most favorable to shareholders, given the fundamental asymmetry of power between managers and shareholders" (*Interim Report of the Committee on Capital Markets Regulation* (30 November 2006, revised version released 5 December 2006), 103).

87 *Id*, 109.

88 Erin White and Aaron O. Patrick, "Shareholders Push for Vote on Executive Pay", *The Wall Street Journal*, 26 February 2007, B1.

89 *Shareholder Vote on Executive Compensation Act* (HR 1257) (2007). After the bill was passed by the House of Representatives, an identical bill (*A bill to amend the Securities Exchange Act of 1934 to provide shareholders with an advisory vote on executive compensation* (S 1181)(2007)) was introduced into the Senate on 20 April 2007, and was referred to the Senate Committee on Banking, Housing and Urban Affairs.

90 Kara Scannell and Siobhan Hughes, "House Clears an Executive-Pay Measure", *The Wall Street Journal*, 21 April 2007, A3.

Few US commentators seem to doubt that there is "ample room for increasing shareholder power" under US corporate law.[91] Nonetheless, the shareholder empowerment reform proposals have elicited a surprisingly polarized debate[92] and backlash,[93] with many commentators doubting the wisdom of increasing shareholder power at the expense of managerial power.

Criticism of the shareholder empowerment proposals emanates from a variety of perspectives. First, paralleling the famous critique over two decades ago by law and economics scholars against the anti-managerialists,[94] some commentators argue that shareholder disempowerment is not a cause for angst, but rather a positive attribute of US corporate law. Rules according deference to managerial autonomy and severely limiting shareholder participation are seen as a deliberate choice, not a perversion, of corporate law. Responses to the shareholder empowerment reform proposals by Chancellor Strine,[95] Bainbridge,[96] Stout,[97] and Lipton and Savitt[98] fall within this

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91 See Iman Anabtawi, "Some Skepticism About Increasing Shareholder Power" (2006) 53 *UCLA L Rev* 561, 569. See also Lynn A. Stout, "The Mythical Benefits of Shareholder Control" (2007) 93 *Va L Rev* 789, 789-790, who agrees with Bebchuk that "shareholder control is largely a myth in public companies today". *Cf* Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733, 734.

92 See, for example, recent special issues of the *Virginia Law Review* and the *Harvard Law Review*, devoted to the shareholder empowerment debate. See generally Lucian A. Bebchuk, "The Myth of the Shareholder Franchise" (2007) 93 *Va L Rev* 675; Lynn A. Stout, "The Mythical Benefits of Shareholder Control" (2007) 93 *Va L Rev* 789; Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733; Stephen M. Bainbridge, "Director Primacy and Shareholder Disempowerment" (2006) 119 *Harv L Rev* 1735; Vice Chancellor Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harv L Rev* 1759; Lucian A. Bebchuk, "Letting Shareholders Set the Rules" (2006) 119 *Harv L Rev* 1784.

93 See "Battling for Corporate America – Shareholder Democracy", *The Economist*, 11 March 2006, 378.

94 See, for example, Ralph K. Winter, "State Law, Shareholder Protection, and the Theory of the Corporation" (1977) 6 *J Legal Stud* 251; Frank H. Easterbrook and Daniel R. Fischel, "Voting in Corporate Law" (1983) 26 *J Law and Economics* 395, 396. For further discussion of this critique, see generally, Jennifer G. Hill, "Visions and Revisions of the Shareholder" (2000) 48 *Am J Comp L* 39, 57-59 and Gregory A. Mark, "Some Observations on Writing the Legal History of the Corporation in the Age of Theory", in Lawrence E. Mitchell (ed), *Progressive Corporate Law* (1996), 67, 71, who states that according to contractarians, "[t]he putative abuse of shareholders … is largely mythical".

95 Vice Chancellor Strine's analysis is from the perspective of the "open-minded corporate law 'traditionalist'". See Vice Chancellor Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harvard L Rev* 1759, 1759.

critical rubric. Bainbridge, for example, does not dispute Bebchuk's assessment of shareholder disempowerment, but rather welcomes it as providing evidence that current US corporate law is based on an efficient model of centralized board authority.[99] This line of criticism highlights the distinction between shareholder participation rights and protection of shareholder interests. Reflecting the earlier contractarian critique of anti-managerialism, it stresses the voluntary nature of investment in public companies[100] and rejects the need for greater participation rights on the basis that shareholder *interests* are already safeguarded via the market,[101] modern governance pressures,[102] and the ability of shareholders to self-protect through mechanisms such as diversification.[103]

Secondly, commentators have criticized the shareholder empowerment proposals from an evolutionary/efficiency perspective, asking why, if shareholder empowerment is a valuable corporate governance attribute, we do not already see it in the

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96 Stephen M. Bainbridge, "Director Primacy and Shareholder Disempowerment" (2006) 119 *Harv L Rev* 1735.

97 Lynn A. Stout, "The Mythical Benefits of Shareholder Control" (2007) 93 *Va L Rev* 789.

98 Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733.

99 See Stephen M. Bainbridge, "Director Primacy and Shareholder Disempowerment" (2006) 119 *Harv L Rev* 1735, 1735-1736. See also Lipton and Savitt, *id*, 740; Vice Chancellor Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harvard L Rev* 1759, 1763.

100 See Lynn A. Stout, "The Mythical Benefits of Shareholder Control" (2007) 93 *Va L Rev* 789, 801. *Cf*, however, Chancellor Leo E. Strine, "Toward Common Sense and Common Ground? Reflections on the Shared Interests of Managers and Labor in a More Rational System of Corporate Governance" (2007) *J Corp L* (forthcoming, available at http://ssrn.com/abstract=989624), noting that we live in an age of "forced capitalism", in which most citizens have "little choice but to invest in the market" (*Id* at 6).

101 See Stephen M. Bainbridge, "Director Primacy and Shareholder Disempowerment" (2006) 119 *Harv L Rev* 1735, 1746-1747. As in the earlier debate between contractarians and anti-managerialists, Bainbridge and Bebchuk exhibit different levels of faith in the market as a constraining force on management.

102 Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733, 747, 752-753.

103 Vice Chancellor Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harvard L Rev* 1759, 1764.

marketplace.[104] While this is an intriguing question with respect to US corporate law, it is a less persuasive argument from a comparative corporate governance perspective. As the events surrounding News Corp's re-incorporation in Delaware show, there is considerable divergence in common law countries concerning shareholder participation in corporate governance.

A third line of criticism is of the "be careful what you wish for" variety. It views the idea of shareholder empowerment as essentially pernicious - certainly more dangerous, at least, than shareholder disempowerment. It has been argued, for example, that that shareholder empowerment would subvert the most advantageous feature of corporations, centralized board power, and potentially result in board blackmail.[105] In the context of the corporate election issue, some commentators have claimed that increased shareholder participation in the director nomination process would promote special interest directors, undermine board collegiality and introduce the risk of "balkanized and dysfunctional boards".[106] A variant of this argument stresses that shareholders are themselves a fragmented and fractured group with disparate interests.[107] The "be careful what you wish for" argument suggests that shareholders are likely to abuse participatory powers, engage in opportunism, prefer their private sectional interests to those of the shareholders generally,[108] or succumb

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104 See Stephen M. Bainbridge, "Director Primacy and Shareholder Disempowerment" (2006) 119 *Harv L Rev* 1735, 1736-1737; Strine, *id*, 1774; Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733, 743-744.

105 Bainbridge, *id*, 1749, 1756.

106 See Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733, 734, 748-749; Martin Lipton and Steven A. Rosenblum, "Election Contests in the Company's Proxy: An Idea Whose Time Has Not Come" (2003) 59 *Bus Law* 67. See also letter from Henry A. McKinnell, the Business Roundtable to Alan L. Beller, SEC, dated 1 October 2003; Statement by the Business Roundtable on the SEC's Proposed Shareholder Access Amendments, Press Release, 8 October 2003 (available at http://www.brt.org); Lewis J. Sundquist, "Comment: Proposal to Allow Shareholder Nomination of Corporate Directors: Overreaction in Times of Corporate Scandal" (2004) 30 *Wm Mitchell L Rev* 1471.

107 See Iman Anabtawi, "Some Skepticism About Increasing Shareholder Power" (2006) 53 *UCLA L Rev* 561, 564-565, 578*ff*; Vice Chancellor Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harvard L Rev* 1759, 1765-1766; Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733, 756-757.

108 Anabtawi, *id*, 598.

to the "momentary majority impulse".[109] Under this line of argument, not only does the company need protection from predatory conduct of its shareholders, but shareholders need protection from each other.[110]

A fourth type of criticism is based on a futility argument. This argument appears, at first sight, difficult to reconcile with the "be careful what you wish for" argument, though they are often conjoined. While the latter argument predicts dire consequences in altering legal rules to permit greater shareholder participation in corporate governance, the futility argument warns of the opposite result. The futility argument suggests that such changes to legal rules would be wholly ineffective, given collective action problems and rational shareholder apathy.[111] The explanation of the paradox between these two arguments appears to lie in the fragmented nature of the shareholder body.[112] Thus, it is assumed that although apathy would generally prevail among the majority of shareholders, including institutional investors,[113] the groups that would take advantage of enhanced shareholder powers are those considered by Bebchuk's detractors most likely to abuse them – namely, union and public employee pension funds.[114]

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109 Vice Chancellor Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harvard L Rev* 1759, 1763. See also Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733, 733.

110 Lynn A. Stout, "The Mythical Benefits of Shareholder Control" (2007) 93 *Va L Rev* 789, 794; Chancellor Leo E. Strine, "Toward Common Sense and Common Ground? Reflections on the Shared Interests of Managers and Labor in a More Rational System of Corporate Governance" (2007) *J Corp L* (forthcoming, available at http://ssrn.com/abstract=989624), 13.

111 See, for example, Stephen M. Bainbridge, "Director Primacy and Shareholder Disempowerment" (2006) 119 *Harv L Rev* 1735, 1745, 1751-1753.

112 See generally, Iman Anabtawi, "Some Skepticism About Increasing Shareholder Power" (2006) 53 *UCLA L Rev* 561.

113 Stephen M. Bainbridge, "Director Primacy and Shareholder Disempowerment" (2006) 119 *Harv L Rev* 1735, 1751-1752.

114 *Id*, 1751; Vice Chancellor Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harvard L Rev* 1759, 1765; Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733, 744-745. On union corporate governance activism generally in the US, see Randall S. Thomas and Kenneth J. Martin, "Should Labor Be Allowed to Make Shareholder Proposals?" (1998) 73 *Wash L Rev* 41.

Fifth, some critics have used a precautionary principle to counter the reform proposals. Building on the "be careful what you wish for" argument, the precautionary principle asserts that, given the "likely and severe negative consequences"[115] of the proposals, a heavy onus should lie on those in favor of reform to demonstrate that the benefits would outweigh the costs. According to Lipton and Savitt, for example, "the policy considerations in favor of not jeopardizing the economy are so strong that not even a remote risk …is acceptable".[116]

Sixth, the timing of the reform proposals has been criticized via a "wait and see" argument. This argument stresses the fact that significant corporate governance changes, such as the strengthening of the role of independent directors, were introduced relatively recently under the US 2002 reforms, and that any rush to adopt additional changes should be deferred until the consequences of those reforms can be known and assessed.[117] This argument parallels recent criticism of the *Sarbanes-Oxley Act*, in which perceived defects of the legislation have been linked to the speed of its passage, and the level of associated deliberation and policy assessment.[118]

Seventh, the shareholder empowerment proposal has been condemned as promoting short-term thinking over long-term sustainability.[119] This critique particularly targets institutional investors, claiming that their incentives, including their compensation structures, encourage short-term goals to be prioritized over long-term wealth

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115 Lipton and Savitt, *id*, 734.

116 *Id*, 747, citing Martin Lipton, "Takeover Bids in the Target's Boardroom" (1979) 35 *Bus Law* 101, 104. See also Lynn A. Stout, "The Mythical Benefits of Shareholder Control" (2007) 93 *Va L Rev* 789, 798, 808.

117 Stephen M. Bainbridge, "Director Primacy and Shareholder Disempowerment" (2006) 119 *Harv L Rev* 1735, 1741.

118 See Roberta Romano, "The *Sarbanes-Oxley Act* and the Making of Quack Corporate Governance" (2005) 114 *Yale Law Journal* 1521, 1528, describing the *Sarbanes-Oxley Act* as "emergency legislation". *Cf* J. Robert Brown, "Criticizing the Critics: *Sarbanes-Oxley* and Quack Corporate Governance" (2006) 90 *Marquette Law Review* 309, who, while acknowledging that the *Sarbanes-Oxley Act* came into force quickly due to political pressures, argues that it nonetheless delivered real benefits and improvements in the corporate governance process.

119 Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733, 745-747.

creation. This problem was seen as a defining element of Enron and other corporate scandals.[120]

Another strand of the short-term versus long-term analysis relates to corporate theory. Some commentators claim that shareholder empowerment proposals rest on the flawed assumption that the role of directors is to serve the interests of shareholders, rather than stakeholders generally.[121] Bebchuk has explicitly disavowed the idea that his shareholder empowerment reform proposals are based upon corporate democracy or shareholder ownership rights.[122] Nonetheless, an underlying theme in the responses by some of his critics is that the concept of shareholder empowerment is misguided, since it would revive an outmoded and inappropriate image of the shareholder as "owner"[123] of the corporation[124] or principal in a principal-agent

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120 Stephen M. Bainbridge, "Director Primacy and Shareholder Disempowerment" (2006) 119 *Harv L Rev* 1735, 1764-1765. Vice Chancellor Strine's traditionalist analysis is also critical of institutional investors for fixating on "ideas du jour with no proven relationship to creating sustainable wealth". See Vice Chancellor Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harvard L Rev* 1759, 1766, 1771.

121 See, for example, Iman Anabtawi, "Some Skepticism About Increasing Shareholder Power" (2006) 53 *UCLA L Rev* 561, 571 and Vice Chancellor Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harvard L Rev* 1759, 1769, who states that "tilting the direction of corporate policy toward short-term thinking is counterproductive, not simply for investors but for other important constituencies such as employees and communities". See also Chancellor Leo E. Strine, "Toward Common Sense and Common Ground? Reflections on the Shared Interests of Managers and Labor in a More Rational System of Corporate Governance" (2007) *J Corp L* (forthcoming, available at http://ssrn.com/abstract=989624).

122 Lucian A. Bebchuk, "The Myth of the Shareholder Franchise" (2007) 93 *Va L Rev* 675, 678.

123 This argument is by no means new. See Edward S. Mason, "Introduction" in Edward S. Mason (ed), *The Corporation in Modern Society* (1959), 5, stating that "those days are gone forever" when corporate ownership by shareholders could be taken seriously. See generally Lynn A. Stout, "The Mythical Benefits of Shareholder Control" (2007) 93 *Va L Rev* 789, 804-805; Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733, 754-755.

124 See, for example, Martin Lipton and Steven A. Rosenblum, "Election Contests in the Company's Proxy: An Idea Whose Time Has Not Come" (2003) 59 *Bus Law* 67, 68, 70. See also Roberta S. Karmel, "Shareholder Nominations: Increased Access to Proxy Card?", *New York LJ*, 18 December 2003, 3; Lewis J. Sundquist, "Comment: Proposal to Allow Shareholder Nomination of Corporate Directors: Overreaction in Times of Corporate Scandal" (2004) 30 *Wm Mitchell L Rev* 1471, 1489*ff*, criticizing "shareholder democracy" as justification for proposed reforms in the area of director elections.

relationship with directors.[125] It is worth noting, however, that although shareholders are accorded significant participatory rights in corporate governance under UK law, the courts have firmly rejected a view of shareholders as corporate owners or principals.[126]

This theoretical critique of the shareholder empowerment proposals focuses on divergence between the interests of shareholders and other stakeholders, and assumes that there is an inevitable link between shareholder participation rights and dominance of shareholder interests. Comparative corporate governance offers some interesting insights about this assumption and suggests that the connection between shareholder participation rights and preeminence of shareholder interests is by no means clear-cut. In the UK and Australia post-Enron reforms, for example, there was strong support for strengthening shareholder participatory rights. Nonetheless, the dominant current policy focus in these countries is not on shareholder rights, but stakeholder interests and corporate responsibility. In the UK, the principle of "enlightened shareholder value",[127] which gained momentum over the last decade, was recently given legislative force under s 172 of the *Companies Act* 2006 (UK). This provision imposes a new statutory duty on directors to "promote the success of the company for the benefit of its members as a whole" and requires directors to consider a range of factors, including the long-term consequences of their decisions, the effect on stakeholder interests, and the impact of the company's operations on the community and environment. Such an emphasis on long-term performance of the company blurs the boundary between shareholder and stakeholder interests.[128] Corporate social responsibility has also recently become a major issue in Australia,[129] resulting in the

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125 See Lynn A. Stout, "The Mythical Benefits of Shareholder Control" (2007) 93 *Va L Rev* 789, 804.

126 See, for example, *Automatic Self Cleansing Filter Syndicate Co, Ltd. v Cuninghame* [1906] 2 Ch 34.

127 See generally Cynthia A. Williams and John M. Conley, "An Emerging Third Way? The Erosion of the Anglo-American Shareholder Value Construct" (2005) 38 *Cornell Int'l LJ* 493.

128 See Margaret M. Blair, "Directors' Duties in a Post-Enron World: Why Language Matters" (2003) 38 *Wake Forest L Rev* 885.

129 The recent focus on corporate social responsibility in Australia is largely as a result of a local scandal, the James Hardie saga. This involved a corporate reconstruction whereby asbestos-related liabilities were separated from other assets in the company through the creation of a

release of two government reports on the topic in 2006, by the Parliamentary Joint Committee on Corporations and Financial Services,[130] and the Corporations and Markets Advisory Committee.[131]

3. The Exodus of News Corp and Related Corporate Governance Issues

> "[W]e are tending toward a managerial, rather than a capitalist society…"
>
> William L. Cary[132]

> "Rupert Murdoch is a great Australian, in the sense that Attila was a great Hun"
>
> Geoffrey Robertson QC[133]

The events surrounding the re-incorporation of News Corporation ("News Corp")[134] are interesting in the light of the shareholder empowerment debate. Although some of Bebchuk's critics have argued that the dearth of shareholder participatory rights under US corporate law provides evidence that they are neither desired nor valued by

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foundation, which was subsequently found to have insufficient funds to meet legitimate compensation claims of mesothelioma sufferers. See generally Edwina Dunn, "James Hardie: No Soul to be Damned and No Body to be Kicked" (2005) 27 *Sydney L Rev* 339; Jennifer G. Hill, "Evolving 'Rules of the Game' in Corporate Governance Reform" in Justin O'Brien (ed), *Private Equity, Corporate Governance and the Dynamics of Capital Market Regulation* (2007), 29, 52-53.

130 Parliamentary Joint Committee on Corporations and Financial Services, *Corporate Responsibility: Managing Risk and Creating Value* (2006).

131 Corporations and Markets Advisory Committee, *The Social Responsibility of Corporations* (2006).

132 William L. Cary, "Federalism and Corporate Law: Reflections Upon Delaware" (1974) 83 *Yale LJ* 663, 670.

133 Cited in Richard Ackland, "We Must Not Over-egg Free Speech Argument", *Sydney Morning Herald*, 31 August 2007, 17.

134 Prior to the re-incorporation, the Australian entity was known as The News Corporation Limited.

investors,[135] background events to News Corp's exodus from Australia to Delaware present another picture. These events highlight the fact that shareholder rights - and the extent to which they are valued - differ considerably within the common law world. The Paulson Committee recognized this regulatory diversity, stating that "[o]verall, shareholders of US companies have fewer rights … than do their foreign competitors"[136] and expressed concern that inadequate shareholder protection might deter corporations from entering US public markets.[137]

The issue of the balance of power between shareholders and management came to the fore in Australia following an announcement by News Corp[138] in 2004, which signaled its intention to shift domicile from Australia to Delaware, to obtain primary listing on the New York Stock Exchange and to seek inclusion in the Standard & Poor's 500 Index ("S & P 500").[139] The re-incorporation proposal, which involved incorporating a new group parent company in the United States, was to be implemented by schemes of arrangement,[140] which rely on both shareholder consent and court approval under Australian law.[141]

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135 See, for example, Stephen M. Bainbridge, "Director Primacy and Shareholder Disempowerment" (2006) 119 *Harv L Rev* 1735, 1737; Lynn A. Stout, "The Mythical Benefits of Shareholder Control" (2007) 93 *Va L Rev* 789, 801-803.

136 Committee on Capital Markets Regulation, *Interim Report of the Committee on Capital Markets Regulation* (30 November 2006, revised version released 5 December 2006), 16.

137 *Id*.

138 News Corporation, Press Release, "News Corporation Plans to Reincorporate in the United States", 16 April 2004 (available at http://www.newscorp.com/news/news_207.html).

139 See, for example, News Corporation, *News Corporation Annual Report* (2004, available at http://www.newscorp.com/Report2004/2004_annual_report.pdf), 4-5; Grant Samuel & Associates, Independent Expert's Report, *Re-incorporation of The News Corporation Ltd in the United States and Acquisition of Queensland Press Pty Ltd*, 14 September 2004, E-1; "News Corp Prepares for U.S. Transfer, Listing on S&P 500", *The Wall Street Journal*, 27 October 2004.

140 See United States Securities and Exchange Commission, News Corporation, Form 8-K, Item 2.01, "Acquisition or Disposition of Assets" (12 November 2004), setting out the structure of the reorganization of the Australian corporation, The News Corporation Limited.

141 Schemes of arrangement are regulated under Chapter 5 of the *Corporations Act* 2001 (Cth). For an overview of the scheme of arrangement procedure in Australia, see Tony Damian and Andrew Rich, *Schemes, Takeovers and Himalayan Peaks: The Use of Schemes of Arrangement to Effect Change of Control Transactions* (2004), 8-19.

According to News Corp, the move to the US, where most of its operations were based,[142] was prompted by legitimate commercial goals, including the desire to gain greater access to US capital markets and enhance shareholder value.[143] Critics of the proposal argued, however, that the purpose of the re-incorporation was to strengthen managerial power vis-à-vis shareholder power within News Corp. They claimed that Delaware law provided less protection for minority shareholders than Australian corporate law, enabling the Murdoch family to entrench its interests more easily in the US.[144] In contrast to the Paulson Committee's concern that minimal shareholder rights might deter corporations from entering US public markets,[145] these critics claimed that this feature of Delaware law constituted its main allure for News Corp.

An independent expert's report,[146] prepared by Grant Samuel & Associates on behalf of News Corp, while finding that the re-incorporation proposal was in the best interests of the company's shareholders as a whole,[147] acknowledged a possible reduction of minority shareholder rights. The report stated that "the costs,

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142 Approximately 70% of the group's revenues and 80% of profits were derived from the US at the time of the re-incorporation proposal. Grant Samuel & Associates, Independent Expert's Report, *Re-incorporation of The News Corporation Ltd in the United States and Acquisition of Queensland Press Pty Ltd*, 14 September 2004, E-3.

143 News Corporation, *News Corporation Annual Report* (2004, available at http://www.newscorp.com/Report2004/2004_annual_report.pdf), 4. For other perceived benefits, see News Corporation, Press Release, "Australian Federal Court Approves Shareholder Meetings to Vote on Proposed Reincorporation", 15 September 2004, 2 (available at http://www.newscorp.com/news/news_216.html).

144 See, for example, Elizabeth Knight, "Murdoch Gymnastics Good for Investors", *Sydney Morning Herald*, 8 October 2004, 25, stating "[w]hat we will never know is the extent to which this move offshore was motivated by the potential re-rating or the deterioration of minorities' rights and the enhancement of Murdoch family control. Was the latter the prime aim or just a collateral gain?". See also Ben Power and Neil Chenoweth, "Funds Lash News Corp's US Move", *Australian Financial Review,* 28 September 2004, 1.

145 Committee on Capital Markets Regulation, *Interim Report of the Committee on Capital Markets Regulation* (30 November 2006, revised version released 5 December 2006), 16.

146 Although an independent expert's report is only required where a party to a corporate reconstruction is entitled to at least 30% of the voting shares (see Corporations Regulations, rules 8303 and 8306, Part 3, Schedule 8), the provision of such a report to members in a scheme of arrangement is standard commercial practice in Australia. See generally Tony Damian and Andrew Rich, *Schemes, Takeovers and Himalayan Peaks: The Use of Schemes of Arrangement to Effect Change of Control Transactions* (2004), 11, 127*ff*.

147 Where required, an independent expert's report must state whether, in the expert's opinion, the proposed scheme is in the best interests of the members and must set out reasons for that opinion: Corporations Regulations, rule 8303, Part 3, Schedule 8.

disadvantages and risks are not inconsequential but do not outweigh the advantages".[148] The Federal Court of Australia, in its subsequent approval of the schemes of arrangement implementing the proposal, noted that these advantages related mainly to the market for News Corp shares, and involved "judgments rather than propositions that can be empirically verified".[149]

In late July 2004, two institutional investors, the Australian Council of Super Investors Inc ("ACSI") and Corporate Governance International ("CGI") met with News Corp to discuss a range of corporate governance concerns relating to the effect of the re-incorporation proposal on shareholder rights.[150] ACSI and CGI, which had the support of several major international institutional investors,[151] subsequently launched a corporate governance campaign urging News Corp to transplant certain Australian shareholder protection provisions into its prospective Delaware charter.

As part of this campaign, ACSI and CGI drafted a document dealing with corporate governance - the so-called "Governance Article"[152] - which was provided to News Corp, with a request that its contents be included in News Corp's Delaware charter.[153] The Governance Article included a large number of Australian statutory provisions and "Best Practice" procedures. Its purpose was expressed to be:-

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148 See Grant Samuel & Associates, Independent Expert's Report, *Re-incorporation of The News Corporation Ltd in the United States and Acquisition of Queensland Press Pty Ltd*, 14 September 2004, E-3, E-126. See also E-10 – E-12, outlining further possible disadvantages for shareholders, particularly minority shareholders.

149 *News Corporation Ltd* [2004] FCA 1480, para [3] (per Hely J).

150 See *UniSuper Ltd v News Corporation* 2005 WL 3529317 (Del Ch).

151 For example, the Global Institutional Governance Network, comprising institutional investors such as British Hermes in the UK and CalPERS in the US, supported ACSI and CGI. See Stephen Bartholomeusz, "Activists Confront News on World Stage", *Sydney Morning Herald*, 28 September 2004, 22; Ben Power and Neil Chenoweth, "Funds Lash News Corp's US Move", *Australian Financial Review*, 28 September 2004, 1.

152 News Corporation Group, *Governance Article for New Delaware Parent Company: Preservation of Australian Public Investor Protection & Empowerment Provisions* (2004, on file with the author).

153 The Governance Article was sent to News Corp on 20 August 2004. See *UniSuper Ltd v News Corporation* 2005 WL 3529317, n8 (Del Ch).

(i) To preserve, in the constitution of this new Delaware incorporated Company and for the benefit of those public investors, key Australian investor protection and empowerment provisions…

(ii) To render inapplicable, for the benefit of those public investors, certain presumptions of Delaware/US law and practice which are contrary to key Australian investor protection and empowerment provisions, and

(iii) To include, in the constitution of this new Delaware incorporated Company and for the benefit of those public investors, other key elements of Australian and international best practice in corporate governance.[154]

Initially, News Corp made no concessions to the institutional investors' demands.[155] Echoing the arguments of Montesquieu,[156] News Corp claimed that the selective transplantation of Australian governance principles into the constitution of a Delaware-incorporated company would limit access to US institutional investor capital, confuse investors and put the corporation at a competitive disadvantage with regard to its US competitors, such as Viacom and Disney.[157]

Following News Corp's refusal to adopt the Governance Article, ACSI issued a critical press release, entitled "News Corporation settles for second best on governance".[158] By late September 2004, Institutional Shareholder Services ("ISS"), the largest US proxy adviser, had become involved in the fracas, adding its voice to

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154 News Corporation Group, *Governance Article for New Delaware Parent Company: Preservation of Australian Public Investor Protection & Empowerment Provisions* (2004, on file with the author), Clause 2, "Purpose and Intention".

155 See ACSI, Press Release, "News Corporation Settles for Second Best on Governance", 27 September 2004 (available at http://www.acsi.org.au/documents/17092004_Press_Release-News_Corporation.doc).

156 Montesquieu, *The Spirit of Laws* (1748). Montesquieu, the acknowledged father of comparative law, warned against the unpredictability and dangers inherent in transplanting elements of one legal system to another.

157 See Ben Power, "News Won't Compromise, Says Murdoch", *Australian Financial Review*, 29 September 2004, 16.

158 ACSI, Press Release, "News Corporation Settles for Second Best on Governance", 27 September 2004 (available at http://www.acsi.org.au/documents/17092004_Press_Release-News_Corporation.doc).

calls for News Corp to adopt certain Australian corporate governance standards.[159] It appears that US institutions held around 21% of ordinary shares, and 35% of preference shares, in News Corp, and that approximately 20-30% of US institutional investors received advice from ISS.[160] Rupert Murdoch's family interests controlled approximately 30% of News Corp's voting stock.[161] News Corp's public shareholders were in a position to prevent the reorganization by virtue of the fact that Australian law required the schemes of arrangement to be approved by separate class resolutions, with the Murdoch family voting as a separate class.[162]

In October 2004, News Corp resiled from its earlier rejection of the institutional investors' demands[163] and agreed to incorporate some shareholder protection provisions into its Delaware charter.[164] The agreed charter amendments related to five main areas of corporate governance, over which the institutional investors had expressed concern.[165]

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159 See Tim Burt, "News Corp in Talks to Avert Revolt", *Financial Times*, 24 September 2004, 29; Ben Power, "News Faces Crucial Test on US Move", *Australian Financial Review*, 27 September 2004, 17.

160 See Malcolm Maiden, "Dominant US Interests the Key to Rupert's Backflip", *The Age*, 7 October 2004, 1.

161 Martin Peers, "News Corp. Strengthens its Takeover Defenses", *The Wall Street Journal*, 8 November 2004, A2.

162 See *UniSuper Ltd v News Corporation* 2005 WL 3529317 (Del Ch). The re-incorporation proposal required approval of schemes of arrangement by News Corp's ordinary and preference shareholders and option holders, and approval by shareholders of a capital reduction under Australian law. See generally s 411(4) *Corporations Act* 2001 (Cth). Federal Court approval of the transactions, which was also required under Australian law (s 411(4)(b)), was given on 19 November 2004 in *News Corporation Ltd* [2004] FCA 1480. Under this procedure, shareholders and option holders effectively exchanged their shares and options in News Corp for shares and options in News Corp US. See generally The News Corporation Limited, SEC Form 6-K, Press Release, "Australian Federal Court Approves News Corporation Reincorporation to United States", 3 November 2004; Trevor Sykes, "Murdoch Bows out … But He'll Still Visit", *Australian Financial Review*, 27 October 2004, 1.

163 On 1 October 2004, News Corp commenced further negotiations with ACSI. See *UniSuper Ltd v News Corporation* 2005 WL 3529317 (Del Ch).

164 See News Corporation, *Letter to Shareholders and Optionholders*, 7 October 2004 (available at http://www.newscorp.com/investor/download/SupplementIMCorpGov.pdf); Australian Council of Superannuation Investors (ACSI), Press Release, "News Corporation Yields to Investor Concerns", 7 October 2004 (available at http://www.acsi.org.au/documents/Media_Release.07.10.04.doc).

165 See generally *UniSuper Ltd v News Corporation* 2005 WL 3529317 (Del Ch).

First, the Governance Article had included a number of specific investor protection provisions of the Australian Securities Exchange ("ASX") Listing Rules,[166] which institutional investors sought to incorporate into News Corp's Delaware charter.[167] News Corp did not accede to this specific demand. Rather, it agreed to include a provision in the charter stating that News Corp would not request removal of full foreign listing from the ASX without majority shareholder approval.[168] Although, after the re-incorporation, its primary listing was on the New York Stock Exchange,[169] News Corp's concession that it would retain full foreign listing on the ASX[170] ensured that all the ASX listing rules, and corporate governance guidelines, would continue to apply to the company.[171]

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166 At the time of the re-incorporation, these rules were called the Australian Stock Exchange Listing Rules.

167 The institutional investors' Governance Article deemed certain specified "public investor protection and empowerment provisions" under the ASX Listing Rules to be included within it. The ASX Listing Rules specified were Rules 7.1-7.9 (requiring shareholder approval for new share issues exceeding 15% of capital); Rules 10.1-10.18 (requiring shareholder consent for transactions between the corporation and persons in a position of influence); Rules 14.2 (requirements for proxy form); 14.2A (rights of CHESS Depositary Interest holders); 14.3 (requirements regarding nomination of directors); 14.4-14.5 (requirements regarding election and rotation of directors) and 14.11 (voting exclusion statements). See News Corporation Group, *Governance Article for New Delaware Parent Company: Preservation of Australian Public Investor Protection & Empowerment Provisions* (2004, on file with the author), Clause 7, "ASX Listing Rules provisions to apply".

168 Under the charter provision, News Corp cannot request removal of full foreign listing from the ASX without the affirmative vote of a majority of all listed shares in the corporation, rather than simply a majority of shares voted on the resolution. See United States Securities and Exchange Commission, Form 8-K, Amended and Restated Certificate of Incorporation of News Corporation, Inc (November 12, 2004), Article IV, Section 4(a)(iv)(1), "Issuance of Certain Stock; Listing on ASX".

169 News Corp obtained secondary listing on both the ASX and the London Stock Exchange. See United States Securities and Exchange Commission, News Corporation, Form 8-K, Item 2.01, "Acquisition or Disposition of Assets" (12 November 2004).

170 The full foreign listing adopted by News Corp is distinguishable from "foreign exempt listing" under the ASX Listing Rules. Foreign exempt listing requirements are far less onerous than full ASX listing. Companies admitted to ASX foreign exempt listing are required merely to satisfy the ASX that they comply with the listing rules of their home overseas exchange, not with ASX Listing Rules themselves (see ASX Listing Rules 1.11, Condition 3, and 1.11 - 1.15). By way of contrast, the full foreign listing adopted by News Corp prima facie carried an obligation to comply with all ASX Listing Rules.

171 See News Corporation, *Letter to Shareholders and Optionholders*, 7 October 2004 (available at http://www.newscorp.com/investor/download/SupplementIMCorpGov.pdf), "1. No removal of full foreign listing on the ASX without shareholder approval"; Australian Council of

At first blush, this appears to be a major concession. The ASX Listing Rules are very stringent by international standards, and employ shareholder consent as a legitimating device in a wide range of circumstances.[172] In particular, the rules prevent the use of entrenchment mechanisms, such as dual class stock[173] and poison pills,[174] which are permitted in many other jurisdictions. The ASX Listing Rules are given statutory backing under the *Corporations Act* 2001 (Cth) ("*Corporations Act*") and, following a failure to comply, are enforceable in court on the application of the Australian Securities and Investments Commission ("ASIC"), the ASX or "a person aggrieved" by the breach.[175] Where the purpose of a listing rule is to protect shareholders, an individual shareholder may have standing to enforce the rule as a person aggrieved.[176]

Nonetheless, there is a crucial difference between the institutional investors' original demand that News Corp include the substance of specified ASX Listing Rules in its charter, and the concession as finally accepted. This difference relates to the potential for modification of the rules. Although News Corp's agreement to retain full foreign listing on the ASX meant that the company was prima facie required to comply fully with the ASX Listing Rules, this could be undermined if the ASX exercised its power

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Superannuation Investors (ACSI), Press Release, "News Corporation Yields to Investor Concerns", 7 October 2004 (available at http://www.acsi.org.au/documents/Media_Release.07.10.04.doc), 2.

172 Under the ASX Listing Rules, matters which require shareholder approval include:- the issue of more than 15% of equity securities (Rule 7.1); the issue of securities during a takeover bid (Rule 7.9); the disposal of substantial corporate assets to certain associated persons (Rule 10.1); any increase in fees payable to non-executive directors (Rule 10.17); the conferral of termination benefits, if the total value of benefits payable to all officers will exceed 5% of equity in the company (Rule 10.19), and the disposal of the main undertaking of the company (Rule 11.2).

173 See ASX Listing Rule 6.9.

174 See ASX Listing Rule 7.1.

175 See ss 793C(1) and (3), s 1101B and s 1324 *Corporations Act* 2001 (Cth).

176 Robert P. Austin and Ian M. Ramsay, *Ford's Principles of Corporations Law* (13th edition, 2007), para [11.233].

to waive particular rules on behalf of News Corp. This aspect of the concession was to become relevant immediately following News Corp's re-incorporation.[177]

Second, the institutional investors tried to ensure that News Corp would not issue super-voting shares without shareholder approval after the Delaware re-incorporation.[178] Australian public listed corporations are prohibited from issuing shares with enhanced voting power under the ASX Listing Rules, unless the rules are waived by the ASX.[179]

There was a history to the institutional investors' concern in this regard. More than a decade earlier, Rupert Murdoch had announced at News Corp's 1993 annual shareholder meeting a plan to issue super-voting shares.[180] News Corp subsequently asked the Australian Stock Exchange to waive the strict "one share, one vote" principle[181] under the ASX Listing Rules, to enable the company to issue shares with differential voting rights.[182] The proposal was widely condemned in Australia as an entrenchment and anti-takeover device, which would erode general shareholder rights.[183] What began as a discrete waiver request by News Corp broadened into a

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177 As discussed later in the article, in the week during which News Corp's re-incorporation became fully effective, the ASX waived a number of its listing rules on News Corp's behalf.

178 See ACSI, Press Release, "News Corporation Settles for Second Best on Governance", 27 September 2004 (available at http://www.acsi.org.au/documents/17092004_Press_Release-News_Corporation.doc), 2, stating "[t]he fact that the Board can create a further class of shares in the United States without shareholder approval is of considerable concern"; Ben Power, "News Faces Crucial Test on US Move", *Australian Financial Review*, 27 September 2004, 17.

179 See ASX Listing Rule 6.9, which mandates a "one share, one vote" rule in relation to voting on a poll.

180 Sue Lecky, "Murdoch Seeks 'Super' Shares", *Sydney Morning Herald*, 13 October 1993, 27.

181 For discussion of the history and economic theory underlying the "one share, one vote" rule, see generally Guido Ferrarini, "One Share – One Vote: A European Rule?", *ECGI – Law Working Paper No 58/2006* (2006) (available at http://ssrn.com/abstract=875620).

182 News Corp wrote to the ASX seeking approval to make a bonus issue of super-voting shares on a 1-for-10 basis, with each new share carrying 25 votes. See generally Saul Fridman, "The News Corporation Super Shares Proposal: Crime of the Century or Tempest in a Teapot" (1994) 4 *Aust J Corp L* 184, 184-185.

183 The deputy managing director of AMP Society, one of Australia's largest institutional investors, stated at the time, "We believe that the only reason for differential voting rights is to allow control to be entrenched in the hands of the minority, perhaps in perpetuity": Emiliya

general policy debate about the future of the “one share, one vote” rule for Australian listed companies.[184] Institutional investor opposition,[185] governmental intervention[186] and public backlash ultimately led News Corp to abandon the plan to issue super-voting shares,[187] leading some prescient commentators at the time to speculate that News Corp might seek to avoid future difficulties of this kind by delisting in Australia or re-incorporating in a jurisdiction such as Delaware.[188]

In its concessions to the 2004 re-incorporation campaign by institutional investors, News Corp agreed to include a provision in its Delaware charter, prohibiting the issue of any super-voting shares in the absence of approval by the majority of all voting shareholders.[189]

Third, the institutional investors raised the issue of the disparity between shareholder rights under Australian law and Delaware law, particularly in the context of shareholder meetings and voting. They were concerned that the re-incorporation proposal would diminish existing shareholder rights, and their Governance Article addressed this by including an extensive list of shareholder protection provisions from

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Mychasuk, “Industry Says No to News Share Plan”, *Sydney Morning Herald*, 30 November 1993, 33. *Cf* Saul Fridman, *id*.

184 See ASX, *Discussion Paper on Differential Voting Rights* (November 1993), 4-6. See also Ivor Ries, “ASX Opens Up One-vote Debate", *Australian Financial Review*, 11 November 1993, 64, arguing that such a change to Australian law would constitute “perhaps the most dramatic shift in the balance of power in favour of the company management and dominant shareholders and away from minority shareholders in Australian corporate history”.

185 See generally Ivor Ries, “Big Guns Open Fire on Murdoch’s Super Shares”, *Australian Financial Review*, 30 November 1993, 52. In spite of the opposition of Australian institutional investors to News Corp’s super-voting shares proposal, it appeared that US institutional investors were generally supportive of it. See Brian Hale, “US Support for Murdoch Share Plan”, *Australian Financial Review*, 11 November 1993, 23.

186 Tim Dodd and Neil Chenoweth, “Govt Steps into Super Share Row”, *Australian Financial Review*, 24 November 1993, 1.

187 “News Corp. Plan for New Shares Bows to Pressure”, *The Wall Street Journal*, 22 November 1993, A11.

188 See, for example, Ivor Ries, “Super-voter Isn’t Dead Yet”, *Australian Financial Review*, 9 December 1993, 48.

189 See United States Securities and Exchange Commission, Form 8-K, Amended and Restated Certificate of Incorporation of News Corporation, Inc (November 12, 2004), Article IV, Section 4(a)(iv)(2), “Issuance of Certain Stock; Listing on ASX”.

the Australian *Corporations Act*. These provisions related to matters such as the convening of meetings;[190] conduct of shareholder meetings;[191] and removal of directors from office.[192]

Several of the Australian provisions included in the Governance Article are worthy of comment. The Governance Article included, for example, s 249D of the *Corporations Act*, which requires directors to convene a meeting upon requisition by shareholders with 5% of votes or 100 members by number, and s 249F, which permits shareholders with at least 5% of votes to convene a meeting directly. It also contained the recently enacted Australian provision, s 250R of the *Corporations Act*, requiring shareholders of an Australian listed company to pass a non-binding resolution at their annual meeting approving the directors' remuneration report.[193] In the area of

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190 Relevant provisions of the *Corporations Act* relating to the convening of meetings, which appeared in the Governance Article, included:- s 249CA (mandatory rule empowering a single director of a listed company to convene a shareholder meeting); s 249D (provision requiring directors to convene a shareholder meeting on the request of shareholders with at least 5% of votes that may be cast in a general meeting or 100 members); s 249E (liability consequences for directors of failing to comply with a valid shareholder request to convene a shareholder meeting under s 249D); s 249F (power of shareholders with at least 5% of votes that may be cast in a general meeting to convene a shareholder meeting to call and hold a shareholder meeting themselves) and s 249HA (mandatory minimum notice period of 28 days for shareholder meetings of listed public companies).

191 Relevant provisions of the *Corporations Act* relating to the conduct of meetings, which appeared in the Governance Article, included:- s 249N (power of shareholders with at least 5% of votes that may be cast in a general meeting, or 100 members, to propose resolutions at a shareholder meeting); s 249O (obligation on company to give notice of shareholder resolutions); s 249P (power of shareholders with at least 5% of votes, or 100 members by number, to require the company to distribute a statement about shareholders' resolutions to shareholders in certain circumstances); s 250R (requiring a non-binding shareholder vote at the annual general meeting on the directors' remuneration report); s 250RA (requiring the auditor of a listed corporation to attend the company's annual general meeting); s 250SA (requiring reasonable opportunity for shareholder discussion of the remuneration report at the annual shareholder meeting); s 250T (requiring reasonable opportunity for shareholders to ask relevant questions of the auditor, if present, at the annual shareholder meeting); s 251AA (requiring listed companies to disclose proxy votes).

192 Section 203D *Corporations Act* (mandatory power of public company shareholders to remove a director from office by ordinary resolution). The Governance Article included various other shareholder protection provisions, such as ss 207-230 (general requirement of shareholder consent for related party transactions).

193 See generally Jennifer Hill, "Regulating Executive Remuneration: International Developments in the Post-Scandal Era" (2006) 3 *European Company Law* 64, 69-72; Larelle Chapple and Blake Christensen, "The Non-Binding Vote on Executive Pay: A Review of the CLERP 9 Reform" (2005) 18 *Aust J Corp L* 263; Kym Sheehan, "Is the Outrage Constraint an Effective Constraint on Executive Remuneration? Evidence from the UK and Preliminary Results from Australia" (March 2007) (available at http://ssrn.com/abstract=974965).

removal of directors from office, the Governance Article advocated inclusion of s 203D of the *Corporations Act*, granting shareholders of public companies an absolute right to remove directors from office, with or without cause, by majority vote.

News Corp made only one concession in this regard. The company agreed to include a provision in its Delaware charter permitting shareholders with 20% or more of Class B common stock to request a special stockholder meeting.[194] While this charter provision was more generous to shareholders than Delaware law (under which they have no prima facie right to convene a special shareholder meeting),[195] it contained significant qualifications,[196] and was far less generous than the Australian approach, which permits shareholders with 5% of votes, or 100 members by number, to requisition a special shareholder meeting.[197]

Fourth, the institutional investors' Governance Article addressed takeovers. Significant differences exist between the US and other common law countries, including Australia, with respect to the balance of power between shareholders and

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194 See United States Securities and Exchange Commission, Form 8-K, Amended and Restated Certificate of Incorporation of News Corporation, Inc (November 12, 2004), Article VI. Perhaps surprisingly, the charter did not include a supermajority provision defending the shareholder rights contained in this provision. I am grateful to Justice Randy Holland for raising this point with me.

195 Under Del. Code Ann, tit 8, s 211(2)(d), a special meeting of the stockholders may only be convened by the board or by a person so authorized in the certificate of incorporation or by the bylaws. *Cf* MBCA s 7.02(a)(2), which prima facie permits members holding at least 10% of votes to convene a special meeting of stockholders. The articles of incorporation may fix a lower or higher percentage, though not exceeding 25%.

196 News Corp's Delaware charter states, for example, that no special meeting of stockholders can be called if written notice by the stockholders is received less than 135 days prior to the first anniversary of the date of the preceding annual meeting of stockholders: see United States Securities and Exchange Commission, Form 8-K, Amended and Restated Certificate of Incorporation of News Corporation, Inc (November 12, 2004), Article VI. The clause also provides that the directors must convene a special shareholders' meeting not later than 100 days after receipt of the stockholders' written request, compared to a 21 day deadline for directors under Australian law: see s 249D(5) *Corporations Act* 2001 (Cth). If the directors fail to convene a meeting within 21 days, a specified proportion of the requisitioning shareholders may convene the meeting themselves and the company may recover meeting expenses from the directors personally (ss 249E(1), 249E(5)) *Corporations Act*.

197 See sections 249D and 249F *Corporations Act* 2001 (Cth).

directors in takeovers.[198] US federal law regulates "tender offers"[199] rather than the concept of "changes of control", which forms the regulatory fulcrum in jurisdictions such as the UK and Australia.[200] Under US law, assessment of directors' defensive conduct in takeovers is the province of state law and the courts. Delaware law, in spite of the potential for intense scrutiny of directors' defensive tactics following the *Unocal* decision,[201] continues to accord great deference to board decisions under a paradigm in which the board occupies a "gatekeeper" role.[202] Views differ on whether this gatekeeper paradigm in fact promotes shareholder interests.[203] Nonetheless, the assumption that board access to defensive tactics is a vital antidote to coercive bids continues to have strong traction in US corporate law scholarship.[204]

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198 See also John C. Coffee, "The Rise of Dispersed Ownership: The Roles of Law and the State in the Separation of Ownership and Control" (2001) 111 *Yale LJ* 1, 18, noting the existence of different regulatory approaches to takeovers within common law jurisdictions.

199 See, for example, ss 14(d) and 14(e) of the *Williams Act*, which was enacted in 1968 and amended in 1970. See generally Jesse H. Choper, John C. Coffee and Ronald J. Gilson, *Cases and Materials on Corporations* (6th ed, 2004), 1114*ff*.

200 Richard Hall, "The Endesa Takeover Battle and its Implications for U.S. Regulation of Cross-Border M&A Transactions", Ross Parsons Centre of Commercial, Corporate and Takeover Law Seminar, University of Sydney Law School (3 October 2007).

201 *Unocal Corp v Mesa Petroleum Corp*, 493 A 2d 946 (Del 1985).

202 It has been stated that the board acts, not just a gatekeeper, but rather as "the defender of the metaphorical medieval corporate bastion and the protector of the corporation's shareholders". See Stephen M. Bainbridge, "Unocal at 20: Director Primacy in Corporate Takeovers" (2006) 31 *Del J Corp L* 769, 772 (citing *Unitrin, Inc. v Am Gen Corp* 651 A 2d 1361, 1387-1388 (Del 1995)). See generally Robert B. Thompson, "Takeover Regulation after the 'Convergence' of Corporate Law" (2002) 24 *Syd L Rev* 323.

203 See, for example, Paul Davies and Klaus J. Hopt, "Control Transactions", in Reinier Kraakman, Paul Davies, Henry Hansmann, Gérard Hertig, Klaus J. Hopt, Hideki Kanda and Edward B. Rock (eds), *The Anatomy of Corporate Law: A Comparative and Functional Approach* (2004), 157, 172, arguing that it is difficult to justify the Delaware takeover law model as an efficient regulatory regime for agency problems in the takeover context. *Cf* Bainbridge, *ibid*, arguing that insulation of board authority is a critical factor in promoting efficient corporate decision-making for the benefit of shareholders.

204 See, for example, Chancellor Leo E. Strine, "Toward Common Sense and Common Ground? Reflections on the Shared Interests of Managers and Labor in a More Rational System of Corporate Governance" (2007) *J Corp L* (forthcoming, available at http://ssrn.com/abstract=989624), who states that it would be "crazy from an investor's perspective for a target board not to have a traditional pill in place to stimulate a value-enhancing auction and to deter structurally coercive bids" (at 22).

In the UK, takeover disputes are resolved not by the courts, but by a specialized non-judicial body, the Panel on Takeovers and Mergers ("the UK Panel"),[205] which is responsible for administering the City Code on Takeovers and Mergers ("the City Code"). The operation of the UK Panel reflects a self-regulatory approach to takeovers, and has served as the blue-print for reform in numerous jurisdictions, including Australia, Hong Kong, Ireland and South Africa.[206] The UK approach has, at least to date, been characterized by an extremely low incidence of tactical litigation compared to the US.[207] Some of the contours of UK takeover regulation were altered recently to implement the Directive on Takeover Bids ("the Directive") under EC law.[208]

In contrast to Delaware's deference to board discretion, the City Code seriously restricts the ability of the board to engage in defensive tactics and implement entrenching mechanisms. It elevates shareholder decision-making power during a takeover,[209] an approach which also underpins recent EC developments in takeover law.[210] A central feature of the City Code is the "frustrating action" principle, which

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205 The UK Panel was established in 1968, the same year that the *Williams Act* was passed in the US. Membership of the UK Panel is drawn from major financial and business institutions. See "Membership of the Panel" (available at http://www.thetakeoverpanel.org.uk/new/).

206 See Emma Armson, "Models for Takeover Dispute Resolution: Australia and the UK" (2005) 5 *Journal of Corporate Law Studies* 401, 402.

207 Tunde I. Ogowewo, "Tactical Litigation in Takeover Contests" [2007] *J Bus L* 589, 608-611.

208 Directive on Takeover Bids (2004/25/EC). Thus, for example, the UK Panel has been designated as the supervisory authority for the purposes of the Directive. Whereas previously takeover regulation in the UK had no direct statutory force, the introduction of Part 28 of the UK *Companies Act* 2006, which implements the Directive on Takeover Bids, now provides a statutory basis for takeover regulation in the UK for the first time. See generally Tunde I. Ogowewo, *id*, 590-592. The UK Government expressed concern that the new legal framework created by the Takeovers Directive might potentially increase the level of tactical litigation in the UK: see UK Department of Trade and Industry, *Company Law Implementation of the European Directive on Takeover Bids: A Consultative Document* (January 2005, available at http://www.berr.gov.uk/files/file10384.pdf), para [2.33].

209 See Paul Davies and Klaus J. Hopt, "Control Transactions", in Reinier Kraakman, Paul Davies, Henry Hansmann, Gérard Hertig, Klaus J. Hopt, Hideki Kanda and Edward B. Rock (eds), *The Anatomy of Corporate Law: A Comparative and Functional Approach* (2004), 157, at 164*ff*.

210 UK Department of Trade and Industry, *Implementation of the EU Directive on Takeover Bids: Guidance on Changes to the Rules on Company Takeovers* (April 2006, revised February 2007, available at http://www.berr.gov.uk/files/file37429.pdf), 4; Davies and Hopt,

prohibits directors, in the absence of shareholder approval, from taking any action that may result in frustration of a bona fide offer or in the shareholders being denied the opportunity to decide an offer on its merits.[211] It has been argued that differences in the prevailing paradigms in the UK and US context are attributable to the stronger influence of institutional investors under the UK self-regulatory regime than in the US, where the balance of power is firmly tilted towards management.[212]

Australia's takeover laws also diverge from the Delaware approach, and have been described as "unique" and "widely regarded as some of the most restrictive among capitalist economies".[213] They are explicitly based on a policy of equality of opportunity and protection of minority shareholders, embodied in the so-called "Eggleston principles".[214] The basic rule under Australian takeover law, which has a historical focus on fairness rather than economic efficiency,[215] is that a bidder cannot acquire control of a parcel of 20% or more of voting shares, except pursuant to a general offer to all shareholders (the "20% threshold rule").[216] Private control transactions are thus precluded. By requiring that an offer be made to all shareholders before a bidder is permitted to pass the control threshold, Australian takeover law ensures that any control premium is shared equally between majority and minority

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id, 164; Peer Zumbansen, "European Corporate Law and National Divergences: The Case of Takeover Regulation" (2004) 3 *Wash U Global Stud L Rev* 867.

211 Rule 21, *City Code on Takeovers and Mergers* (UK). Examples of frustrating actions are set out in Rule 21 and include matters such as:- issuing new shares; granting options over unissued shares; creating securities that carry rights of conversion into shares; selling or acquiring assets of a material amount, and entering into contracts otherwise than in the ordinary course of business.

212 See John Armour and David A. Skeel, "Who Writes the Rules for Hostile Takeovers, and Why? The Peculiar Divergence of U.S. and U.K. Takeover Regulation" (2007) 95 *Geo LJ* 1727.

213 Justin Mannolini, "Convergence or Divergence: Is There a Role for the Eggleston Principles in a Global M&A Environment?" (2002) 24 *Syd L Rev* 336.

214 The Eggleston Principles are embedded in s 602 *Corporations Act* 2001 (Cth), which outlines the purposes of the Chapter in the Act that governs takeovers. The provision includes a purpose that "as far as practicable" the holders of voting shares "all have a reasonable and equal opportunity to participate in any benefits" accruing from the acquisition of a substantial interest: see s 602(c). See also Mannolini, *id*, 337-338.

215 Mannolini, *ibid*.

216 See ss 606(1) and 611 *Corporations Act* 2001 (Cth).

shareholders. This rule is particularly strict by international standards, including UK law, which permits private control transactions[217] provided that a general offer or "mandatory bid" is then made to all shareholders.[218]

Australian law moved closer to UK law in 2000, when responsibility for the resolution of takeover disputes shifted from the courts to the Australian Takeovers Panel.[219] Although Australian courts traditionally adopted a fiduciary duty analysis to assess directors' defensive conduct, after 2000 the Australian Takeovers Panel diverged sharply from this approach, by implementing its own frustrating action policy.[220] This frustrating action policy focused on the effect, rather than the purpose, of directors' conduct in response to a takeover,[221] and limited permissible action by the board in the absence of shareholder consent.[222] It constituted a major shift in the balance of power between the board and shareholders during a bid under Australian law.[223]

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217 Under Rule 9.1 of the *City Code on Takeovers and Mergers* (UK), the relevant control threshold is 30% of voting shares.

218 Justin Mannolini, "Convergence or Divergence: Is There a Role for the Eggleston Principles in a Global M&A Environment?" (2002) 24 *Syd L Rev* 336, 357-8.

219 *Corporations Act* 2001 (Cth), Part 6.10, Division 2 – "The Takeovers Panel". The policy basis for this change was the perception that there was widespread use of tactical litigation in the Australian context. See Tunde I. Ogowewo, "Tactical Litigation in Takeover Contests" [2007] *J Bus L* 589, 602-603. Note that the Australian Takeovers Panel has recently been the subject of a High Court constitutional challenge. See generally Emma Armson, "*Attorney-General (Commonwealth) v Alinta Limited*: Will the Takeovers Panel Survive Constitutional Challenge?" (2007) 29 *Syd L Rev* 495. The High Court upheld the constitutional validity of the Takeovers Panel's powers in a judgment delivered on 13 December 2007. See Takeovers Panel, *Attorney-General (Commonwealth) v Alinta Ltd*: *High Court Appeal Allowed*, TP07/105 (13 December 2007).

220 The frustrating action policy arises from the reasonable and equal opportunity principle under s 602(c) *Corporations Act*. See generally Takeovers Panel, *Guidance Note 12: Frustrating Action* (16 June 2003, available at http://www.takeovers.gov.au/content/120/download/GN12.pdf); Emma Armson, "The Frustrating Action Policy: Shifting Power in the Takeover Context" (2003) 21 *C&SLJ* 487.

221 See Jennifer Hill, "Back to the Future? Bigshop 2 and Defensive Tactics in Takeovers" (2002) 20 *C&SLJ* 126, 129-130.

222 See Robert B. Thompson, "Takeover Regulation after the 'Convergence' of Corporate Law" (2002) 24 *Syd L Rev* 323, 324; Jennifer Hill, "Back to the Future?: Bigshop 2 and Defensive Tactics in Takeovers" (2002) 20 *C&SLJ* 126; Jennifer Hill and Jeremy Kriewaldt, "Theory and Practice in Takeover Law – Further Reflections on Pinnacle No 8" (2001) 19 *C&SLJ* 391.

223 According to the Australian Takeovers Panel, "[a]lthough it is generally the responsibility of a company's directors to make company decisions, decisions about control and ownership of the

There has been increasing recognition of the extent of variation in international takeover regulation. Academic commentators have explored possible reasons for the "peculiar divergence" between US and UK takeover rules.[224] A US court, in the recent decision *E.On AG v Acciona, SA and Finanzas Dos, SA*,[225] concerning a 47 billion euro hostile takeover in Madrid, acknowledged this diversity and warned of the need for caution in applying US takeover principles in cross-border acquisitions, where the acquirer may be acting in compliance with the laws of the home jurisdiction.[226] Takeovers also constituted an important theme in the Paulson Committee report. The committee compared the "pro-shareholder" approach of the UK regulatory regime with the "pro-management" approach of the Delaware courts, and recommended certain reforms to the US system to shift more power to shareholders.[227]

The institutional investors' Governance Article addressed the takeover issue by advocating that News Corp's Delaware charter should include the 20% threshold rule found in Australian takeover law, to ensure that any control premium would be shared between all stockholders. Furthermore, the Governance Article tackled the issue of defensive conduct by the board of directors. Clause 8.1 of the Governance Article contained a general limitation on the board's power in relation to corporate control transactions.[228] It also included a provision expressly stating that that "the Board shall

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company are properly made by its shareholders." Takeovers Panel, *Guidance Note 12: Frustrating Action* (16 June 2003, available at http://www.takeovers.gov.au/content/120/download/GN12.pdf), 1.

224 See generally John Armour and David A. Skeel, "Who Writes the Rules for Hostile Takeovers, and Why? The Peculiar Divergence of U.S. and U.K. Takeover Regulation" (2007) 95 *Geo LJ* 1727.

225 *E.On AG v Acciona, SA and Finanzas Dos, SA* 2007 WL316874 (SDNY).

226 *Id*, *12.

227 Committee on Capital Markets Regulation, *Interim Report of the Committee on Capital Markets Regulation* (30 November 2006, revised version released 5 December 2006), 93-105.

228 Clause 8.1 of the Governance Article stated that "[t]he Board shall not have power to, and shall not, restrict, limit or hinder in any way the opportunity and capacity of shareholders to decide whether or not control of the Company should pass under any takeover bid which may be made in compliance with Delaware law and New York Stock Exchange listing requirements. For the avoidance of doubt, this provision applies throughout the life of the

not have power to, and shall not, create or implement any device, matter or thing the purpose, nature or effect of which is commonly described as a 'poison pill'".[229]

News Corp made certain concessions in the takeover context. It was agreed, for example, that the Murdoch interests would be subject to restrictions analogous to the Australian 20% threshold rule under a series of voting agreements.[230] Subject to specified "permitted transfers", the Murdoch interests were prohibited from acquiring more than an additional 3% of News Corp's outstanding shares every six months.[231] News Corp also accepted a restriction on the board's power to issue poison pills. However, this restriction was contained not in the charter, as the institutional investors had requested, but rather in a board policy. The ostensible reason for this was logistical constraints.[232] News Corp issued a press release and letter to shareholders announcing that the board of the new Delaware corporation had "established a policy that if any stockholder rights plan (known as a "poison pill") is adopted without stockholder approval, it will expire after one year unless it is ratified by stockholders".[233]

Company and whether or not any takeover bid is anticipated or current". News Corporation Group, *Governance Article for New Delaware Parent Company: Preservation of Australian Public Investor Protection & Empowerment Provisions* (2004, on file with the author), Clause 8, "Presumptions of Delaware/US law and practice not to apply".

229 *Ibid*.

230 See "Summary of Agreement Between News Corp US and the Murdoch Interests", News Corporation, *Letter to Shareholders and Optionholders*, 7 October 2004 (available at http://www.newscorp.com/investor/download/SupplementIMCorpGov.pdf), para (b). See also, "4. Restrictions on the rights of the Murdoch interests to acquire further shares, and to transfer existing shares, in News Corp US", *id*.

231 "Summary of Agreement Between News Corp US and the Murdoch Interests", *id*, para (a).

232 During negotiations, News Corp's General Counsel, Ian Phillip, told the President of ACSI, Michael O'Sullivan, that it would not be possible, in the limited time available before the shareholder vote on the corporate reconstruction, to draft and finalize an appropriate charter restriction on poison pills. See *UniSuper Ltd v News Corporation* 2005 WL 3529317, *2 (Del Ch).

233 News Corporation, *Letter to Shareholders and Optionholders*, 7 October 2004 (available at http://www.newscorp.com/investor/download/SupplementIMCorpGov.pdf), "5. Board policy on stockholder rights plans". See also News Corporation, Press Release, *News Corporation Adopts Additional Corporate Governance Provisions*, 6 October 2004 (available at http://sec.edgar-online.com/2004/10/07/0001193125-04-168358/Section3.asp), 2.

Finally, the institutional investors' Governance Article included a number of principles of best practice derived from Australian and international corporate governance.[234] News Corp did not agree to include these provisions in its Delaware charter. It did, however, agree to establish board committees "to consider" certain corporate governance issues prior to the company's first annual meeting under Delaware law. These issues included standards of independence for board members, disclosure of the company's process for determining leadership succession, procedures for assessing reasonable shareholder proposals and elimination of the company's staggered board structure.[235]

The adoption of these various concessions effectively quelled the corporate governance revolt by institutional investors,[236] and at News Corp's general meeting in Adelaide in October 2004,[237] shareholders overwhelmingly approved the re-incorporation proposal, with over 90% of votes cast in its favor.[238]

Although News Corp's concessions were far more limited than the institutional investors' original demands in the Governance Article,[239] the compromise was

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234 News Corporation Group, *Governance Article for New Delaware Parent Company: Preservation of Australian Public Investor Protection & Empowerment Provisions* (2004, on file with the author), Clause 9, "Other Best Practice provisions to apply".

235 See News Corporation, *Letter to Shareholders and Optionholders*, 7 October 2004 (available at http://www.newscorp.com/investor/download/SupplementIMCorpGov.pdf), "6. Corporate governance committees"; News Corporation, Press Release, *News Corporation Adopts Additional Corporate Governance Provisions*, 6 October 2004 (available at http://sec.edgar-online.com/2004/10/07/0001193125-04-168358/Section3.asp).

236 See John Durie, "Murdoch Peace Deal to Gain Support for US Move", *Australian Financial Review*, 6 October 2004, 1.

237 See News Corporation, Press Release, "Australian Federal Court Approves Shareholder Meetings to Vote on Proposed Reincorporation", New York, 15 September 2004 (available at http://www.newscorp.com/news/news_216.html).

238 Votes cast in favor of the schemes of arrangement at the various class meetings of News Corp were as follows:-

Ordinary shareholders:	91.28% in favor; 8.72% against;
Preferred shareholders:	96.23% in favor; 3.77% against;
Option holders:	99.95% in favor; 0.05% against.

The schemes of arrangement were unanimously approved at the separate class meetings of the Murdoch interests. See *News Corporation Ltd* [2004] FCA 1480, para [3].

239 News Corporation Group, *Governance Article for New Delaware Parent Company: Preservation of Australian Public Investor Protection & Empowerment Provisions* (2004, on file with the author). See also Malcolm Maiden, "Dominant US Interests the Key to Rupert's

generally portrayed in the Australian financial press as a significant victory for the institutional investors.[240] One commentator, for example, described the News Corp concessions as heralding "a major step forward" for shareholder democracy;[241] others however, viewed them as insignificant and a mirage.[242]

4. News Corp's Poison Pill

4.1 Adoption of the Pill - Comparative Law Perspectives

> "I think he's the most brilliant financial mind I know … I should think we are all responding to John Malone, dancing to his tune. I still do sometimes".
>
> Rupert Murdoch[243]

> "Rupert is a great guy but I never found him of compelling generosity".
>
> John Malone[244]

> "[Murdoch is] a shark, always dangerous, always on the move. By contrast, Malone is a swamp alligator, content to lie secreted in the mud, to let the prey come to him".

Backflip", *The Age*, 7 October 2004, 1, stating that the agreed changes were "at the top of a much more extensive list" sought by ACSI and CGI.

240 See, for example, Stephen Bartholomeusz, "News Corp Capitulation a Victory for Shareholders", *The Age*, 7 October 2004, 1.

241 Elizabeth Knight, "Murdoch Gymnastics Good for Investors", *Sydney Morning Herald*, 8 October 2004, 25.

242 See Ben Power, "News Rejects Murdoch Loophole Claim", *Australian Financial Review*, 19 October 2004, 15; Wendy Frew, "News Charter has Self-destruct Clause", *Sydney Morning Herald*, 19 October 2004, 22. See also Christian Catalano, "News Finally Goes, and with a Big Tick", *The Age*, 27 October 2004, 3, claiming that even after revisions to the corporate governance charter, investors were still concerned about takeover protection retained by Murdoch interests.

243 Cited in Neil Chenoweth, "Malone's Ambitious Plan to Sneak up on Murdoch", *Australian Financial Review*, 18 October 2005, 1.

244 Cited in Christian Catalano, "Murdoch Looks Set to Do a Deal with Malone", *Sydney Morning Herald*, 20 April 2005, 22.

David Elstein[245]

On 8 November 2004, in the same week that the re-incorporation became fully effective, one problematical aspect of the domicile change[246] emerged as a reality. News Corp issued a press release announcing that its board of directors had adopted a poison pill.[247] The poison pill was in the form of a stockholder rights plan,[248] granting each shareholder a dividend distribution of one right for each voting and non-voting common stock held. These inchoate rights would crystallize, and become exercisable, if an acquirer obtained 15% or more of News Corp's voting common stock. When triggered, the rights would entitle their holder (with the exception of the acquirer) to purchase News Corp's voting and non-voting common stock at half price, and, in the event of a merger or acquisition of News Corp, to buy shares in the acquiring company at half price.[249]

The press release expressly referred to News Corp's recently adopted board policy that any poison pill would expire after one year unless approved by shareholders.

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245 Quoted in David Usborne, "John Malone: The Man Who Shook up Murdoch", *The Independent* (London), 13 November 2004, 44.

246 See Grant Samuel & Associates, Independent Expert's Report, *Re-incorporation of The News Corporation Ltd in the United States and Acquisition of Queensland Press Pty Ltd*, 14 September 2004, E-11.

247 News Corp, Press Release, *News Corporation Announces Stockholder Rights Plan*, 8 November 2004 (available at http://www.asx.com.au/asxpdf/20041108/pdf/3nlcbk2lxx2rz.pdf). The decision was originally made by the board of directors as constituted prior to News Corp's re-incorporation. On 23 November 2004, the reconstituted board approved the earlier decision to implement a poison pill. See United States Securities and Exchange Commission, News Corporation, Form 8-K, Item 3.03, "Material Modification to Rights of Security Holders" (available at http://www.secinfo.com/d14D5a.166n6.htm0). See also Martin Peers, "News Corp. Strengthens its Takeover Defenses", *The Wall Street Journal*, 8 November 2004, A2.

248 News Corp's stockholder rights plan is set out in News Corporation, SEC Form 6-K Filing, Exhibit B, News Corporation, Inc and Computershare Investor Services, LLC (as Rights Agent), "Rights Agreement", 8 November 2004 (available at http://www.secinfo.com/dsVsj.12Gu.htm).

249 News Corp, Press Release, *News Corporation Announces Stockholder Rights Plan*, 8 November 2004 (available at http://www.asx.com.au/asxpdf/20041108/pdf/3nlcbk2lxx2rz.pdf), 1. See John Armour and David A. Skeel, "Who Writes the Rules for Hostile Takeovers, and Why? The Peculiar Divergence of U.S. and U.K. Takeover Regulation" (2007) 95 *Geo LJ* 1727, 1734, describing the technical operation of poison pills.

However, references to this policy were nebulous and suggested a cetain malleability. According to the press release:-

> [T]he Rights Plan currently provides that the rights will expire in one year. At or prior to such one year anniversary, the Board of Directors will take such action as it deems appropriate in the light of facts and circumstances existing at such time, including, if appropriate, implementing such policy (whether by seeking stockholder ratification or by allowing the rights to expire).[250]

The press release also revealed that the poison pill was a direct response to the actions of Liberty Media Corp ("Liberty Media"),[251] the investment vehicle of cable TV magnate John Malone, with whom Murdoch had a longstanding involvement.[252] Five days before the pill's adoption, Liberty Media disclosed that it had entered into a $1.48 billion equity swap[253] for News Corp shares with Merrill Lynch & Co.[254] There have been several recent controversial transactions in Australia, where cash-settled equity swaps were used strategically in a takeover context,[255] and there is growing

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250 News Corp, Press Release, *id*, 2.

251 *Ibid*, 1. News Corp's press release noted that this action was taken by Liberty Media "without any discussion with, or prior notice to, News Corporation". *Ibid*.

252 This involvement included Malone's participation in a News Corp capital raising in the early 1990s, which rescued New Corp from near bankruptcy at the time. At one stage, Murdoch and Malone had also apparently contemplated appointing Malone to the board of News Corp. See generally Martin Peers, "Mogul vs. Mogul: Stock Gambit Strains Relations Between Two Media Titans", *The Wall Street Journal*, 3 March 2005, A1; Neil Chenoweth, "Malone's Ambitious Plan to Sneak up on Murdoch", *Australian Financial Review*, 18 October 2005, 1.

253 For a description of a cash-settled equity swap, see *Glencore International AG v Takeovers Panel* (2005) 220 ALR 495, 498 (Emmett J).

254 The equity swap for 84.7 million class B News Corp shares was scheduled for completion by April 2005. See Tim Burt, "News Corp Channels Energies into Pay-TV", *Financial Times*, 4 November 2004, 20; "Liberty Media Buys Another Chunk of News Corp", *Denver Business Journal*, 4 November 2004, 3 (cited in Louise McCoach, *The Glencore Decision: A Case for Reform?* (2005, unpublished manuscript, on file with author)).

255 Cash-settled equity swaps were used to obtain a pre-bid acquisition stake or a blocking position in control transactions, such as the 2005 takeover by BHP Billiton of WMC Resources Ltd (see Bryan Frith, "BHP King Hit Knocks Rivals out of the Ring", *The Australian*, 9 March 2005, 36). However, the most prominent example was the use of equity swaps by Glencore International AG ("Glencore") to obtain a blocking position during a 2005 takeover bid by Centennial Coal Co Ltd for Austral Coal Ltd. See, generally, *Glencore International AG v Takeovers Panel* (2005) 220 ALR 495; Emma Armson, "The Australian Takeovers Panel and Judicial Review of its Decisions" (2005) 26 *Adelaide L Rev* 327. Glencore's equity swap provided a good illustration of the contemporary phenomenon of hidden or "morphable" ownership, and the associated regulatory challenges of such

concern in the US about the regulatory implications of equity swaps.[256] In this instance, the equity swap transaction permitted Liberty Media to raise its voting stake in News Corp from approximately 9% to 17%, only 13 percentage points below the Murdoch family's voting interests.[257]

Liberty Media's equity swap transaction was an opportunistic one, taking advantage of instability in News Corp shares during the domicile change.[258] This instability was due to the fact that many index funds in Australia and Asia were required to sell News Corp shares, in anticipation of its removal from Australian stock indices.[259] Analysts considered that, but for the presence of a poison pill, Liberty Media could have raised its voting stake to 49% of News Corp shares, by swapping its 421.6 million non-voting Class A ordinary shares[260] for Class B voting stock.[261] In contrast, Mr

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ownership. See Henry T. Hu and Bernard Black, "The New Vote Buying: Empty Voting and Hidden (Morphable) Ownership" (2006) 79 *S Cal L Rev* 811, 839*ff*, discussing the attempted use of hidden ownership through equity swaps in the Glencore matter to avoid disclosure under Australia's takeover rules.

256 See Andrew Ross Sorkin, "A Loophole Lets a Foot in the Door", *New York Times*, 15 January 2008, 1.

257 See Martin Peers, "News Corp.'s Net Increases by 27% on TV Strength – Liberty Media Gains Right to Boost its Voting Stake in Murdoch-led Concern", *The Wall Street Journal*, 4 November 2004, B3; Tim Burt, "Liberty Share Deal Unsettles News Corp: Murdoch Issues Poison Pill as John Malone's Media Group Lifts Stake", *Financial Times*, 9 November 2004, 30.

258 See Christian Catalano, "Murdoch Looks Set to Do a Deal with Malone", *Sydney Morning Herald*, 20 April 2005, 22. Speculation existed on Wall Street that the equity swap constituted a negotiating strategy to put pressure on News Corp to purchase certain Liberty Media assets. See Martin Peers, "Malone Gets a Step on Murdoch", *The Wall Street Journal*, 9 November 2004, C1.

259 See Martin Peers, "Mogul vs. Mogul: Stock Gambit Strains Relations Between Two Media Titans", *The Wall Street Journal*, 3 March 2005, A1; The Lex Column, "News Corp", *Financial Times*, 9 November 2004, 20; Jane Schulze, "News Up as it Awaits Move on Index Shift", *The Australian*, 28 October 2004, 34.

260 Liberty Media owned approximately 17% of News Corp's non-voting shares. This non-voting stake had been accumulated through deals with News Corp itself and was worth approximately $6 billion. By late 2003, Liberty Media was the largest shareholder in News Corp on a global basis, including voting and non-voting stock. See Sam Matthews, "Liberty Looks to Double Voting Stake in News Corporation", *Brand Republic*, 8 November 2004, 1; Martin Peers, "Mogul vs. Mogul: Stock Gambit Strains Relations Between Two Media Titans", *The Wall Street Journal*, 3 March 2005, A1.

261 Tim Burt, "News Corp Unveils Poison Pill Defence Strategy: Murdoch's Board Acts to Ward off Any Liberty Media Bid after Malone Raises Voting Interest", *Financial Times*, 9 November 2004, 21; Lex Column, "News Corp", *Financial Times*, 9 November 2004, 20.

Murdoch was constrained in his ability to purchase any News Corp shares which came onto the market during this period, as a result of the concessions extracted by the institutional investors to the effect that the Murdoch family could not acquire more than an additional 3 percent of News Corp's outstanding shares every six months.[262]

News Corp's poison pill specifically exempted existing shareholdings above the 15% threshold (such as the Murdoch interests), and previously disclosed contracts to purchase stock (such as Liberty Media's equity swap arrangement).[263] Further acquisitions of more than 1% by any party could, however, trigger the pill.[264] The pill therefore ensured that Liberty Media could not raise its voting stake in News Corp beyond 18%, without experiencing massive dilution.[265]

Although Chancellor Chandler has suggested that Liberty Media "suddenly appeared" as a hostile acquirer,[266] it in fact seems that Liberty's acquisition strategy commenced much earlier. It is now known that Liberty Media lodged an application with the Australian Foreign Investment Review Board ("FIRB") in 2002. This information only became publicly known due to a 2005 Administrative Appeals Tribunal ("AAT") decision, *Re Mangan v The Treasury*.[267] The AAT decision concerned a Freedom of Information application[268] which had been made by a Deutsche Bank analyst, Michael

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262 See "Summary of Agreement Between News Corp US and the Murdoch Interests", News Corporation, *Letter to Shareholders and Optionholders*, 7 October 2004 (available at http://www.newscorp.com/investor/download/SupplementIMCorpGov.pdf), para (a); Martin Peers, "Mogul vs. Mogul: Stock Gambit Strains Relations Between Two Media Titans", *The Wall Street Journal*, 3 March 2005, A1.

263 See News Corp, Press Release, *News Corporation Announces Stockholder Rights Plan*, 8 November 2004 (available at http://www.asx.com.au/asxpdf/20041108/pdf/3nlcbk2lxx2rz.pdf), 1.

264 *Ibid*.

265 See Martin Peers, "Malone Gets a Step on Murdoch", *The Wall Street Journal*, 9 November 2004, C1.

266 *UniSuper Ltd v News Corporation* 2005 WL 3529317, *3 (Del Ch).

267 [2005] AATA 898 (15 September 2005).

268 The application was made under the *Freedom of Information Act* 1982 (Cth).

Mangan,[269] to the Australian Treasury, for release of information about whether Liberty Media had lodged a FIRB application seeking clarification of any ownership restrictions on News Corp.[270] Treasury denied Mr Mangan access to certain documents falling within the scope of his Freedom of Information application, on the basis that their release would adversely affect Liberty Media's "lawful business, commercial and financial affairs".[271] In review proceedings, the AAT upheld Treasury's decision, refusing disclosure of the documents on a variety of grounds, including that disclosure would reveal Liberty Media's "strategy for maintaining and increasing its interest" in News Corp, and would disadvantage Liberty Media vis-à-vis its competitors in any acquisition of News Corp shares.[272] The AAT also rejected the applicant's argument that disclosure was now justified, since News Corp's adoption of a poison pill had effectively destroyed the commercial value of the relevant documents.[273]

Liberty Media's 2002 FIRB application is interesting, since it suggests the possibility that Liberty may have contemplated a full takeover bid for News Corp under Australian law at least two years before its controversial equity swap transaction,[274] and provides some support for the theory that the main motivation behind News

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269 Michael Mangan reappeared in the News Corp tableau in 2005. A respected Australian media analyst, who had covered News Corp for 15 years, Mangan claimed that he was retrenched by Deutsche Bank after he downgraded News Corp stock to a "sell" recommendation in early 2005. Mangan was openly skeptical about the effect of the Delaware re-incorporation on News Corp shareholder value. See Michael Mangan, "Hardball, Murdoch Style", *Eureka Report*, 14 October 2005; Lisa Murray, "Analyst Says News Threatened Brokers", *Sydney Morning Herald*, 15 October 2005, 47. Rupert Murdoch later publicly denied any attempt by News Corp to put pressure on Deutsche Bank because of Mangan's sell recommendation. See Mark Coultan, "Don't Blame Us, Says Murdoch – Share Price Will Rise, Eventually", *Sydney Morning Herald*, 24 October 2005, 19.

270 *Re Mangan v The Treasury* [2005] AATA 898, paras [1], [3], [4].

271 *Id*, paras [2], [7], [9]. The relevant provisions on exemptions from disclosure are ss 43 and 45, *Freedom of Information Act* 1982 (Cth).

272 *Id*, para [29]. From a policy perspective, the AAT also considered that an order requiring disclosure would seriously limit the information that Liberty Media would be willing to provide voluntarily to FIRB in any future applications: *id*, paras [30], [44]-[47].

273 *Id*, paras [32]-[33], [38]-[39].

274 See Neil Chenoweth, "Malone's Ambitious Plan to Sneak up on Murdoch", *Australian Financial Review*, 18 October 2005, 1.

Corp's move to Delaware was to adopt a poison pill, which is not permissible under Australian law.[275]

Unlike Delaware,[276] and some other jurisdictions such as Canada,[277] France and Japan,[278] Australia and the UK have not proven to be hospitable terrain for poison pills. Poison pills are, for all intents and purposes, non-existent in Australia, though there appears little consensus as to why this is so. There is no general prohibition upon specific defensive measures of this kind, however, at least three areas of Australian corporate law and governance have tended to impede the development of poison pills.

First, a possible explanation for the absence of poison pills in Australia is the general law on fiduciary duties.[279] Directors are subject to a fundamental duty to act bona fide for the benefit of the company and for proper purposes.[280] Defeating a takeover or ensuring that the current target board retains control are prima facie improper purposes.[281] UK and Australian case law contains strong dicta to the effect that it is

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275 See Alan Kohler, "Shock! News Screws Punters", *Sydney Morning Herald*, 13 August 2005, 45.

276 In the post-Enron era, however, shareholder pressure has led to the elimination of poison pills in an increasing number of US companies. In 2005, less than 50% of companies in the S&P 500 had poison pills and this figure fell to 37% in 2006. See ISS, *Poison Pills in France, Japan, the U.S. and Canada: Takeover Barriers Rise in Europe and Japan, But Fall in North America* (2007), 10-11.

277 Note, however, that in Canada the poison pill has evolved in an idiosyncratic way, providing shareholders "with protections that were never intended by the original designers of poison pills". See Philip Anisman, "Poison Pills: The Canadian Experience" in Theodor Baums, Klaus J. Hopt and Norbert Horn (eds), *Corporations, Capital Markets and Business in the Law: Liber Amicorum Richard M. Buxbaum* (2000), 1 at 12.

278 Poison pills have only been introduced in Japan and France very recently. See ISS, *Poison Pills in France, Japan, the U.S. and Canada: Takeover Barriers Rise in Europe and Japan, But Fall in North America* (2007), 6-9.

279 See, for example, Deborah A. DeMott, "Shareholders as Principals", *Duke Law School Public Law and Legal Theory Working Paper Series: Working Paper No. 15* (2001, available at http://ssrn.com/abstract=275049), 32-33; Lynden Griggs, "Golden Parachutes, Crown Jewels and the Arrival of the White Knight - Strategies to Defeat a Takeover. What Use in an Era of Rigorous Enforcement of Directors' Duties" (1998) 5 *Canberra L Rev* 203, 214-216.

280 An analogous statutory duty is found in s 181 *Corporations Act* 2001 (Cth).

281 *Hogg v Cramphorn Ltd* [1967] Ch 254, 268; *Howard Smith Ltd v Ampol Petroleum Ltd* [1974] AC 821, 837. Directors' conduct may, however, in limited circumstances be characterized as

unconstitutional for directors to allot shares to manipulate control,[282] and that shareholders have a personal right to be protected against dilution of their voting rights by improper board conduct.[283] Any such share issue by the directors would be voidable, unless ratified by the shareholders in general meeting.[284] Since poison pills, if triggered, produce substantial dilution of the bidder's stake[285] and often discriminate between shareholders,[286] in most cases it would be difficult for directors to argue that they have fulfilled their duty to act for a proper purpose in the best interests of the company.[287] A statutory oppression remedy is also available for conduct which is unfairly prejudicial or discriminatory to a shareholder under Australian law.[288]

The second inhibiting factor is the approach of the Australian Takeovers Panel to defensive conduct by target boards. The frustrating action policy would seem to

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within the proper sphere of managerial discretion, even though the conduct incidentally thwarts a takeover bid. *Cf Howard Smith Ltd v Ampol Petroleum Ltd*, *ibid*: *Harlowe's Nominees Pty Ltd v Woodside (Lakes Entrance) Oil Co NL* (1968) 121 CLR 483; *Teck Corp Ltd v Millar* (1973) 33 DLR (3d) 288.

282 *Hogg v Cramphorn Ltd* [1967] Ch 254, 268; *Howard Smith Ltd v Ampol Petroleum Ltd* [1974] AC 821, 837.

283 See, for example, *Residues Treatment and Trading Co Ltd v Southern Resources Ltd* (1988) 51 SASR 177, 202 (per King CJ).

284 *Hogg v Cramphorn Ltd* [1967] Ch 254.

285 Depending on whether the poison pill has a "flip-in" or a "flip-over" feature, the dilution may relate to the equity of either the target company or the hostile bidder. See Tunde I. Ogowewo, "Tactical Litigation in Takeover Contests" [2007] *J Bus L* 589, n2.

286 Such discrimination will occur where the bidder is excluded from the invitation to target shareholders to buy two shares for the price of one under the shareholder rights plan. See John Armour and David A. Skeel, "Who Writes the Rules for Hostile Takeovers, and Why? The Peculiar Divergence of U.S. and U.K. Takeover Regulation" (2007) 95 *Geo LJ* 1727, 1734.

287 Lynden Griggs, "Golden Parachutes, Crown Jewels and the Arrival of the White Knight - Strategies to Defeat a Takeover. What Use in an Era of Rigorous Enforcement of Directors' Duties" (1998) 5 *Canberra L Rev* 203, 215-216. See also *Criterion Properties Plc v Stratford UK Properties LLC* [2002] EWCA Civ 1883; [2003] 1 WLR 2108, para [26]. See, however, John Plender, "An Acceptable Poison Pill? It's Not an Oxymoron", *Financial Times*, 10 April 2006, 20, discussing one form of poison pill, as adopted by the Japanese company, Nippon Steel Corporation, which might be beneficial for long-term shareholders.

288 Section 232(e) *Corporations Act* 2001 (Cth).

preclude the adoption of a poison pill without shareholder consent,[289] and the Panel has made some specific remarks about poison pills that are consistent with this interpretation.[290] Further support for this position can be derived from the important decision of the Takeovers Panel concerning a 2003 takeover bid by Centro for the AMP Shopping Centre Trust.[291] This decision, in the context of managed schemes, demonstrated that the Panel is "willing to scrutinize measures that tend to act as poison pills … to ensure that unitholders are not unfairly deprived of the opportunity for a takeover premium".[292] The Panel stressed the "principle of 'non-entrenchment'" as a basis for its finding of unacceptable circumstances.[293] This reasoning also appears to underpin the English Court of Appeal decision in the leading UK case on poison pills, *Criterion Properties Plc v Stratford UK Properties LLC*.[294]

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289 This policy was developed in *Re Pinnacle VRB Ltd (No 5)* (2001) 39 ACSR 43; *Re Pinnacle VRB Ltd (No 8)* (2001) 39 ACSR 55; *Re Bigshop.com.au Ltd (No. 2)* [2001] ATP 24 (17 October 2001). See generally Emma Armson, "The Frustrating Action Policy: Shifting Power in the Takeover Context" (2003) 21 *C&SLJ* 487.

290 The Australian Takeovers Panel has stated, for example, that "[a]greements which the Panel considers are 'poison pills' and have not been approved by relevant shareholders may be found to create unacceptable circumstances": Takeovers Panel, *Guidance Note 12: Frustrating Action* (16 June 2003, available at http://www.takeovers.gov.au/content/120/download/GN12.pdf), para [12.28], note 11. Although Guidance Note 12 stated that the Panel may issue a further guidance note specifically on poison pills in the future if it appeared necessary (para [12.35]), this has not occurred to date.

291 See *Re AMP Shopping Centre Trust (No 1)* (2003) 45 ACSR 496; [2003] ATP 21; BC200302947; *Re AMP Shopping Centre Trust (No 2)* (2003) 45 ACSR 524; [2003] ATP 24; BC200302948, which concerned a managed investment scheme. The Australian Takeovers Panel held, at first instance, that the granting of certain pre-emptive rights to acquire interests in AMP Shopping Centre Trust (ART), exercisable on a change of responsible entity in ART, constituted "unacceptable circumstances". Unacceptable circumstances existed because:- (a) the pre-emptive rights would potentially deter a takeover bid for the target and entrench ART's existing responsible entity, which was contrary to the principles of an efficient, competitive and informed market (b) there had had not been adequate disclosure to unitholders about the effect of the pre-emptive rights; and (c) the pre-emptive rights had not been approved by unitholders. The Review Panel upheld the first instance decision. See generally Allens Arthur Robinson, 'In the Deal', 7 August 2003 (available at http://www.aar.com.au/pubs/itd/aug03/index.htm).

292 Braddon Jolley, Justin Mannolini and Rebecca Maslen-Stannage, "Takeovers Panel Doesn't Swallow Poison Pill" (July 2003, available at http://www.findlaw.com.au/article/9240.htm), 2-3.

293 *Re AMP Shopping Centre Trust (No 1)* (2003) 45 ACSR 496; [2003] ATP 21; BC200302947, paras [66]-[68].

294 [2002] EWCA Civ 1883, [2003] 1 WLR 2108. An appeal to the House of Lords ([2004] 1 WLR 1846) was decided on different grounds. It has been noted that, although Lord Justice Carnwath referred to the defensive arrangement in this case as a "poison pill", it in fact more

The third, and most likely, factor to have curtailed the use of poison pills in Australia is the ASX Listing Rules.[295] It has been argued, for example, that a former ASX Listing Rule, 3G(7),[296] which specifically prohibited certain defensive measures, would have invalidated the use of poison pills.[297] Although this particular Listing Rule is no longer operative, one commentator has argued that the more general wording of Listing Rule 6.1, which affords the ASX discretion to ensure that the terms governing each class of equity securities are "appropriate and equitable", could also be used to invalidate poison pills.[298]

Even if a poison pill is not directly prohibited under the ASX Listing Rules, the rules require shareholder approval for a range of transactions relating to changes of control or alterations to the capital structure of a listed company,[299] and some of these would affect the adoption of a poison pill. Listing Rule 7.1 has particular relevance in this regard.

Listing Rule 7.1 requires shareholder approval for any issue of more than 15% of the company's share capital, otherwise than on a pro-rata basis.[300] The rule's policy

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closely resembled a lock-up agreement. See John Armour and David A. Skeel, "Who Writes the Rules for Hostile Takeovers, and Why? The Peculiar Divergence of U.S. and U.K. Takeover Regulation" (2007) 95 *Geo LJ* 1727, n261.

295 See Rodd Levy, *Takeovers: Law and Strategy* (2nd ed, 2002), 151-152.

296 ASX Listing Rule 3G(7) prohibited a company from "issuing an option which, in the opinion of the stock exchange, was designed to frustrate a takeover bid or frustrate a person from becoming entitled to more than 20 per cent of equity securities in the company, or a person already entitled to more than 20 per cent of equity securities acquiring further equity securities in the company."

297 Rodd Levy, *Takeovers: Law and Strategy* (2nd ed, 2002), 151-152.

298 *Ibid*.

299 These ASX Listing Rules include:- Rule 10.1 (acquisition or disposal of a substantial asset to a person in a position of influence); Rule 11.2 (change in the main undertaking of the company); Rule 7.1 (issue of more than 15% of capital currently on issue); Rule 7.6 (issue of shares if 50% of shareholders call a meeting to appoint or remove directors); Rule 7.9 (issue of shares within three months of written notice of a takeover proposal). See generally Takeovers Panel, *Guidance Note 12: Frustrating Action* (16 June 2003, available at http://www.takeovers.gov.au/content/120/download/GN12.pdf), paras [12.8]- [12.9].

300 For a discussion of the history of Listing Rule 7.1 and a comparison of its operation with capital raising barriers in other jurisdictions, see ASX, Exposure Draft, *Capital Raising*

origin was concern about defensive share placements that might frustrate takeover bids and dilute the interests of existing shareholders.[301] In 2003, only six months before News Corp announced its Delaware re-incorporation plan, the ASX considered reform proposals to Listing Rule 7.1 aimed at providing more discretion to directors in issuing securities. The ASX considered that Listing Rule 7.1 was more restrictive and interventionist than the rules and practices of comparable exchanges, and the reform proposals sought to align it better with international markets.[302] Specific reform proposals included raising the 15% threshold for shareholder consent to 20%,[303] and allowing shareholders to confer a general mandate on management to issue securities.[304] Ultimately, however, no changes were made to Listing Rule 7.1 and the 15% threshold for shareholder consent to a securities issue remains. The triggering of a poison pill arguably falls within the ambit of Listing Rule 7.1 and would therefore require shareholder approval.

The ASX Listing Rules, therefore, undermine management's ability to establish entrenching mechanisms, such as poison pills, without shareholder consent. Recent empirical research, suggesting that that the presence of entrenching mechanisms may reduce firm value and stockholder returns, supports the approach taken by the listing rules from a policy perspective.[305]

The anti-entrenchment effect of the ASX Listing Rules seems to present a profound dilemma in relation to the News Corp re-incorporation story. This is due to the fact

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Mechanisms in a Disclosure-Based Market – ASX Proposals for Informed Choice: A Review of Listing Rule 7.1 – Proposed ASX Listing Rule Amendments (October 2003), paras [6.1] – [6.4], [8.1] – [8.3].

301 *Id*, paras [7.1]-[7.3].

302 *Id*, paras [4.1]-[4.3], [8.3].

303 *Id*, para [9.1].

304 It was proposed that such a general mandate would permit management to issue securities without the need for specific shareholder consent for a 13 month period from the date of the mandate. *Id*, para [9.2].

305 Lucian Arye Bebchuk, Alma Cohen and Allen Ferrell, "What Matters in Corporate Governance?", *Harvard Law School John M. Olin Discussion Paper No. 491* (2004, available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=593423).

that, in its concessions to the institutional investors, News Corp agreed to retain full foreign listing on the ASX, thereby binding itself to compliance with these listing rules. As such, even after its re-incorporation in Delaware, News Corp should still have been prohibited from issuing a poison pill, as a result of the operation of the ASX Listing Rules.

The answer to this puzzle may lie in the ability of the ASX to waive compliance with its listing rules. In the week that the Delaware re-incorporation became fully effective, it appears that News Corp applied for, and was granted, an array of waivers by the ASX, exempting the company from complying with particular listing rules.[306] While some of these waivers involved technical aspects of the re-incorporation, others related to fundamental corporate governance matters. Indeed, a number of the waivers related to specific listing rules that the institutional investors had included in their Governance Article, and had sought to incorporate into News Corp's Delaware charter.[307] The underlying policy of these listing rules is shareholder protection.[308] It

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306 On 2 November 2004, the ASX issued a waiver exempting News Corp from compliance with ASX Listing Rule 6.23. On 4 November 2004, further waivers were issued in favor of News Corp in relation to the following ASX Listing Rules:- LR 1.1 (condition 3); LR 1.1 (condition 8); LR 6.8; LR 6.9; LR 6.22; LR 6.23; LR 7.1; LR 8.10; LR 10.11; LR 14.3; LR 14.4 and LR 15.15. In 2005, further waivers were granted to News Corp regarding LR 3.8A and LR 7.33, and in 2007, a waiver was granted of LR 2.4.

307 ASX waivers were granted to News Corp with respect to the following listing rules, which had been included in the institutional investors' Governance Article:- LR 7.1 (requiring shareholder approval for new share issues exceeding 15% of capital); LR 10.11 (requiring shareholder approval for issue of securities to a related party); LR 14.3 (requirements regarding nomination of directors); LR 14.4 (requirements regarding election and rotation of directors). See News Corporation Group, *Governance Article for New Delaware Parent Company: Preservation of Australian Public Investor Protection & Empowerment Provisions* (2004, on file with the author), Clause 7, "ASX Listing Rules provisions to apply".

308 The waivers granted by the ASX specify the "underlying policy" for each listing rule waived. According to ASX Listing Waiver for LR 7.1 (waiver number WLC040532-007), the underlying policy of LR 7.1 is to "provide greater protection to smaller holders against dilution". ASX Listing Waiver for LR 10.11 (WLC040532-009) states that, by requiring shareholder approval for an issue of securities to a related party, LR 10.11 is "directed at preventing related party obtaining securities on advantageous terms and increasing their holding proportionate to other holdings". ASX Listing Waiver for LR 14.3 (WLC040532-010) states that LR 14.3, which provides that an entity must accept nominations for the election of directors up to 35 business days before the date of meeting, "gives reasonable opportunity for candidates to be nominated" and "supports shareholder democracy". According to ASX Listing Waiver for LR 14.4 (WLC040532-011), LR 14.4, regarding election and rotation of directors, "prevents entrenchment of directors" and "supports shareholder democracy" (waivers on file with the author).

is particularly interesting that one of the waivers related to ASX Listing Rule 7.1, the rule that primarily stands in the path of Australian companies issuing a poison pill.

In granting waivers to News Corp at the time of the re-incorporation, the ASX faced an inevitable position of conflict. The ASX had been subject to criticism since its demutualization and listing as a public company,[309] on the basis that a conflict of interest existed between its twin goals of regulation and profit maximization.[310] This conflict lay particularly close to the surface in its relations with News Corp. There had been consternation in the Australian marketplace that News Corp might delist from the ASX.[311] News Corp's decision to retain full secondary listing ensured that the ASX continued to receive revenue from trading of News Corp shares in Australia.

A further entrenchment mechanism, which is closely allied to poison pills, is the staggered board. In the US, the conjunction of poison pill and staggered board will constitute a virtually impregnable takeover defense.[312] Under Delaware law, directors may be elected for a staggered term of up to three years,[313] and, unless the certificate of incorporation provides otherwise, these directors can only be removed "for cause".[314] This insulates directors from removal and effectively prevents an acquirer from obtaining control of the board in a single election. While it is common for Australian and UK public companies to have staggered election terms for directors,

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309 The ASX was one of the first stock exchanges in the world to demutualize and to list as a public company on its own market. See generally Gwen Robinson, "Australia – Another Milestone Nears", *Financial Times*, 24 March 1998, 7; Fleur Leyden, "Best Result for ASX is Humphry's Last", *The Age*, 29 July 2004, 1.

310 See, for example, Editorial, "The Best Way to Restore Faith", *Australian Financial Review*, 23 July 2002, 62.

311 See, for example, Stephen Bartholomeusz, "News Move to NY Not Good for ASX", *Sydney Morning Herald*, 27 April 2004, 18.

312 Lucian Arye Bebchuk, John C. Coates and Guhan Subramanian, "The Powerful Antitakeover Force of Staggered Boards: Theory, Evidence and Policy" (2002) 54 *Stanford L Rev* 887.

313 Del. Code Ann, tit 8, s 141(d).

314 Del. Code Ann, tit 8, s 141(k)(1). This contrasts with the modern default rule, applying to non-classified boards, that directors may be removed with or without cause. Removal of directors "for cause" is no easy matter, and has been described as a "weapon of last resort": Charles R.T. O'Kelley and Robert B. Thompson, *Corporations and Other Business Associations: Cases and Materials* (5th ed, 2006), 163. See also *Campbell v Loew's, Inc* 134 A 2d 852 (Del Ch 1957), the leading case on removal for cause.

staggered boards cannot operate as an entrenchment and anti-takeover device in these jurisdictions. This is because shareholders possess an absolute right to remove directors with or without cause under Australian and UK law.[315] At the time of News Corp's re-incorporation, the institutional investors were unsuccessful in their attempt to include an analogous right in the Delaware charter.[316] Instead, the charter provided for a staggered board,[317] the directors of which would, according to the Delaware norm, be removable only for cause.[318]

4.2 Extension of the Pill and its Aftermath

> "It was never a bylaw. It was never a promise. It was never a pledge".
>
> Rupert Murdoch[319]

> "News Corp thus finds itself in a stew of its own making".
>
> Chancellor Chandler[320]

If News Corp's adoption of a poison pill in 2004 aroused institutional investor concern, its actions the following year produced a furor. In August 2005, News Corp

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315 This right cannot be altered in the constitution or by agreement. See s 203D *Corporations Act* 2001 (Cth); s 168, *Companies Act* 2006 (UK).

316 News Corporation Group, *Governance Article for New Delaware Parent Company: Preservation of Australian Public Investor Protection & Empowerment Provisions* (2004, on file with the author), 2.

317 See United States Securities and Exchange Commission, Form 8-K, Amended and Restated Certificate of Incorporation of News Corporation, Inc (November 12, 2004), Article V. This was in spite of the fact that there has been a trend recently towards declassification of US boards. In 2006, for the first time in recent years, a majority of S&P 500 companies had annually elected boards. See ISS, *Poison Pills in France, Japan, the U.S. and Canada: Takeover Barriers Rise in Europe and Japan, But Fall in North America* (2007), 11.

318 Del. Code Ann, tit 8, s 141(k)(1). Note, however, that News Corp's charter discards this norm in limited circumstances, stating that "[a]t any time that there shall be three or fewer stockholders of record, directors may be removed with or without cause". United States Securities and Exchange Commission, Form 8-K, Amended and Restated Certificate of Incorporation of News Corporation, Inc, *ibid.*

319 Cited in Lisa Murray, 'Poison Pill – There Was No Promise, Says Murdoch", *Sydney Morning Herald*, 13 October 2005, 21.

320 *UniSuper Ltd v News Corporation* 2006 WL 207505, *1 (Del Ch).

announced that its board had decided to extend the poison pill for two years beyond its expiration date in November 2005 without shareholder approval.[321] The announcement made no reference either to the board policy on poison pills, or to the reasons for deviation from that policy. The general reaction of the Australian financial press was severe, with one critic describing the announcement as "quite breathtaking" and evidence that News Corp was "mostly run by untrustworthy people".[322]

In a response to this criticism, John Hartigan, CEO and chairman of News Corp's wholly-owned Australian subsidiary, News Ltd,[323] justified the board's decision as necessary on the basis that changes of control are less stringently regulated under US law than under Australian law. According to Hartigan, the board's gatekeeper role under US law operates as the functional equivalent of Australian law's 20% threshold rule, in ensuring that all shareholders are treated fairly and equitably.[324] He said that, but for the reversal of the board's policy on poison pills, all News Corp shareholders "would now be potentially at risk of a predator who could assume control without paying a premium for it".[325]

Rupert Murdoch claimed simply that no promise to make the board policy unalterable had ever been made.[326] News Corp's undertaking concerning the extension of poison pills had appeared, however, not only in its board policy, but also as an attachment to

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321 See United States Securities and Exchange Commission, News Corporation, Form 8-K, 10 August 2005, 7. See also Keith L. Johnson and Andrew Clearfield, "Improving Governance by Joint Shareholder Action; Investors Await Trial to Assert Rights on News Corp. Poison Pill" (2006) 34(5) *Pensions and Investments* 12.

322 See Alan Kohler, "Shock! News Screws Punters", *Sydney Morning Herald*, 13 August 2005, 45.

323 See News Corporation, Press Release, *John Hartigan Appointed Chairman of News Limited*, 19 August 2005.

324 See John Hartigan, "News Ltd Boss Fires Back over Poison Pill", *Sydney Morning Herald*, 20 August 2005, 46.

325 *Ibid*.

326 Lisa Murray, "Poison Pill – There Was No Promise, Says Murdoch", *Sydney Morning Herald*, 13 October 2005, 21.

the Australian Federal Court proceedings,[327] which approved the corporate restructuring and re-incorporation.[328] In August 2005, the Australian corporate regulator, ASIC, announced that it intended to carry out an investigation into News Corp's actions in the context of statements made to the market,[329] but this inquiry was later discontinued.[330]

In October 2005, a group of twelve predominantly Australian and European institutional investors filed legal proceedings against News Corp and its directors in the Delaware Chancery Court.[331] The plaintiffs sought to invalidate News Corp's extension of the poison pill, and any subsequent extensions, unless authorized by shareholder vote. The plaintiffs' claim was based on a variety of grounds including:- breach of contract, promissory estoppel, fraud, negligent misrepresentation, and breach of fiduciary duty.[332] The defendants, on the other hand, argued that reversal of its earlier board policy did not breach a binding contractual undertaking by News

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327 See Kate Askew and Lisa Murray, "A Hard Act to Swallow" *Sydney Morning Herald*, 20 August 2005, 43.

328 In the Federal Court proceedings confirming the schemes of arrangement, Hely J made specific reference to the fact that News Corp had agreed to additional corporate governance provisions. See *News Corporation Ltd* [2004] FCA 1480 (19 November 2004), para [5].

329 Kate Askew and Lisa Murray, "A Hard Act to Swallow", *Sydney Morning Herald*, 20 August 2005, 43.

330 In announcing the decision to discontinue the inquiry, ASIC's head of compliance stated "[o]bviously, it's a concern when a company makes a statement to shareholders, only to go back on it, so we had a good look at it … But the statement was made by a US company under US law and it would require a very resource-intensive exercise for us to pursue the matter. We have decided we should stay out of it" (cited in Lisa Murray, "Poison Pill – There Was No Promise, Says Murdoch", *Sydney Morning Herald*, 13 October 2005, 21).

331 The majority of institutional shareholders were from Australia (six of the plaintiffs being members of ACSI), the Netherlands and the UK. Only two of the plaintiffs were US institutional investors. The plaintiffs to the action were UniSuper Ltd, Public Sector Superannuation Scheme Board, Commonwealth Superannuation Scheme Board, United Super Pty Ltd, Motor Trades Association of Australia Superannuation Fund Pty Ltd, HEST Australia Ltd, CARE Super Pty Ltd, Universities Superannuation Scheme Ltd, Britel Fund Nominees Limited, Stichting Pensioenfonds ABP, Connecticut Retirement Plans and Trust Funds, and the Clinton Township Police and Fire Retirement System. See *UniSuper Ltd v News Corporation* 2005 WL 3529317, *3 (Del Ch); Keith L. Johnson and Andrew Clearfield, "Improving Governance by Joint Shareholder Action; Investors Await Trial to Assert Rights on News Corp. Poison Pill" (2006) 34(5) *Pensions and Investments* 12; Stephen Bartholomeusz, 'Murdoch and the Global Fund Alliance That Bites", *Sydney Morning Herald*, 11 October 2005, 19.

332 *UniSuper Ltd v News Corporation* 2005 WL 3529317, *3 (Del Ch).

Corp,[333] and that indeed, any such contract between shareholders and the board would be contrary to Delaware law, as an impermissible constraint on centralized managerial authority under Del GCL s 141(a).[334]

In a motion filed by the defendants to dismiss the case, Chancellor Chandler ruled in late 2005 that the plaintiffs' action for breach of contract and estoppel[335] could proceed.[336] The plaintiffs claimed that an agreement existed, either in the form of an oral contract or a written contract, in which News Corp had consented to subject any extension of the poison pill to a shareholder vote.[337] Although Chancellor Chandler considered that the complaint asserted few facts to support either form of contract, the plaintiffs were entitled to the benefit of all reasonable inferences under their complaint.[338]

Chancellor Chandler raised some problematical aspects of the plaintiffs' claim. He observed, in reasoning reminiscent of *Metropolitan Life Insurance Co v RJR Nabisco, Inc*,[339] that the plaintiffs were sophisticated institutional investors, who clearly could have protected their interests by negotiating an enforceable agreement or changes to the corporate charter, as had indeed occurred in the case of some other concessions.[340]

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333 News Corp claimed that it had promised to establish a board policy, but had not promised that the policy would be immutable. *Id*, n34.

334 *Id*, *6. See also Peg Brickley, "News Corp Wins Right to Appeal Holder Suit in Delaware", *Dow Jones Newswires*, 21 January 2006.

335 The defendants' motion to dismiss was successful in relation to the counts of fraud, negligent misrepresentation and equitable fraud, and breach of fiduciary duty. See *UniSuper Ltd v News Corporation* 2005 WL 3529317, *1 (Del Ch).

336 *Ibid*.

337 It was argued that the parties entered into a written contract evidenced by News Corp's Press Release and Letter to Shareholders at the time of its re-incorporation: *UniSuper Ltd v News Corporation, id*, *4.

338 *Ibid.*

339 716 F Supp 1504 (SDNY 1989).

340 *UniSuper Ltd v News Corporation* 2005 WL 3529317, *4 (Del Ch).

He also noted that interpretational difficulties could arise in the future about ambiguities in the alleged agreement.[341]

In spite of these difficulties, the plaintiffs' claim withstood the defendants' motion to dismiss. Chancellor Chandler rejected the defendants' argument that any agreement between the board and shareholders would be contrary to the general grant of managerial power under Delaware law.[342] Adopting a principal/agent theory of the relationship between shareholders and the board,[343] he viewed shareholders as "the ultimate holders of power", or "owners" of the company,[344] and saw no impediment to directors entering into such a contract with the shareholders.[345] Although Chancellor Chandler's theory of the shareholder does not accord with modern UK and Australian law,[346] the outcome in the case is consistent with legal principles concerning allocation of power in these jurisdictions. However, it should be remembered that the *UniSuper* case is a decision of the Delaware Chancery Court,[347] and it is open to doubt whether the Delaware Supreme Court would agree with it.[348]

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341 *Id*, *5.

342 *Id*, *6.

343 *Id*, *6, *8.

344 *Id*, *6.

345 *Id*, *6.

346 Although 19th century UK corporate law adopted an agency analysis (*Isle of Wight Railway Co v Tahourdin* (1884) LR 25 Ch D 320), this analysis was definitively rejected in *Automatic Self Cleansing Filter Syndicate Co Ltd v Cuninghame* [1906] 2 Ch 34. See generally Jennifer G. Hill, "Visions and Revisions of the Shareholder" (2000) 48 *Am J Comp L* 39, 42-44, 48.

347 News Corp asked the Court of Chancery to certify the case for immediate appeal, and, although the Court of Chancery did so (see *UniSuper Ltd v News Corp*, 2006 WL 207505 (Del Ch)), the Delaware Supreme Court declined, to accept an appeal in the case.

348 Indeed, this point was made by a Delaware Supreme Court judge in a recent hearing. Vice Chancellor Lamb said "UniSuper is a decision by the Court of Chancery. It's not a Supreme Court decision, and it isn't necessarily true that the Supreme Court would agree, is it?": Transcript of Final Hearing at 36, Bebchuk (Civil Action No 2145-N) (cited in Guhan Subramanian, "The Emerging Problem of Embedded Defenses: Lessons from Air Line Pilots Ass'n, International v. UAL Corp" (2007) 120 *Harv L Rev* 1239, n35).

Policy issues were clearly influential in *UniSuper Ltd v News Corporation*.[349] Chancellor Chandler noted that a "troubling" aspect of the defendants' view of Delaware law was that, if correct, it would potentially invalidate all of the governance concessions made by News Corp in favor of the institutional investors, not merely the board policy on poison pills.[350] Yet, the judge accepted that without these concessions, News Corp's re-incorporation would not have occurred.[351] Echoing certain policy concerns of the Paulson Committee,[352] Chancellor Chandler suggested that shareholders of foreign companies would in future be unlikely to vote for re-incorporation in Delaware, if inducements to procure their vote were held to be unenforceable there.[353]

On 6 April 2006, less than three weeks before the case was due to go to trial, the parties settled the proceedings and News Corp agreed to allow shareholders to vote on the extension of the poison pill at its October 2006 annual meeting.[354] On 20 October 2006, New Corp shareholders voted to approve the continuance of the poison pill defense. The approval margin was relatively slim, with 57% in favor of, and 43% against, renewal of the pill.[355] Shareholder backlash was also evident in voting to re-elect four directors.[356] The conflict was finally resolved, when Rupert Murdoch and

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349 *UniSuper Ltd v News Corporation* 2005 WL 3529317 (Del Ch).

350 *UniSuper Ltd v News Corporation* 2006 WL 207505, *1 (Del Ch).

351 *Ibid*.

352 Committee on Capital Markets Regulation, *Interim Report of the Committee on Capital Markets Regulation* (30 November 2006, revised version released 5 December 2006), 16.

353 *UniSuper Ltd v News Corporation* 2006 WL 207505, *1 (Del Ch).

354 The trial had been scheduled for 24 April 2006. See generally Joshua Chaffin, "News Corp Settles Poison Pill Lawsuit", *Financial Times*, 7 April 2006, 25; John Plender, "An Acceptable Poison Pill? It's not an Oxymoron", *Financial Times*, 10 April 2006, 20; Julia Angwin, "News Corp. to Put Poison Pill to Shareholder Vote", *The Wall Street Journal*, 7 April 2006, A3.

355 Liberty Media voted against renewal of the poison pill. See Julia Angwin, "News Corp. Fends off Liberty Media", *The Wall Street Journal*, 21 October 2006, A3.

356 CGI and ISS recommended that that shareholders withhold their votes from the four directors seeking re-election. When the re-election vote took place, 15% of shares voted withheld support from three directors seeking re-election and 13% of shares voted withheld support for News Corp's President, Peter Chernin. See Sundeep Tucker, "News Corp Tries to Halt Poison Pill Revolt", *Financial Times*, 11 October 2005, 23; Andrew Edgecliffe-Johnson and Aline Van Duyn, "Murdoch Weathers Investor Protests", *Financial Times*, 22 October 2005,

John Malone settled their differences via an $11 billion asset swap, with News Corp agreeing to lift its contentious pill.[357]

Although the *UniSuper* case was ultimately settled, its implications for the balance of managerial and shareholder power in the US continue to be tested. In June 2006, *Bebchuk v CA, Inc*[358] came before the Delaware Court of Chancery. Like the *UniSuper* case, *Bebchuk v CA, Inc* concerned poison pills. It involved the validity of a proposed stockholder bylaw, which sought to restrict the authority of the board of directors to enact any stockholder rights plan in the absence of shareholder consent.[359] The corporation argued that the proposed bylaw could be omitted from its proxy materials, on the basis that its adoption would violate Delaware law by seeking to limit the authority of the board of directors and interfere with managerial power.[360]

In *Bebchuk v CA, Inc*,[361] Vice Chancellor Lamb dismissed the request for declaratory relief as "unripe",[362] noting that the court should be particularly cautious in giving

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1; Julia Angwin, "News Corp.'s Murdoch Claims Victory in Poison-pill Decision", *The Wall Street Journal*, 22 October 2005, A3.

357 Under the deal with News Corp, Liberty Media agreed to swap its $11.2 billion stake in News Corp for News Corp's 38.5% stake in DirecTV, $588 million in cash (raised from $550 million under an initial agreement in December 2006) and three local Fox sports channels, valued at approximately $550 million. The deal was generally considered to favor Liberty Media. The elimination of Liberty Media's News Corp stake increased the voting stake of other News Corp shareholders, including Murdoch family interests, which rose from approximately 31.2% to 38% after the deal. See Julia Angwin and Matthew Karnitschnig, "Liberty is Expected to Seek Partner for DirecTV – With News Corp Deal. Set, Investors Look for Tie-up; Murdoch to Drop Poison Pill", *The Wall Street Journal*, 23 December 2006, A3. The asset swap was later overwhelmingly approved by News Corp Class B shareholders. See "News Corp. Shareholders Accept Liberty Deal", *New York Times*, 4 April 2007, 6.

358 (2006) 902 A 2d 737 (Del Ch).

359 Under the proposed amendment to the company's bylaws, in the absence of shareholder consent, any adoption, or extension, of a stockholder rights plan by the board of directors, would require unanimous consent of directors and would automatically expire one year after its adoption or amendment. *Id*, 739.

360 The SEC refused to give a "no-action letter" in connection with CA's proposed omission of the shareholder proposal, since litigation was pending. See SEC, *CA, Inc.: No-Action Letter*, 2006 WL 1547985 (June 5, 2006).

361 (2006) 902 A 2d 737 (Del Ch).

362 According to the court, the action would only become ripe and within its jurisdiction if the bylaw were put to a stockholder vote and adopted. *Id*, 741.

advisory or hypothetical opinions in matters that raise novel and significant issues under Delaware law.[363] Nonetheless, in *obiter dictum* the court stated that the proposed bylaw was not "obviously invalid".[364] The court, while acknowledging that the power to adopt a rights plan is clearly vested in the board of directors, observed that it was "less clear that the exercise of that power can never be the subject of a bylaw, whether enacted by the board of directors or by the stockholders."[365] The court relied on the *UniSuper* decision in support of the proposition that a contractual restraint on the board's power to issue a poison pill is valid under Delaware law.[366]

Therefore, although the conflict between News Corp and its institutional shareholders was settled, the ruling in *UniSuper Ltd v News Corporation*[367] - that under Delaware law shareholders may enter into enforceable agreements with the board concerning the allocation of power under corporate governance structures[368] - continues to exert influence. Given the Delaware courts' traditional legitimization of poison pills without the need for shareholder consent,[369] the *UniSuper* case has been described as marking "a symbolic shift"[370] in this regard. It has been suggested that the potential

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363 *Id*, 740.

364 *Id*, 742.

365 *Id*, 743.

366 *Id*, n34. The court also considered that future factual matters, such as the possibility that the CA board might voluntarily restrict its powers in relation to poison pills as in the *UniSuper* case, could also affect the justiciable issues in the case. *Id*, 743.

367 2005 WL 3529317 (Del Ch).

368 *Id*, *5-*6 (Del Ch); Keith L. Johnson and Andrew Clearfield, "Improving Governance by Joint Shareholder Action; Investors Await Trial to Assert Rights on News Corp. Poison Pill" (2006) 34(5) *Pensions and Investments* 12.

369 See, for example, *Moran v Household International*, *Inc* 500 A 2d 1346 (1984).

370 John Plender, "An Acceptable Poison Pill? It's Not an Oxymoron", *Financial Times*, 10 April 2006, 20. See also Stuart M. Grant and Megan D. McIntyre, "*UniSuper v News Corporation*: Affirmation that Shareholders, Not Directors, are the Ultimate Holders of Corporate Power" (2006, on file with the author), viewing the decision as a significant victory for shareholder rights.

weakening of poison pills through the *UniSuper* case and *Bebchuk v CA, Inc*[371] may lead to the development of alternative forms of takeover defense in the US.[372]

5. Commercial Backlash - The Boral Amendment and the Coca-Cola Amatil Prenuptial Debate

> "He was also an adept at breaking rules, or diverting them to ends not intended by those who had framed them".
>
> Anthony Powell, *A Dance to the Music of Time*[373]

Much recent corporate governance debate has focused on the role played by legal rules in enhancing or diminishing shareholder participation. As already discussed, News Corp's institutional investors sought to include the substance of many Australian legal rules into the company's Delaware charter to enhance shareholder rights. Yet, while legal rules clearly matter in establishing the balance of power between the board and shareholders, commercial practice may play an equally important role.

An interesting tension has emerged between Australian legal rules and commercial practice in this respect. In spite of the existence of legal rules designed to enhance shareholder participation, a number of commercial developments have pulled in the opposite direction. Two developments in particular demonstrate this evolving tension: the successful 2003 amendment to the constitution of Boral Ltd ("the Boral amendment"), and the unsuccessful attempt by several Australian companies to introduce corporate prenuptial agreements for non-executive directors.

5.1 The Boral Backlash

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371 (2006) 902 A 2d 737 (Del Ch).

372 See Guhan Subramanian, "The Emerging Problem of Embedded Defenses: Lessons from Air Line Pilots Ass'n, International v. UAL Corp" (2007) 120 *Harv L Rev* 1239, 1243-1244.

373 Anthony Powell, *A Dance to the Music of Time: Spring* (1997, trilogy containing three volumes first published 1951, 1952, 1955), 8.

Paradoxically, whereas News Corp's institutional investors fought for the inclusion of stronger shareholder participatory rights in the company's Delaware charter, the Boral amendment involved a vote by shareholders at Boral Ltd ("Boral") to curtail their powers in the future.

Under Australian law, changes to the corporate constitution may be initiated by shareholders and can generally be effected by a special resolution, passed by at least 75% of votes actually cast by shareholders entitled to vote on the resolution.[374] It is possible, however, for the constitution to provide that the special resolution is not effective to alter the constitution unless a further specified requirement has been satisfied.[375] Theoretically at least, amendment of the constitution is a potent shareholder right, since there is no restriction on the content of the alteration. Although, when the constitution vests managerial power in the board,[376] shareholders are unable to pass a resolution relating to managerial matters, this restriction does not apply to alterations to the constitution reallocating power between the board and shareholders. It is also exceptionally easy for shareholders to propose changes to the constitution under Australian law. Under the controversial "100 member rule", 5% of the shareholders, or 100 shareholders by number, may requisition a shareholder meeting to alter the company's constitution[377] or propose a resolution to that effect where a meeting has already been convened by the company.[378] News Corp's institutional investors sought unsuccessfully to include both limbs of the 100 member rule into the company's Delaware charter.[379]

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374 See ss 136(2) *Corporations Act* 2001 (Cth). "Special resolution" is defined in s 9 *Corporations Act* 2001 (Cth).

375 See s 136(3) *Corporations Act* 2001 (Cth).

376 Section 198A *Corporations Act* 2001 (Cth) is a replaceable rule, stating that "[t]he business of a company is to be managed by or under the direction of the directors". See generally *Automatic Self Cleansing Filter Syndicate Co Ltd v Cuninghame* [1906] 2 Ch 34; *NRMA v Parker* (1986) 11 ACLR 1.

377 Section 249D *Corporations Act* 2001 (Cth).

378 Section 249N(1) *Corporations Act* 2001 (Cth).

379 See News Corporation Group, *Governance Article for New Delaware Parent Company: Preservation of Australian Public Investor Protection & Empowerment Provisions* (2004, on file with the author), 2.

Resolution 3 of the notice of meeting for Boral's 2003 annual shareholder meeting, however, proposed a constitutional amendment, which would reverse the effects of the 100 member rule at Boral. The resolution, which was passed by a special resolution,[380] limited the ability of Boral shareholders to requisition a meeting, or propose a resolution, to alter the constitution in the future. It achieved this by inserting further conditions which needed to be met before Boral's "new constitution" could be altered. Any proposed constitutional amendment would first have to be approved by either the board of directors or shareholders holding at least 5% of voting shares. The Boral amendment therefore subverted both limbs of the 100 member rule in their application to alterations of the company's constitution. Whereas previously 100 shareholders acting together could requisition a meeting, or propose a resolution, to alter the constitution, the Boral amendment meant that in future this could only be done by shareholders with $160 million worth of Boral shares,[381] unless they had the board's consent.

At first sight, it seems puzzling that Boral shareholders voted to restrict their participatory powers under Australian law. However, this was a matter where there was arguably a schism between large institutional shareholders and small shareholders.[382] There had been several high profile examples of Australian companies in which environmental activists had taken a relatively small stake and

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[380] Only approximately 6% of votes cast on the resolution were opposed to the constitutional change. See Boral Limited, "ASX Announcement – Annual General Meeting – Outcome of Business and Declaration of Polls", 21 October 2003, 2; Stuart Wilson, "Boring into Minorities a Big Blue in Boral Board War", *The Australian*, 28 October 2003, 24.

[381] In other words, 5% of Boral's capital. See Stephen Bartholomeusz, "Heavy-handed Boral Could Help Strengthen the Hand of Critics", *The Age*, 23 October 2003, 3. The 100 member rule would still apply to ordinary resolutions and special resolutions not involving an alteration to the constitution.

[382] The institutional investors were criticized for their role in the Boral constitutional amendment. While Stephen Conroy, the Labor spokesman for financial services and corporate governance, condemned these investors for "turning a blind eye" to the implications of the Boral amendment, other financial press commentators pointed out that the institutional investors actively supported management's position on the issue. See Bryan Frith, "Right to Clip Board Powers", *The Australian*, 2 December 2003, 20.

utilized the 100 member rule to initiate constitutional changes.[383] Boral had itself been the target of shareholder activism by the Transport Workers' Union ("TWU"),[384] reflecting a trend, both in Australia and the US,[385] for unions to propose corporate governance resolutions at annual shareholder meetings.[386] Large institutional investors at Boral presumably shared management's concern that small activist shareholders could use the 100 member rule to further a social agenda.[387] Thus, the events at Boral reflect Bainbridge's concern that the conferral of greater shareholder participatory rights could empower classes of shareholders who might misuse those powers[388] and Justice Strine's argument that, in certain circumstances, even investors themselves might not favor strong shareholder rights.[389]

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383 Environmental activism in major Australian companies included, for example, the requisitioning by shareholders of extraordinary general meetings at North Ltd and Gunns Ltd. See Shelley Bielefeld, Sue Higginson, Jim Jackson and Aidan Ricketts, "Directors' Duties to the Company and Minority Shareholder Environmental Activism" (2004) 23 *C&SLJ* 28, 43-47.

384 The TWU used the 100 member rule to propose a number of resolutions at the 2003 annual shareholder meeting relating to safety concerns and corporate governance matters, including executive remuneration. None of the resolutions was passed. For further details of these events, see Michael Rawling, "Australian Trade Unions as Shareholder Activists: The Rocky Path Towards Corporate Democracy" (2006) 28 *Syd L Rev* 227, 229-233; Kirsten Anderson and Ian Ramsay, "From the Picket Line to the Board Room: Union Shareholder Activism in Australia" (2006) 24 *C&SLJ* 279, 289-292.

385 See, for example, Stewart J. Schwab and Randall S. Thomas, "Realigning Corporate Governance: Shareholder Activism by Labor Unions" (1998) 96 *Mich L Rev* 1018.

386 For an overview and analysis of recent instances of union shareholder activism in Australia, see Kirsten Anderson and Ian Ramsay, "From the Picket Line to the Board Room: Union Shareholder Activism in Australia" (2006) 24 *C&SLJ* 279. For discussion of the growth of shareholder activism by labor unions in the US, see generally Stewart J. Schwab and Randall S. Thomas, *ibid*.

387 This concern was also expressed by the Corporations and Securities Advisory Committee (now known as the Corporations and Markets Advisory Committee (CAMAC)). In its 2000 Report entitled *Shareholder Participation in the Modern Listed Company*, CASAC criticized the 100 member rule on the basis that the threshold level of shareholder support was too low, was inconsistent with much higher thresholds in other jurisdictions, and could be abused by activist shareholders with a social agenda (CASAC, *Shareholder Participation in the Modern Listed Public Company*, Final Report (July 2000), Recommendation 2, 15). In contrast, other commentators have praised this particular aspect of the 100 member rule. Michael Rawling, for example, suggests that in the context of widespread shareholder apathy, the use of the rule by activist groups provides a crucial measure of management accountability that would otherwise be lacking: Michael Rawling, "Australian Trade Unions as Shareholder Activists: The Rocky Path Towards Corporate Democracy" (2006) 28 *Syd L Rev* 227, 241-243. Rawling also observes that the interests of such activist groups do not necessarily diverge from more 'traditional' shareholder concerns: *id*, 231-232.

388 Stephen M. Bainbridge, "Director Primacy and Shareholder Disempowerment" (2006) 119 *Harv L Rev* 1735, 1751.

Resolution 3 explicitly relied for its validity on s 136(3) of the Australian *Corporations Act*, which, as mentioned earlier, permits a company to stipulate that "a further requirement" is necessary before a special resolution to alter the constitution is effective.[390] This section envisages the possibility of virtual entrenchment of constitutional provisions, depending upon the stringency of the "further requirement".[391] However, it is not clear that the Boral amendment is validated by this provision, since, rather than stipulating a "further requirement" to a special resolution altering the company's constitution, the Boral amendment prevents voting at all on the proposed special resolution in certain circumstances.

The Boral amendment has been controversial, and its legitimacy was questioned in Parliamentary Joint Committee hearings on the CLERP 9 Bill 2003.[392] Nonetheless, for some time it appeared that legislative intervention might make it unnecessary for corporate management to seek to circumvent the 100 member rule by such indirect means. In February 2005, the Australian federal government announced its intention to abolish the 100 member rule in relation to requisitioning shareholder meetings.[393]

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389 Vice Chancellor Leo E. Strine, "Toward a True Corporate Republic: A Traditionalist Response to Bebchuk's Solution for Improving Corporate America" (2006) 119 *Harv L Rev* 1759, 1759.

390 Section 136(3) of the *Corporations Act* 2001 (Cth) states that "[t]he company's constitution may provide that the special resolution does not have any effect unless a further requirement specified in the constitution relating to that modification or repeal has been complied with".

391 There is no reference in the *Corporations Act* to the kind of "further requirement" contemplated, however, earlier incarnations of the legislation referred to matters such as a supermajority voting requirement or the need for the approval of a particular person before the amendment would take effect. See, for example, s 176(3) *Corporations Law.*

392 Commonwealth of Australia, Joint Committee on Corporations and Financial Services, *Official Committee Hansard*, 18 March 2004, 12-13; Commonwealth of Australia, Joint Committee on Corporations and Financial Services, *Official Committee Hansard*, 16 March 2004, 10-11, 62-67; Commonwealth of Australia, Joint Committee on Corporations and Financial Services, *Official Committee Hansard*, 9 March 2004, 36-37.

393 See Chris Pearce, Parliamentary Secretary to the Treasurer, Press Release, "Government Consults on Proposed Corporate Governance Reforms", 7 February 2005; Corporations Amendment Bill (No 2) 2005, Explanatory Memorandum, Exposure Draft. A concession embedded in the reform proposal was that the number of shareholders required to propose a resolution at an annual general meeting was to be lowered from 100 to 20. See s 249N *Corporations Act* 2001 (Cth).

The proposed reforms appear to have been a response to lobbying by companies which had previously experienced high levels of shareholder activism.[394]

However, the future of the reform proposals was placed in jeopardy after state leaders rejected them at a meeting of the Ministerial Council for Corporations in July 2006.[395] Prior to the meeting, several states cast doubt on the supposed detriment caused to Australian companies by the 100 member rule, and expressed concern over the effect of reform on the rights of minority shareholders.[396] The fate of the proposed reforms now appears even more uncertain, given the recent change of federal government in Australia.[397]

5.2 Background to the Coca-Cola Amatil Prenuptial Debate - The NAB Dispute

Another commercial development in Australia, which arguably affected the balance of power between shareholders and directors, was the emergence of the corporate prenuptial agreement. This development emerged in response to the 2004 corporate governance dispute between members of the board of the National Australia Bank

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394 See generally Anne Lampe, "Money – There Goes Democracy", *Sydney Morning Herald*, 11 December 2002, 4; Simon Milne and Nicola Wakefield Evans, "Shareholder Requisitions: The 5%/100 Member Provision" (2003) 31 *Aust Bus L Rev* 285 at 286-287.

395 See Chris Pearce, Parliamentary Secretary to the Treasurer, Press Release, "Key Corporate Governance Reforms in Jeopardy", 27 July 2006. The states' rejection of the reforms was criticized by a number of industry bodies, including the Australian Institute of Company Directors, the Australian Investor Relations Association, the Business Council of Australia, Chartered Secretaries Australia, the Investment & Financial Services Association, the Australian Employee Ownership Association and the Financial Services Institute of Australasia. See Chartered Secretaries Australia, Media Release, "Shareholders Caught in Political Shenanigans", 26 July 2006; Leon Gettler, "IFSA Censures States over 100 Member Reform", *The Sydney Morning Herald*, 21 June 2006, 37.

396 See Joseph Kerr, "States Resist 100-member Rule Reform", *The Australian*, 14 June 2006, 24. As an alternative, the states proposed a rule allowing a number of shareholders equal to the square root of the total number of shareholders to requisition an extraordinary general meeting. See Brian Salter, "Corporations Law Best Left to the Feds", *Australian Financial Review*, 20 September 2006, 63.

397 In a federal election held on 24 November 2007, the Liberal Government, which had proposed abolition of the 100 member rule, was defeated by the Australian Labor Party, with Kevin Rudd replacing John Howard as Prime Minister of Australia.

Limited ("NAB"). The NAB dispute also had interesting implications for what is expected of independent directors and boards.

The dispute stemmed from a foreign exchange trading scandal, revealed by NAB in January 2004,[398] which prompted resignations of the bank's CEO and chairman.[399] NAB also announced that it had commissioned PricewaterhouseCoopers ("PwC") to conduct an investigation and prepare a report into the foreign exchange trading scandal.[400]

One of NAB's non-executive directors, Catherine Walter, challenged the report's legitimacy in advance, claiming that PwC had significant conflicts of interest which compromised the report and rendered it procedurally flawed.[401] The PwC Report[402] was released on 12 March 2004, in conjunction with a probity advice by Blake Dawson Waldron certifying the Report's independence.[403] The PwC Report found

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398 The foreign exchange trading scandal became public in early 2004, when NAB announced that it had identified, and was investigating, currency option losses originally estimated to be around A$180 million. See National Australia Bank, "ASX Announcement – Announcement of Irregular Trading Losses", 13 January 2004 (available at http://www.nabgroup.com/0,,40255,00.html). Within two weeks, the estimate of loss had escalated to A$360 million. See National Australia Bank, "ASX Announcement - Update on Unauthorised Foreign Currency Options Trading", 27 January 2004 (available at http://www.nabgroup.com/0,,41213,00.html). See generally Andrew Cornell and Stewart Oldfield, "Where NAB Went Wrong", *Australian Financial Review*, 8 May 2004, 20; Pamela Williams, "The Heretic", *Australian Financial Review*, 27 August 2004, 74.

399 See National Australia Bank, "ASX Announcement – John Stewart Appointed the National's Managing Director & Chief Executive Following the Resignation of Frank Cicutto", 2 February 2004 (available at http://www.nabgroup.com/0,,41673,00.html); National Australia Bank, "ASX Announcement – Mr Graham Kraehe Appointed the National's Chairman Following the Resignation of Mr Charles Allen", 16 February 2004 (available at http://www.nabgroup.com/0,,42633,00.html).

400 See National Australia Bank, "ASX Announcement – Letter to Shareholders from DCK Allen, Chairman of the Board of Directors", 21 January 2004 (available at http://www.nabgroup.com/0,,40733,00.html).

401 Ms Walter argued that, as a result of the close business relationship between NAB and PwC and particularly the fact that PwC had a strategic alliance with NAB to provide internal audit services, the report "lacked legitimacy in serious respects". See Pamela Williams, "The Heretic", *Australian Financial Review*, 27 August 2004, 74.

402 PricewaterhouseCoopers, *Investigation into Foreign Exchange Losses at the National Australia Bank*, 12 March 2004 (available at http://www.nabgroup.com/vgnmedia/downld/pwcreport.pdf).

403 Blake Dawson Waldron, *Probity of Governance Advice: PricewaterhouseCoopers ("PwC") Report into Foreign Exchange Losses*, 12 March 2004 (available at

that four foreign exchange currency traders had exploited weaknesses in the bank's risk management controls to hide trading losses and protect bonuses.[404] The Report was highly critical of aspects of NAB's corporate culture,[405] and considered that ultimate responsibility for the "tone at the top" lay with the board of directors and the CEO.[406]

At the time of the release of the PwC Report, the NAB chair, Graham Kraehe, announced that Walter would be removed from the audit committee.[407] At a subsequent board crisis meeting, Walter was asked to resign as a director. Upon her refusal to do so, the bank announced that it had received a request from the other non-executive directors to convene an extraordinary shareholder meeting to remove Walter from office.[408]

Catherine Walter, in a strategy reminiscent of Samson, announced that she would propose alternative resolutions at a shareholder meeting, seeking the staged removal of the entire NAB board, including herself, and the immediate replacement of Kraehe as chair. She also proposed several resolutions censuring the board for its role in the

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http://www.nabgroup.com/vgnmedia/downld/bdwreport.pdf). The Blake Dawson Waldron probity advice found that a conflict existed in respect of one aspect of PwC's investigation only, and that this conflict had been satisfactorily resolved by the separate engagement of a non-conflicted expert.

404 PricewaterhouseCoopers, *Investigation into Foreign Exchange Losses at the National Australia Bank*, 12 March 2004 (available at http://www.nabgroup.com/vgnmedia/downld/pwcreport.pdf), 3, 17, 21-28.

405 Dysfunctional aspects of the corporate culture included a focus on process and documentation over substance, and a systemic abrogation of responsibility: *id*, 32. The Australian Prudential Regulatory Authority ("APRA") also considered that cultural issues in the currency options division were central to the bank's losses. According to APRA, "[t]he culture … was one in which risk management controls were seen as trip-wires to be negotiated rather than presenting any genuine constraint on risk-taking behaviour". See APRA, *Report into Irregular Currency Options Trading at the National Australia Bank*, 23 March 2004, 6 (available at http://www.nabgroup.com/vgnmedia/downld/APRAreport_24march04.pdf).

406 PricewaterhouseCoopers, *Investigation into Foreign Exchange Losses at the National Australia Bank, id*, 3-4, 31-32.

407 National Australia Bank, "ASX Announcement – Board Changes at the National", 12 March 2004 (available at http://www.nabgroup.com/0,,44475,00.html).

408 See National Australia Bank, "ASX Announcement – National Shareholders to End Board Impasse", 26 March 2004 (available at http://www.nabgroup.com/0,,45934,00.html); Pamela Williams, "The Heretic", *Australian Financial Review*, 27 August 2004, 74.

foreign exchange scandal, and calling on the directors to forgo more than $1 million in retirement benefits.[409] Both groups in the NAB dispute vigorously lobbied institutional investors in the lead-up to the proposed shareholder meeting,[410] and it appears that dialogue with major investors was influential in resolving the dispute.[411] A showdown at the scheduled shareholder meeting[412] was ultimately avoided when, as part of a compromise, Kraehe, two other long-standing directors and Walter all agreed to resign from the NAB board.[413]

Opinion was sharply divided on the NAB corporate governance dispute, and to some degree parallels debate in the US on greater shareholder participation in board nominations.[414] Opponents of Catherine Walter, stressing the need for board harmony, argued that her criticism of the PwC Report was baseless and that her public campaign had seriously damaged the bank's commercial standing and shareholder

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409 See National Australia Bank, "ASX Announcement – Notices Submitted by Mrs Catherine Walter", 29 March 2004 (available at http://www.nabgroup.com/0,,45973,00.html); Stephen Bartholomeusz, "Shareholders to Decide Future of Bank's Board", *Sydney Morning Herald*, 20 April 2004, 21.

410 In early May 2004, NAB's major shareholders, AMP, Perpetual and the Australian Council of Super Investors announced their somewhat reluctant support of NAB chair, Graham Kraehe. See Andrew Cornell and Stewart Oldfield, "Where NAB Went Wrong", *Australian Financial Review*, 8 May 2004, 20. Corporate Governance International, however, advised its clients to vote in favor of removal of all directors, except the CEO, John Stewart. See Stewart Oldfield, "Kraehe Digs in, Snubs Walter", *Australian Financial Review*, 5 May 2004, 1.

411 Cornell and Oldfield, *ibid*.

412 Technically, in fact, three separate shareholder meetings were scheduled to consider the different sets of resolutions proposed. See National Australia Bank, "ASX Announcement – National General Meetings to be Held on 21 May 2004", 19 May 2004 (available at http://www.nabgroup.com/0,,47233,00.html).

413 Graham Kraehe announced that he would retire after overseeing a board reconstruction and that two of NAB's longest serving directors, Ken Moss and Ed Tweddell, would retire in three months. See National Australia Bank, "ASX Announcement – Statement by Seven Non-executive Directors of the National", 5 May 2004 (available at http://www.nabgroup.com/0,,48073,00.html). Catherine Walter announced her resignation the following day. See National Australia Bank, "Statement by Catherine Walter, National Australia Bank Ltd Director", 6 May 2004 (available at http://www.nabgroup.com/vgnmedia/downld/CWalter_statement_060504.pdf).

414 See, for example, Martin Lipton and William Savitt, "The Many Myths of Lucian Bebchuk" (2007) 93 *Va L Rev* 733, 734, 748-749; Martin Lipton and Steven A. Rosenblum, "Election Contests in the Company's Proxy: An Idea Whose Time Has Not Come" (2003) 59 *Bus Law* 67, warning of the dangers of "balkanized and dysfunctional boards".

interests.[415] Supporters, however, echoing the view of Warren Buffett that there should be more dissent in the boardroom,[416] argued that she had fulfilled admirably the role envisaged for an independent director.[417]

5.3 The Coca-Cola Amatil Prenuptial Agreement

The NAB corporate governance dispute sent reverberations through the Australian commercial community, and demonstrated the power of shareholder opinion.[418] One commentator predicted that, following the NAB dispute, chairs would become even more conservative in their nomination of directors, to avoid similar intra-board conflicts.[419] Yet, some companies, including Coca-Cola Amatil and NAB itself, were already considering the adoption of a commercial device which could prove an even more powerful antidote to board disharmony: the prenuptial agreement.

Coca-Cola Amatil announced that in future, all non-executive directors would be required to sign a contract with the company prior to their appointment to the board. The central undertaking in this contract was that Coca-Cola Amatil would review the director's performance every two years, and if a majority of the board considered that performance unsatisfactory and requested the director to resign, the director agreed to

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415 See Stephen Bartholomeusz, "Shareholders to Decide Future of Bank's Board", *Sydney Morning Herald*, 20 April 2004, 21; Stephen Bartholomeusz, "Zero Tolerance of Board Errors a Lose-lose Trend", *Sydney Morning Herald*, 8 May 2004, 46.

416 See "Dissent Is Needed in the Boardroom - Higgs' Critics Have Failed to Grasp Why Change Is Needed", *Financial Times*, 10 March 2003, 20.

417 See, for example, Alan Kohler, "Take Two on 'Pre-nups' For Quiet Departures", *The Age*, 11 August 2004, 1. See also Amir N. Licht, "Legal Plug-Ins: Cultural Distance, Cross-Listing, and Corporate Governance Reform" (2004) 22 *Berkeley J Int'l L* 195, 224, describing the ideal independent director as "a person who is unrelated to the company's insiders with regard to family or business ties, who will insist on transparency and accountability from senior managers, and who is capable of openly challenging the chairperson and other members of the board…".

418 See Andrew Cornell and Stewart Oldfield, "Where NAB Went Wrong", *Australian Financial Review*, 8 May 2004, 20.

419 See Stephen Bartholomeusz, "Zero Tolerance of Board Errors a Lose-lose Trend", *Sydney Morning Herald*, 8 May 2004, 46. See also Andrew Cornell and Stewart Oldfield, "Where NAB Went Wrong", *ibid*, claiming that one of the lessons of NAB was that "major investors will not support mavericks on the board".

do so.[420] NAB and several other major Australian companies also considered introducing prenuptial agreements.[421]

The concept of prenuptial agreements provoked widespread controversy, and debate about whether they breached the provisions of the Australian *Corporations Act*. A major concern voiced was that the agreements constituted an illicit transfer of power from shareholders to the board. For example, the Australian Labor Party's then-shadow minister for financial services, Stephen Conroy, condemned prenuptial agreements on the basis that they "aim to erode shareholders' rights and avoid accountability".[422] In contrast, the chair of Coca-Cola Amatil claimed that the agreements were designed to enhance, rather than undermine, board accountability and performance, by strengthening the effectiveness of performance review.[423] Some commentators suggested, however, that the focus on failure to perform under prenuptials "was universally seen as code for 'toe the line'".[424]

Two key issues arose in the public debate concerning Coca-Cola Amatil's prenuptial agreements. First, were the agreements valid and legally binding and secondly, as a normative matter, should agreements of this kind be permitted under Australian law?

The appointment and removal of directors has traditionally been viewed as a core right of shareholders and the flip-side of centralized managerial control. While shareholders have no power to override managerial decisions of the board,[425] the

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420 See generally Stewart Oldfield, "Boards Seek Power to Sack Directors", *Australian Financial Review*, 20 July 2004, 1; Katherine Jimenez, "'Pre-nuptial Deal' Torn Up as Coke Bows to Investor Pressure", *The Australian*, 10 August 2004, 19.

421 See James McConvill, "Removal of Directors of Public Companies Takes Centre Stage in Australia: An Exploration of the Corporate Law and Governance Issues" (2005) 1 *Corp Gov L Rev* 191, 198-199.

422 See Michelle Grattan, "Director 'Prenuptials' Erode Shareholder Rights, Says ALP", *The Age*, 2 August 2004, 13.

423 *Ibid*.

424 Alan Kohler, "Moral Win to Walter, Say Peers", *Sydney Morning Herald*, 11 August 2004, 25.

425 See *Automatic Self Cleansing Filter Syndicate Co Ltd v Cuninghame* [1906] 2 Ch 34.

power of shareholders to remove directors from office reflects the basic corporate constitutional structure, in which shareholders exercise ultimate control.[426] It also provides an important buffer against managerial entrenchment.[427]

The provisions under the Australian *Corporations Act* on removal of directors from office reflect this fundamental principle. For proprietary companies, s 203C of the Act provides for the removal of directors by ordinary resolution, namely a resolution passed by simple majority of shareholders present and voting at the meeting, in person or by proxy.[428] However, s 203C is a replaceable rule only, and can be ousted or modified by the company's constitution.[429] For proprietary companies, it is therefore possible to displace this default rule with a provision in the constitution permitting the board to remove a director from office.[430]

The position is stricter in relation to removal of public company directors under Australian law. This scenario is covered by s 203D of the *Corporations Act*, which unlike its proprietary company counterpart,[431] is a mandatory, rather than a replaceable, rule. Section 203D(1) provides that shareholders in a public company may remove a director from office, despite anything in the company's constitution or

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426 See, for example, Richard M. Buxbaum, "The Internal Division of Powers in Corporate Governance" (1985) 73 *Cal L Rev* 1671, 1696, n110; Bernard Cartoon, "The Removal of Company Directors" [1980] *Journal of Bus L* 17, 17-18.

427 See *Allied Mining & Processing v Boldbow Pty Ltd* [2002] WASC 195, paras [47], [52].

428 For a discussion of the historical development of Australia's system of simple majority voting, and the rejection of a model of absolute majority voting voting, see I. M. Cameron, "Majority Rule; The Development of General Principle in Cases on Chartered Corporations" (1985) 15 *Melb U L Rev* 116.

429 Section 135(2) *Corporations Act* 2001 (Cth). Prior to the introduction of s 203C under the *Corporate Law Economic Reform Program Act* 1999 (Cth), no statutory removal power existed for proprietary companies, which were therefore required to rely upon a constitutional provision, such as Table A regulation 62(1). Table A regulation 62(1) stated that "the company may by resolution remove any director before the expiration of his period of office".

430 See Stephen Knight, "The Removal of Public Company Directors in Australia: Time for Change?" (2007) 25 *C&SLJ* 351, 353, citing *Hillig v Darkinjung* [2006] NSWSC 594 at [35] per Austin J for this proposition.

431 Section 203C *Corporations Act* 2001 (Cth).

any agreement between the director and the company or members.[432] Furthermore, s 203E clearly distinguishes removal of directors in a public company from a proprietary company context, by rendering void any action by the directors of a public company to remove a director, or require the director to leave office.[433]

As discussed earlier, s 203D was one of the Australian law provisions which News Corp's institutional investors sought unsuccessfully to include in the company's Delaware charter.[434] For public companies, one of the practical effects of s 203D is to prevent the use of staggered boards as an anti-takeover device in Australia.[435] This contrasts with Delaware law, where directors may be insulated from removal from office through the adoption of a staggered board structure, in conjunction with a norm of removal for cause in the case of a classified board.[436]

Did the Coca-Cola Amatil prenuptial agreement breach the provisions of s 203D or s 203E? The corporate regulator, the Australian Securities and Investments Commission ("ASIC"), considered that the agreements were in breach of the *Corporations Act* and thus void. In an Information Release on the issue, ASIC stated "[t]he *Corporations Act 2001* says that only shareholders can remove a director of a public company and that attempts by directors to remove another director from office

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432 Section 203D: "A public company may by resolution remove a director from office despite anything in:
(a) the company's constitution (if any); or
(b) an agreement between the company and the director; or
(c) an agreement between any or all members of the company and the director."

433 Section 203E: "A resolution, request or notice of any or all of the directors of a public company is void to the extent that it purports to:
(a) remove a director from their office; or
(b) require a director to vacate their office."

434 News Corporation Group, *Governance Article for New Delaware Parent Company: Preservation of Australian Public Investor Protection & Empowerment Provisions* (2004, on file with the author), 2.

435 An analogous provision, s 168 *Companies Act* 2006 (UK), also has the effect of preventing the use of staggered boards as an entrenchment and anti-takeover mechanism in the UK context.

436 Del. Code Ann, tit 8, s 141(k)(1).

are void".[437] Yet, the relevant provisions in the *Corporations Act* are surprisingly ambiguous, and the law concerning removal of a public company director from office is rather less certain than ASIC's terse statement would suggest. For example, while some commentators regard s 203D as providing the exclusive means by which directors of a public company may be removed from office,[438] there is recent caselaw rejecting this interpretation.[439] The history and wording of s 203D show that it is more focused on ensuring that shareholders have an unerodable,[440] rather than an exclusive, right to remove directors from office.[441] Also, historically it has been permissible for companies to provide in their constitutions for self-executing disqualifying events that will automatically terminate the office of director.[442]

The Coca-Cola Amatil prenuptial agreement did not purport to eliminate the right of shareholders to remove a director from office; rather it provided an additional mechanism for removal. Nonetheless, in the context of a board conflict such as the NAB dispute, the practical effect of the operation of a prenuptial agreement would be to shift power to the board, by preempting a decision by shareholders as to whether the director should be removed from office.[443]

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437 ASIC, Information Release IR 04-40, "Removal of Directors of Public Companies", 17 August 2004.

438 See Jean J. du Plessis and James McConvill, "Removal of Company Directors in a Climate of Corporate Collapses" (2003) 31 *Aust Bus L Rev* 251, 256, 264. Note, however, that McConvill expressly recants his original position on the interpretation of s 203D in a later article: see James McConvill, "Removal of Directors of Public Companies Takes Centre Stage in Australia: An Exploration of the Corporate Law and Governance Issues" (2005) 1 *Corp Gov L Rev* 191, 226-227.

439 See, for example, *Allied Mining and Processing v Boldbow Pty Ltd* [2002] WASC 195.

440 Yet, even in this respect, the courts have tolerated a range of techniques, including the use of weighted voting provisions in a company's constitution, which have effectively eroded shareholder power vis-à-vis directors. See generally, Nicholas Bourne, "The Removal of Directors" (2004) 25 *Bus L Rev* 194; Christopher L. Ryan, *Company Directors: Liabilities, Rights and Duties* (1987), 325*ff*.

441 See, for example, *Shanahan v Pivot Pty Ltd* (1998) 16 ACLC 859; *Link Agricultural Pty Ltd v Shanahan* (1998) 16 ACLC 1462. See also *Holmes v Life Funds of Australia Ltd* (1971) 1 NSWLR 860.

442 See generally Stephen Knight, "The Removal of Public Company Directors in Australia: Time for Change?" (2007) 25 *C&SLJ* 351, 355. See also Robert P. Austin and Ian M. Ramsay, *Ford's Principles of Corporations Law* (13th ed, 2007), [7.210].

443 Alan Kohler, "Take Two on 'Pre-nups' for Quiet Departures", *The Age*, 11 August 2004, 1.

There is a stronger argument however, that the proposed prenuptial agreements would breach s 203E of the *Corporations Act.* On a technical reading of s 203E, it could be argued that the director's vacation of office under a prenuptial agreement would arise not from any act of removal by the board, but simply from performance of the contract by the relevant director.[444] Yet, such an interpretation is tenuous. The prohibition in section 203E is not restricted to actions of board members which directly remove a director from office. It also includes actions of board members which "require" a director to vacate office.[445] There seems little reason why this provision should be interpreted narrowly to exclude from its ambit vacation of office pursuant to a contractual obligation triggered by a vote of no confidence by the board.[446] The predecessor to s 203E[447] explicitly stated that the prohibition on removal from office by the board existed "notwithstanding anything in the constitution *or any agreement*".[448]

The policy debate about prenuptial agreements is an apt one in the post-Enron era of independent directors and enhanced shareholder participation in governance.[449] On

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444 *Cf* James McConvill and Evan Holland, "'Pre-nuptial Agreements' for Removing Directors in Australia – Are They a Valid Part of the Marriage Between Shareholders and the Board" [2006] *J Bus L* 204, who support such an interpretation of s 203E and Stephen Knight, "The Removal of Public Company Directors in Australia: Time for Change?" (2007) 25 *C&SLJ* 351, 353-354.

445 Section 203E(b) *Corporations Act* 2001 (Cth).

446 Although note the decision in *Maloney v NSW National Coursing Association* [1978] 1 NSWLR 161, in which a similar provision to s 203E (s 120(8) of the former *Companies Act* 1961 (NSW)) was held not to invalidate a resolution that had the indirect effect of removing a director from office. For a discussion of this case, and its implications for the validity of prenuptial agreements under s 203E, see Stephen Knight, "The Removal of Public Company Directors in Australia: Time for Change?" (2007) 25 *C&SLJ* 351, 354-355.

447 Section 227(12) *Corporations Law*.

448 Section 227(12) *Corporations Law* stated "A director of a public company shall not be removed by, or be required to vacate his or her office because of, any resolution, request or notice of the directors or any of them notwithstanding anything in the constitution or any agreement." See generally Jean J. du Plessis, "Some Peculiarities Regarding the Removal of Company Directors" (1999) 27 *Aust Bus L Rev* 6.

449 James McConvill observes that the issue of removing directors initially received little attention in the post-scandal corporate governance debate, but that this changed dramatically following the conflict at NAB. See James McConvill, "Removal of Directors of Public Companies Takes Centre Stage in Australia: An Exploration of the Corporate Law and Governance Issues" (2005) 1 *Corp Gov L Rev* 191, 192-193. For further discussion of the

the one hand, prenuptial agreements potentially stifle the lone dissentient voice on the board. Supporters of prenuptial agreements argue, however, that they contribute to increased board accountability, since it is often practically difficult to remove underperforming directors.[450]

Australian law on removal of directors from office diverges from UK law in one important respect. In contrast to Australian law, which maintains a clear distinction between removal of directors of public and private companies, UK law makes no such distinction. A statutory power of removal was originally introduced in the UK in 1948[451] following the Cohen Committee Report,[452] to strengthen shareholder control over management by conferring power on shareholders to remove a director from office by ordinary resolution, irrespective of anything in the company's articles.[453] The UK statutory removal provision has at all times applied to public and proprietary companies equally.[454]

UK law also treats the statutory removal power as only one method of removing directors from office, and recognizes removal of directors based upon provisions in the articles as valid both for public and proprietary companies.[455] There is no restriction equivalent to s 203E of the Australian *Corporations Act*, prohibiting removal of a director of a public company by the board. In fact, it appears that UK companies routinely include a provision for the removal of a director by the board in

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policy considerations surrounding the involvement of the board in removing directors, see Stephen Knight, "The Removal of Public Company Directors in Australia: Time for Change?" (2007) 25 *C&SLJ* 351, 359-362.

450 McConvill articulates the tension between competing corporate governance aims in the debate over prenuptial agreements. He notes that critics of such agreements believe that they will undermine recent advances in corporate governance designed to enhance shareholder participation (*id*, 206-209). Supporters of the agreements, however, characterize them as a desirable corporate governance development, which will increase accountability and allow for effective peer review of directors (*id*, 209-211).

451 Section 184(1) *Companies Act* 1948 (UK).

452 *Report of the Committee on Company Law Amendment,* Cmd 6659 (HMSO, 1945).

453 See also Companies Bill, Second Reading, 16 November 1961, 2588, 2598-2599.

454 This removal power is now contained within s 168(1) of the *Companies Act* 2006 (UK).

455 See Nicholas Bourne, "The Removal of Directors" (2004) 25 *Bus L Rev* 194.

their articles,[456] specifically to address the type of situation that arose in the NAB controversy. UK commentators have pointed out that such a provision appears to be particularly common in the case of public companies "to enable directors to deal with conflict within the boardroom"[457] and to enable boardroom disputes "to be settled out of the public eye".[458]

Ultimately, in response to pressure from ASIC[459] and opposition by a number of fund managers, Coca-Cola Amatil announced that the proposed prenuptial agreements would not be implemented in their original form.[460] Rather, directors' letters of appointment would be amended to provide that, where a majority of the board considered a particular director's performance to be unsatisfactory, a motion for the director's removal from office would be put to shareholders at the next annual general meeting.[461] ASIC welcomed this amendment, while stressing the need for shareholders to be provided with full background information to enable informed participation[462] in the removal of directors under this revised model.[463] ASIC's interpretation of the Australian provisions dealing with removal of public directors from office also appears to have prompted some major companies to alter provisions

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456 See, for example, *Lee v Chou Wen Hsien* [1984] 1 WLR 1202, 1205, where the Privy Council states that the provision dates back to the 1902 edition of *Palmer's Company Precedents*.

457 Christopher L. Ryan, *Company Directors: Liabilities, Rights and Duties* (1987), 56.

458 Desmond Wright, *Rights and Duties of Directors* (1987), 19.

459 See ASIC, Information Release IR 04-40, "Removal of Directors of Public Companies", 17 August 2004.

460 Annabel Hepworth, "Coke Cans Pre-nuptials for Directors", *Australian Financial Review*, 10 August 2004, 1. NAB also announced that it would not introduce prenuptial agreements at that time.

461 See Alan Kohler, "Take Two on 'Pre-nups' for Quiet Departures", *The Age*, 11 August 2004, 1.

462 See Richard M. Buxbaum, "The Internal Division of Powers in Corporate Governance" (1985) 73 *Cal L Rev* 1671, 1679, stating that "[i]nformed participation is as important as participation per se" in corporate governance.

463 Annabel Hepworth, "Coke Cans Pre-nuptials for Directors", *Australian Financial Review*, 10 August 2004, 1.

in their constitution to ensure that they constitute self-executing disqualification of directors, rather than removal by the board.[464]

Conclusion

> "We used to joke that the problem with News Corp stock was half of the shareholders are afraid Rupert will die and the other half are afraid that he won't".
>
> John Malone[465]

The aim of this article has been to reconsider an embedded assumption of the convergence debate: that a unified common law corporate governance model exists. The article uses the migration of News Corp from Australia to Delaware as a case study for this assessment. News Corp's re-incorporation story is an ambiguous one. While News Corp asserted that the re-incorporation would enhance shareholder value, critics of the proposal claimed that its real purpose was to strengthen managerial power vis-à-vis shareholder power.[466]

The News Corp re-incorporation saga highlights a number of important differences between US and Australian corporate law rules relating to shareholder rights, and provides a valuable comparative law counterpoint to the recent US shareholder empowerment debate. Other recent Australian developments show the tension

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464 See, for example, Stephen Knight, "The Removal of Public Company Directors in Australia: Time for Change?" (2007) 25 *C&SLJ* 351, 355, discussing a constitutional amendment passed at the 2004 Annual General Meeting of shareholders of the Commonwealth Bank. The existing article stated that the directors could resolve to remove a director who had been absent from board meetings for at least six months. In the light of ASIC's comments about the prohibition on the board removing a director from office under s 203E, a shareholder resolution was passed altering the article so that it now provided that such an absentee director would automatically cease to hold office, "unless the Directors resolve otherwise".

465 Cited in Neil Chenoweth, "Malone's Ambitious Plan to Sneak up on Murdoch", *Australian Financial Review*, 18 October 2005, 1.

466 See, for example, Elizabeth Knight, "Murdoch Gymnastics Good for Investors", *Sydney Morning Herald*, 8 October 2004, 25, stating that the real reason for the move to Delaware may never be known.

between legal rules designed to enhance shareholder power, and commercial practices designed to readjust power in favor of the board of directors.

An assessment of News Corp's re-incorporation emphasizes the fact that, although there are many basic similarities between corporate governance in the US and Australia, there are, nonetheless, sufficient differences to make comparative analysis, in the tradition of Professor Gower, both fruitful and interesting.[467]

[467] See L.C.B. Gower, "Some Contrasts Between British and American Corporation Law" (1956) 69 *Harv L Rev* 1369, 1370, stating "if there are sufficient basic similarities to make a comparison possible, there are, equally, sufficient differences to make it fruitful."

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