COMPANIES AND SECURITIES LAW REVIEW COMMITTEE

Companies Act 1981 (Cwlth) Section 315 Compromise or arrangement with holders of options over company's unissued shares

The Companies and Securities Law Review Committee draws the attention of the Ministerial Council to the possible need to amend section 315 of the Companies Act 1981 (Cwlth) so that it will extend to a compromise or arrangement between a company and holders of options to take up unissued shares.

The Committee did not issue a discussion paper on this matter.

1. If section 315 did not exist, a company that wanted to make a binding compromise or arrangement with its creditors or members would have to obtain the agreement of all creditors or all members. Section 315 relaxes the requirements of the common law of contract by enabling a compromise or arrangement to be made binding on all creditors or all members when the proposal for compromise or arrangement has been approved by a special majority of creditors or members as specified in section 315(4) and has been approved by the Supreme Court.

2. A company that has issued options to take an allotment of shares in it may wish to make a compromise or arrangement with the option-holders. For example, it may wish to reduce its issued capital by cancelling a proportion of its issued shares and it may wish to make a reduction in the number of outstanding options. In another example, in a reconstruction it may be desirable to cancel all options and substitute options issued by a new holding company.

3. In Re Austamax Resources Ltd. (1985) 10 ACLR 194, 4 ACLC 76 and Re Asia Oil & Minerals Ltd. (1986) 5 NSWLR 42 the respective Courts decided ex parte that option-holders could be regarded as contingent creditors and as creditors within the meaning of section 315 but each Court expressed reservations.

In Re BDC Investments Ltd. (1988) 6 ACLC 85 Needham J, on a summons to convene meetings of option-holders doubted Whether an option-holder could be considered a contingent creditor. His Honour ordered meetings but directed that a copy of his judgment be made available to option-holders so that the point would stay open when the scheme (if passed by the option-holders) came back to the Court for approval. When the scheme later came before Young J. for approval ((1988) 13 ACLR 201, 6 ACLC 1196) his Honour doubted whether an option-holder could be called a contingent or prospective creditor but he approved the scheme because he did not think it appropriate in the particular case to let his doubts run against "the tide of decision, especially in an ex parte case where

it would appear that all persons involved are in a commercial sense completely satisfied with the result"

5. However, Young J. said (13 ACLR at 203, 6 ACLC at 1198):

"Because this is an area where the rights of a large number of people may be affected, I commend to those in charge of reviewing the Companies Code that they make the appropriate amendments to the Code to make the position plain one way or the other. To develop this point, the tension is between an individual's rights to hold on to his option no matter what on the one side, and the interests of commercial efficiency in permitting those who control companies to compulsorily acquire options held by minorities in the same way as they can under other provisions of the Code compulsorily acquire shares or compulsorily compel creditors to compound their debts."

6. Two situations deserve consideration. In one the company may wish to extinguish options or to vary their terms. In another situation the company may wish to extinguish shares or debentures or vary the terms on which shares or debentures are held but does not seek to vary the legal rights attached to options.

7. In the latter situation the company would be free to extinguish shares or debentures or vary their terms without reference to the option-holders : Hirsch and Co. v Burns (1897) 77 LT 377. Short of fraud, a company is free to reorganise its capital as it thinks fit, with such advantages or disadvantages as might ensue to option holders : Forsayth Oil and Gas NL v Livia Pry Ltd. (No 2) (1985) 9 ACLR 831 at 836, 3 ACLC 697 at 701, [1985] BCLC 378 at 384. It is not desirable to alter the principle that a company may make a compromise or arrangement with its members or creditors without reference to option-holders.

8. But there is a case for allowing a compromise or arrangement with option-holders to be within section 315. If that be accepted, there is a need to amend section 315 to remove the doubts that have been expressed. Consequential amendments would be needed in section 316 and in Schedule 9 to the Regulations.

9. Section 315(4) specifies the respective majorities required at meetings of creditors and meetings of members. For creditors, the majority required is a majority in number of creditors present and voting, being a majority whose debts or claims amount, in the aggregate, to not less than 75 per cent of the total amount of the debts and claims of creditors present and voting in person or by proxy. For members, the necessary majority is a majority in number of members present and voting, being, in the case of a company having a share capital, a majority whose shares have nominal values that amount, in the aggregate, to not less than 75 per cent of the total of the nominal values of all the shares of the members present and voting in person or by proxy. Section 315(4) also prescribes

an appropriate majority for a class of creditors or a class of members.

10. An option-holder occupies a special position different from that of a creditor or that of a member and it would seem appropriate to specify the required majority in terms congruent with the option-holder's special position. Thus, section 315(4)(a) might have added to it some such provision as:

"(iii) in the case of a compromise or arrangement between a company and holders of options or a class of such holders - the compromise or arrangement is agreed to by a majority in number of the holders, or of the holders included in that class of holders, present and voting, either in person or by proxy, being a majority whose options carry the right to be allotted shares having nominal values, that amount, in the aggregate, to not less than 75 per cent of the total of the nominal value of all shares that could be allotted under the options by virtue of which the holders present and voting are entitled to attend and vote; and"

11. A definition of "option" would be needed. It should comprehend a right to take up unissued shares in the company other than a right enjoyed by the holder under the terms of a debenture.

12. A holder of a debenture who has an option to take up shares by way of redemption has two capacities : one as creditor and one as option-holder. The definition of option should exclude options in the form of convertible debentures.

13. The Committee recommends an amendment to section 315 along the lines suggested above.

14. The Committee has under review the requirement in section 37(1)(c) that a company's memorandum must state an amount of share capital. If the Committee were to recommend the introduction of no par value shares and that recommendation were to be adopted, the provision now recommended and other parts of section 315 would need to be amended.

15. The Committee is of the view that there is a need to make the amendment now recommended without waiting for completion of the review of section 37(1)(c).

16. If the amendment to section 315 now recommended is made, it should not be necessary to amend Companies Regulations regulation 62 and Schedule 9 to the Companies Regulations.

Option-holders are not in a relationship to the company that is so close as that of members or creditors.

The prescription of disclosure and registration now in section 316 seems to be suitable for extension to, and adequate for, a compromise or arrangement with option-holders. It may be that the explanatory statement required under section 315 to be approved by the Court before circulation to option-holders for consideration prior to the relevant meeting need not contain all the details (set out in Schedule 9) which are required in the case of meetings of creditors or members. The legislation could provide that the statement in the case of meetings of option-holders should contain such information as the Commission reasonably requires, having regard to the particular facts of each case.

H A J FORD (Chairman)

G W CHARLTON

O A CRAWFORD

A B GREENWOOD

O R MAGAREY

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