Privy Council Appeal No. 3 of 1977

The Taupo Totara Timber Company Limited *Appellant*

v.

Darcy Kevin Rowe – – – – – – *Respondent*

FROM

THE COURT OF APPEAL OF NEW ZEALAND

JUDGMENT OF THE LORDS OF THE JUDICIAL COMMITTEE OF THE PRIVY COUNCIL, DELIVERED THE 28TH JUNE 1977

Present at the Hearing:

LORD WILBERFORCE
LORD HAILSHAM OF SAINT MARYLEBONE
LORD SIMON OF GLAISDALE
LORD FRASER OF TULLYBELTON

[*Delivered by* LORD WILBERFORCE]

This is an appeal from a Judgment of the Court of Appeal of New Zealand which reversed a decision of Moller J. in the Supreme Court in which he rejected the respondent's claim against the appellant company for a sum of $67,500 and interest. The issues for decision arise out of a service agreement between the respondent Mr. D. K. Rowe and the appellant company and depend, in the first instance and mainly, upon the construction of the agreement.

The respondent became a director of the company in 1964 and later held the post of General Manager. On 26 June 1969 an agreement was entered into between the company and Mr. Rowe by which he was appointed General Manager for a term of five years. The agreement contained a number of clauses as to which it is sufficient to say that they were substantially to the same effect as those contained in the agreement next to be mentioned. This circumstance is relevant to the question, later to be examined, whether the subsequent agreement was *intra vires* the company and its directors.

In December 1971 Mr. Rowe was appointed Managing Director: probably owing to the Christmas holiday period, the new agreement defining his position was not executed until 20 January 1972 and was sealed on 28 January 1972.

The agreement was expressed to be made between the company and Mr. Rowe, Managing Director "hereinafter called 'the employee'" and recited that it was desired to record in writing "the terms of his employment with the company". He was to be employed as Managing Director for a term of five years from 9 December 1971. There are three clauses particularly relevant to this appeal. These are:

"3. The employee may resign his office upon giving to the company not less than six months notice in writing of his desire to do so.

5. Notwithstanding that the terms of employment of the employee is for five years as aforesaid the directors shall be entitled to give to him notice of termination of his employment (for any cause whatsoever) and the remedy for any breach of this agreement by the company shall be in damages only so that the employee shall not continue in office contrary to the will of the directors of the Company.

7. Notwithstanding the foregoing provisions of this agreement, in the event of any person or other company or companies or any person or organisation or group of persons on their behalf acquiring either by means of a take-over offer or otherwise not less than 50% of the issued capital of the company, the employee shall be entitled at any time within a period of twelve months from and after the date of acquisition of capital as aforesaid, to resign his office upon giving to the company not less than three months notice in writing of his desire to do so. Should the employee resign his office pursuant to the right conferred on him by, and in the circumstances as mentioned in this paragraph 7 hereof, or should he receive from the company at any time during the said period of twelve months, notice of termination of his employment for any cause whatsoever then and in either such case the employee shall be entitled to receive from the company (in addition to any superannuation benefits or other rights to which he is entitled) on the date on which he ceases to be employed by the company and the company shall pay to the employee on that date, a sum of money equivalent to five times the gross annual salary being paid by the company to the employee immediately prior to the date of the acquisition of such share capital of the company as aforesaid and it is expressly declared that all income and other taxes on the sum of money to be paid to the employee pursuant to this paragraph 7 shall be payable by the company to the end and intent that the said sum of money will not be taxable in the hands of the employee at any time after the date of the receipt thereof by him."

Clause 7, as can be seen from its terms, was evidently drafted with the object of providing for the possibility of a take-over of the company. This in fact came about. On 28 January 1972 a take-over proposal was made on behalf of N.Z. Forest Products Ltd. The company's directors decided to recommend acceptance on 20 April 1972. The take-over became effective on 23 August 1972 by virtue of a transfer of shares in the company to N.Z. Forest Products Ltd. on that date. Thus the twelve months period contemplated by Clause 7 would expire on 23 August 1973.

On 28 May 1973 the respondent wrote to the company's Chairman a letter which contained this paragraph:

"I wish to tender my resignation as Managing Director of this Company and as a Director of Subsidiary Companies under its control to take effect as at the 31st August, 1973, in terms of my service agreement duly executed under the Seal of the Company, a copy of which is held by N.Z. Forest Products Ltd."

On 25 July the Company, by its then Chairman, wrote to the respondent a letter which contained the following:

"I have to advise you that the Board has, with regret, accepted your resignation to take effect as at 31st August, 1973 as requested by you in your letter giving notice of resignation.

. . . . . .

I must, however, advise you that the Board has noted that the terms of your notice of resignation preclude you from entitlement to receive the lump sum payment on resignation which is provided for in Clause 7 of your service contract with the Company dated 20th January, 1972 in the event of resignation taking place in accordance with the conditions contained in the clause. This interpretation may well conflict with your expectation in the matter so that I must inform you that Queen's Counsel's opinion has been secured confirming this view."

On 6 August 1973 a notice was displayed stating that the respondent had submitted his resignation effective from 31 August 1973.

Thus the facts are that the respondent's notice of resignation was given within the twelve months period; that it was for not less than three months; that it expired after the twelve months period. So was it valid, or invalid, under the terms of Clause 7 of the agreement so as to entitle him to a sum equal to five years' salary? The question is by no means as easy to answer as to state, and the Courts have taken different views upon it.

It is first necessary to consider the purpose of the provisions in Clause 7. Broadly, it was to provide for the possibility that, after a take-over of the company, which would be likely to involve a change of control and direction, the employee, either in his own view or in that of the company, might not fit into the new organisation. The clause appears to contemplate a period of twelve months during which either side would be expected to decide whether the employee should stay or quit. However, one of the consequences of the company's contention that notice must take effect within the twelve months is that the employee in reality only has nine months in which to decide. This appears to their Lordships as a substantial argument against that contention, but it must of course be weighed against difficulties the other way and against the meaning of the language used.

The critical phrase is " to resign his office upon giving to the company not less than three months notice in writing of his desire to do so ". Does this contemplate two events (notice and effective resignation) both of which must occur within the twelve months, or only one (notice of resignation)?

A comparison of this phrase with other clauses suggests the latter. Clause 3, on a natural reading, suggests that the employee resigns upon, *i.e.* by, giving six months notice—it is the notice that is the resignation, not the expiration of the period set. Similarly in Clause 5 the natural implication is that the employment is terminated by the notice—not thereafter. In Clause 7 itself any notice of termination by the company, given at any time during the twelve months period, entitles the employee to receive the payment there provided for. All this suggests that, in the case of the employee, what is required, and only required, is a notice of resignation within the period. As is pointed out by Cooke J. in his judgment there is respectable support in books of precedents for reading " on ", or (which must be the same) " upon ", as meaning " by ".

This interpretation, as does that of the company, produces possible anomalies which their Lordships do not minimise. Particularly, if it is right, the employee could delay giving notice until the end of the twelve months period and then give his notice, which need not necessarily be as short as three months. Whether in that event he could claim salary as well as the compensation, or whether the company could terminate his employment, may be obscure. But—in this their Lordships agree with the Court of Appeal—contracts such as these, which are evidently loosely

drawn, ought not to be interpreted by reference to extreme cases which neither side, nor the draftsman, may have thought of. Preferable guides are the natural meaning of the language, and the business sense of the contract. Their Lordships, recognising that this is a matter of impression, which admits and even invites a division of view, on the whole prefer the interpretation accepted by all three members of the Court of Appeal. This being the conclusion it is not necessary to deal with an alternative submission of the respondent that the employment was " terminated " by the company in July 1973.

It next becomes necessary to consider the appellant's contention that payment of the sum claimed by the respondent would be unlawful by virtue of s.191 of the Companies Act 1955. This is as follows:

> " 191. *Approval of company requisite for payment by it to director for loss of office, etc.*—It shall not be lawful for a company to make to any director of the company any payment by way of compensation for loss of office, or as consideration for or in connection with his retirement from office, without particulars with respect to the proposed payment (including the amount thereof) being disclosed to members of the company and the proposal being approved by the company in general meeting."

This section is identical with s.191 of the Companies Act 1948 (U.K.) and, with one qualification, with s.129 of the Companies Act 1961 (Victoria). That qualification is that the Victorian section adds, after " compensation for loss of office ", the words " as director ", and refers to " retirement from *such* office ".

These changes may be either clarificatory or restrictive. Since there is no obvious reason why Australian legislatures should wish to narrow the scope of the section, the former alternative seems the more likely. The belief of the draftsman as to what the section was intended to mean is of course not decisive.

The New Zealand section raises two questions. First whether it extends to payments made to persons who are directors in connection, not simply with the office of director, but also with some employment held by the director. Secondly whether it applies to payments which the company is obliged, under contract, to make, or is limited to payments which the company, not being obliged to make, proposes to make. Although the section deals first with " compensation for loss of office ", which is a well enough known type of transaction popularly described as a golden handshake, it is said that in continuing with a reference to payments as consideration for, or in connection with, retirement from office, the section is casting a wider net, capable of including contractual payments.

There is only one reported case, to their Lordships' knowledge, in which these points have been considered: the Victorian case of *Lincoln Mills (Aust.) Ltd. v. Gough* [1964] V.R. 193, a case like the present concerned with a managing director. Hudson J. gave a careful judgment, the relevant part of which is fully quoted by Richmond P., in which he decided, on both the points above mentioned, that the payment was not illegal.

Their Lordships agree with the judgment of Hudson J., and, although unassisted by the additional words appearing in the Victorian statute, would apply it to the present case. Mr. Rowe, as well as being a director, was an employee, and, as other employees with this company, had the benefit of a service agreement: he was described as " employee " in it. In certain events, which might not happen, he could become contractually entitled to a sum of money, on resignation or dismissal, the amount of which was not fixed by the agreement and could only be

ascertained if and when the event happened. The directors had full power under the Article 116 to appoint him as Managing Director on such terms as they thought fit. There was no obligation on them to seek approval of this agreement by the company in general meeting: to do so indeed would be both unusual and possibly undesirable. Then, if the agreement was, as (subject to any point as to *vires*—see below—) it undoubtedly was, valid in itself, does s.191 require the directors to seek the approval of a general meeting for carrying it out? Presumably this approval would be sought at a time when the obligation to make the payment had arisen and when its amount was known, but meanwhile the position of the employee would be uncertain and difficult. In their Lordships' view the section imposes no such requirement. The section as a whole read with sections 192 and 193 which are in similar form and the words " proposed payment " and " proposal " point to a prohibition of uncovenanted payments as contrasted with payments which the company is legally obliged to make. Their Lordships note that this contrast is drawn by the authoritative Report of the Jenkins Committee (1962) Cmnd. 1749 para. 93: there is also text book support for it. Their Lordships on this point also agree with the Court of Appeal.

There remains an argument based upon *vires*. It was suggested that the agreement was *ultra vires* the company or *ultra vires* the directors of the company. Their Lordships cannot accept either of these contentions. There can be no doubt as to the general power of the company to engage servants and to enter into service agreements with them. There is no question as to the *bona fides* of the directors in entering into this particular agreement. It was shown that similar agreements had been entered into with other employees and that to do so had been the company's policy for several years. The view that inclusion of a provision giving protection in the event of a take-over was in the interests of the company, was clearly one that reasonable and honest directors might take. In its absence, the staff might be likely to go elsewhere. In the case of Mr. Rowe, as has been noted, an agreement in substantially similar form had been entered into in 1969 and there could be nothing suspicious, or open to criticism, in replacing that agreement in 1972 when he became Managing Director. As has been pointed out, there is explicit power in the Articles to appoint a Managing Director on such terms as the directors—acting of course *bona fide*—think fit. These points therefore fail.

Their Lordships will humbly advise Her Majesty that the appeal be dismissed. The appellant must pay the costs of the appeal.

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In the Privy Council

THE TAUPO TOTARA TIMBER COMPANY LIMITED

v.

DARCY KEVIN ROWE

DELIVERED BY

LORD WILBERFORCE

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