CASE NOTES CASE NOTES CASE NOTES CASE NOTES CASE

NEW SOUTH WALES v. COMMONWEALTH (The Corporations Act Case)[1]

By Garrie Moloney

Given the recent trend in judicial interpretation of the scope of the corporations power in s. 51(20) of the Commonwealth Constitution, the Commonwealth and its Parliamentary counsel had reason to feel confident that federal power extended to the complete regulation of Australian trading and financial corporations, and foreign corporations, including in the case of trading and financial corporations, their incorporation, internal management and operations, and winding-up. The Corporations Act 1989 (Cth) is designed to impose a new national law for the regulation of corporations to replace the co-operative scheme between the Commonwealth and the States which has governed companies since 1981.

Section 51(20) of the Commonwealth Constitution, upon which the Corporations Act largely relies for its constitutional validity,[2] empowers the Commonwealth Parliament to make laws "with respect to ... foreign corporations, and trading or financial corporations formed within the limits of the Commonwealth". In the last twenty years the High Court has adopted a progressively expanding notion of the scope of this power. In 1971, in *Strickland v. Rocla Concrete Pipes Ltd* ,[3] the High Court, overruling its earlier decision in *Huddart Parker & Co. Pty Ltd v. Moorehead*,[4] had accepted that the power extended to regulating and controlling the trading activities of trading corporations. The Court also upheld Commonwealth power to legislate to protect the business of a s. 51(20) corporation from activities of others calculated to cause harm to that business[5] and in the landmark *Tasmanian Dam Case*[6], it was held that the Commonwealth could control any non-trading activity of a s. 51(20) corporation undertaken for the purposes of its trade. In that case there are, in the majority opinions, some suggestions that the Court would

1. Unreported, High Court of Australia, 6th February, 1990.
2. There are of course other heads of power upon which the Commonwealth can depend to support certain aspects of this national legislation: for example, s. 51(8) (the 'banking' power), and s. 51(17) (the 'insolvency' power). Moreover, under s. 122 (the 'territories' power), the Commonwealth has plenary power over companies organised and operating within a Commonwealth Territory, including the power of incorporation.
3. (1971) 124 CLR 468.
4. (1909) 8 CLR 330.
5. *Actors and Announcers Equity Association v. Fontana Films Pty Ltd* (1982) 150 CLR 169.
6. *Commonwealth v. Tasmania* (1983) 158 CLR 1.

eventually accept the proposition that the power extends the regulation of any activity of those corporations specified in s. 51(20).[7]

None of these cases, however, was concerned with the question of the Commonwealth's power over incorporation [8] and continuing doubts have existed as to whether or not a Commonwealth law could control the incorporation, and internal affairs of s. 51(20) corporations. The view that incorporation of trading and financial corporations is not a matter upon which the Commonwealth can validly legislate is based primarily upon the wording of s. 51(20) itself, which speaks of trading of financial corporation *formed within the limits of the Commonwealth.* This phrase has been taken to restrict the Commonwealth's power to the regulation of corporations which are already in existence in accordance with some other law. [9] Moreover, in *Huddart Parker & Co. Pty Ltd v. Moorehead,*[10] all members of the Court had declared that the power did not extend to the creation of corporations.

It was against this constitutional background that New South Wales, South Australia and Western Australia challenged those provisions of the Corporations Act which provided for the registration of companies.[11] By a majority of 6 to 1, the High Court upheld the States' challenge holding that all the challenged provisions were invalid.[12] The joint judgment of the majority applied the conclusion reached in the earlier *Huddart Parker Case* that the Commonwealth lacked the power under s. 51(20) to legislate for the incorporation of companies. Its power is limited to those already formed corporations answering the description of foreign, trading or financial corporations.

The reasoning of the majority was based upon the language of the s. 51(20) itself, its history, contemporary interpretations and precedent. It was accepted that the phrase "formed within the limits of the Common-

7. Ibid., 148 per Mason, J; 179 per Murphy, J and 269–272 per Deane, J. See also A.F. Mason, "The Australian Constitution 1901–1988" (1988) 62 *Australian Law Journal* 752, 757; G.J. Lindell, 'The Corporations and Races Powers' (1984) 14 *Federal Law Review* 219, 252 and D. Rose's Commentary, (1984) 14 *Federal Law Review* 253, 254.
8. In the *Actors Equity Case* (1982) 150 CLR 169, 212, Murphy J asserted, by way of dictum, that the corporations power included the power to incorporate trading and financial corporations; see also *Kathleen Investments (Australia) Ltd v. Australia Atomic Energy Commission* (1977) 139 CLR 177, 199 per Murphy J.
9. Howard, *Australian Federal Constitutional Law* (3rd edn 1985) 471.
10. (1909) 8 CLR 330.
11. The particular sections under challenge were ss. 112 and 113 which sought to prohibit the formation of 'outsize' unincorporated partnerships or associations; ss. 114–125 which deal with incorporation by registration and the investiture of a corporation incorporated under the Act with the usual functions attaching to legal personality; ss. 155–158 which sought to require "companies" seeking incorporation to file an "activities" statement and incorporated companies thereafter annually to file such statements. These statements would have required a company to establish that it was, or would be, engaged in trading, financial or interstate banking activities. Where a company could not make that statement, it would either be refused registration under the Act or else have its registration cancelled.
12. The majority were Mason, CJ, Brennan, Dawson, Toohey, Gaudron and McHugh, JJ. Deane, J dissented.

wealth" was intended to distinguish local corporations from foreign ones but that it also operated to impose a limitation on the scope of the power, namely that it extended only to laws with respect to already formed corporations. On this point, the majority said:

> The word 'formed' is a past participle used adjectivally, and the participial phrase 'formed within the limits of the Commonwealth' is used to describe corporations which have been or shall have been created in Australia. The subject of a valid law is restricted by that phrase to corporations which have undergone the process of formation in the past, corporations. That being so, the words 'formed within the limits of the Commonwealth' exclude the process of incorporation itself.[13]

The introductory words, 'with respect to' despite their wide import do not, according to the majority, effect any expansion of the power in s. 51(20) to cover the formation of corporations.[14]

The history of the paragraph was taken by the majority to confirm their interpretation. They reaffirmed the legitimacy of the Court using the Convention Debates "to establish the subject to which the paragraph was directed" and the various drafts of the Constitution to assist in the construction of one of its provisions.[15] The successive drafts of s. 51(20) spoke of companies 'formed in any State or part of the Commonwealth'. 'Formed' in these drafts was taken to have meant 'which have been formed' and this was confirmed by Sir Samuel Griffith's rejection, as inappropriate, of a specific suggestion to amend the paragraph to cover incorporation at the 1891 Convention.[16]

Surprisingly, the majority also relied upon the unanimous dicta in the *Huddart Parker Case* that the power did not extend to incorporation as the central judicial support for the narrow interpretation, despite that case having been decisively overruled in *Strickland* and emphatically rejected by Mason J in *The Tasmanian Dam Case.*[17] The majority dismissed the Commonwealth's submission that the *Huddart Parker Case* was so infected by the reserved powers heresy as to be a worthless authority on any point. Their reason was that the conclusion on the incorporation point was arrived on the basis of 'purely textual considerations'. They were comforted further by the 'unequivocal' acceptance of the narrow interpretation by Isaacs J who was the sole dissentient in the *Huddart Parker Case* and who did not adhere to the reserved powers doctrine.[18] Moreover, the rejection of the case in *Strickland* did not include a negation of the Court's view on the incorporation point.[19]

13. High Court Pamphlet, 4.
14. Ibid., 4–5.
15. Ibid., 9 applying the dicta in *Cole v. Whitfield* (1988) 165 CLR 360, 385; *Port MacDonnell Fishermen's Association Inc. v. South Australia* (1989) 63 ALJR 671, 683 and *Tasmania v. Commonwealth and Victoria* (1904) 1 CLR 329, 333.
16. High Court Pamphlet, 9–10. This view of the proper meaning of s. 51(20) was consistent with the contemporary opinion expressed by Quick and Garran in their *Annotated Constitution of the Australian Commonwealth* (1901) 607.
17. (1983) 158 CLR 1, 147; Mason J did recognise that Isaacs J was the only member of the Court not to take, in one way or another, a very restricted view of the operation of the power but he also highlighted Isaacs J's opinion that the powers did not extend to cover the internal management of companies.
18. High Court Pamphlet, 6.
19. Ibid., 7.

The final ground of the majority's reasoning focuses upon a supposed practical impediment to a wider construction of the power. Accepted principle provides for the determination of whether a company is a trading or financial corporation to be based on its actual or intended activities. The majority, therefore, considered that the potential for the status of a particular corporation to vary from one point of time to another made 'it less likely at least that s. 51(xx) was intended to confer power upon the Commonwealth to incorporate companies over which its power of regulation might fluctuate, possibly without knowledge upon either side'.[20]

Deane J, in a more tightly reasoned opinion, dissented. He rejected the textual argument on three grounds. First, the States' argument that until a trading or financial corporation is 'formed', it does not exist as the subject-matter of the power failed to distinguish between what he called the "abstract subject-matter of the legislative power and concrete instances of that subject-matter". By way of example, he said that the States' construction would mean that a legislative power with respect to locally manufactured motor vehicles would not cover laws concerning the local manufacture of those vehicles or a power over lighthouses would not permit the regulation of their construction. The power can only be activated once those objects are in existence — a construction which he regarded as unsound.[21] Secondly, the States contention ignored the true effect of the introductory words, 'with respect to' which required that par. (xx), which is a constitutional grant of plenary power, be liberally not narrowly or technically, construed'.[22] Thirdly, Deane J preferred to treat the phrase 'formed within the limits of the Commonwealth' as intended only to distinguish local corporations from foreign ones. It, therefore, did not, as a matter of grammar, impose any temporal limitation on the power. On this point, he said:

> In the context of the use of the phrase 'formed within the limits of the Commonwealth' in contradistinction to 'foreign', the word 'formed' is properly to be understood as representing a use of the past participle as part of an adjectival phrase which is without temporal significance... When the word is so understood it affords no basis for excluding the formation or incorporation within the limits of the Commonwealth of trading or financial corporations from the scope of the legislative power granted by the second limb of par.(xx). To the contrary, it tends to focus attention upon that aspect of the grant of power.[23]

20. Ibid., 11.
21. Ibid., 15.
22. Ibid.
23. Ibid., 16. Deane J also read the power as permitting the Commonwealth to regulate the local 'incorporation' of foreign corporations within the Commonwealth; *Ibid*, 15. On this point, he said: [I]t appears to me to be plain that para.(xx)'s grant of legislative power with respect to foreign corporations cannot properly be confined to exclude the power to make laws defining the circumstances and establishing the procedures under and by which artificial entities invested with corporate personality under other systems of law may acquire or enjoy such personality under the law of this country. This dictum was offered as a refutation of the argument that as the power could not be concerned with the creation of foreign corporation, consistently it could not support the creation of trading or financial corporations: see the joint judgment, ibid., 5. With respect, Deane J's comments appear to blur the distinction between the incorporation of foreign corporations and their local recognition.

He also dismissed the majority's reliance upon *Huddart Parker* which he described colourfully as having been 'disinterred and dissected for the occasion'. He regarded the reasoning of the majority in *Huddart Parker* as so permeated by fundamental errors in the proper mode of constitutional interpretation that the dicta concerning incorporation could not be legitimately salvaged.[24] Similarly, he rejected the dictum of Isaacs J on the basis that the reasons to support it were wrong.[25] As for the historical materials and contemporary interpretations, he concluded that the few references in the Convention Debates were not 'compelling'. Furthermore, there were other contemporary authors who advanced opposing views to that of Quick and Garran, upon whom the majority had relied.[26] He was also at pains to denounce the improper use of extrinsic materials in the interpretation of the Constitution. On this fundamental point, he stated that it is impermissible 'to constrict the effect of the words which were adopted by the people as the compact of a nation by reference to the intentions or understandings of those who participated in or observed the Convention Debate.[27] He dismissed the convenience argument accepted by the majority on the grounds that it is one more directed to the exercise of the power by Parliament than to the proper scope of its legislative power under s. 51(20) and that the advantages of national companies legislation 'overwhelmingly outweigh the alleged inconvenience.'[28]

In the absence of a suitable intergovernmental solution to the problem created by the deficit in Commonwealth power exposed by the majority, the Commonwealth Attorney-General has indicated that the Corporations Act will be amended to remove the invalid provisions.[29] The reasoning of the majority may, however, infiltrate further into the Act than simply the provisions which were specifically struck down by the Court. The Commonwealth Attorney-General has stated that the majority decision does not affect other provisions of the Act covering the registration and regulation of companies once they have been incorporated under another law. This, however, may be rather too optimistic and may ignore the underlying consequences of the majority's reasoning. There are respectable arguments that if the Commonwealth lacks the power to legislate for the incorporation of s. 51(20) corporations, then, it also lacks the power, to some extent, to control their internal administration and structure (aside from those matters which are incidental to their trading, and financial activities) and, under s. 51(20), their dissolution. To assign to the States only the power over incorporation of trading and financial corporations, it is argued, would result in an absurd and artificial division of powers, with the power over incor-

24. Ibid.
25. Ibid., 20–22.
26. Ibid., 22 citing W. Harrison Moore, *The Constitution of the Commonwealth of Australia* (1902) 148.
27. Ibid., 22.
28. Ibid., 23–24.
29. *Australian Financial Review* (Sydney) 12 Feb., 1990.

poration reduced to a mere matter of formality.[30] Again, all the members of the Court in *Huddart Parker*, including Isaacs J, concluded that the Commonwealth lacked power to control the internal affairs of s. 51(20) corporations. While it may be possible to dismiss the majority opinions on this point as based upon reserved powers notions, it is more difficult to ignore Isaacs J's similar conclusion now that the High Court has endorsed his conclusion on the incorporation point. As Deane J perceptively observed, any fair reading of Isaacs J's judgment indicates that his conclusion that the power did not extend to control a company's internal procedures or management influenced his conclusion on the formation point.[31] To accept Isaacs J's reasoning on the formation point as valid because it was based only on a textual analysis, but to reject the remainder of his related conclusions on the scope of the power to deal with internal company matters is, it is submitted, altogether too artificial a reading of his opinion. On these points, either all the reasoning is correct or none of it. Professor Zines has suggested a less drastic result may flow if the Commonwealth lacks the power of creation under s. 51(20). In his opinion, "it is not an unreasonable argument that those matters which are part and parcel of creating a corporation and without which the corporation would be an empty shell, incapable of functioning as juristic person at all, are similarly outside Commonwealth power.[32] Even if this proposition is applied, it is not entirely clear that only those sections of the Corporations Act which were invalidated by the Court are affected.

Moreover, the decision of the majority must call into question those provisions of the Act dealing with winding-up which rely on s. 51(20) for their validity. It would be odd if the proper division of power between the Commonwealth and States denied the Commonwealth the power to regulate the formation of trading and financial corporations but allowed it the power to control their destruction.[33]

30. See, for example, P.H. Lane, "Corporations — Can there be a Commonwealth Companies Act?" (1972) 46 *Australian Law Journal* 407. Cp the contrary views of O.I. Frankel and J.L. Taylor, "A 1973 National Companies Act? The Challenge to Parochialism" (1973) 47 *Australian Law Journal* 119 and G. Winterton, "Comment on Section 51(xx)" (1984) 14 *Federal Law Review* 258, 261.
31. High Court Pamphlet, 20.
32. L. Zines, *The High Court and the Constitution* (2nd edn 1987) 89.
33. Ibid.