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The Proper Purpose Rule as a Constraint on Directors' Autonomy –

Eclairs Group Limited v JKX Oil & Gas plc

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The recent case of *Eclairs Group Limited v JKX Oil & Gas plc* highlights the pressures faced by company directors in change of control situations, in which they may be tempted to take action to prevent or discourage such change. The Supreme Court decision provides important clarity on the scope of the proper purpose rule in these (and other) situations. We explore the implications of different judicial interpretations of the proper purpose rule for the autonomy of directors in their decision making. We do this by focusing on the scope of the proper purpose rule, whether a subjective or objective test is employed in the application of the rule and the test for causation where a director is motivated by mixed purposes.

INTRODUCTION

Directors, as fiduciaries, are subject to duties and constraints to ensure they act in the interests of the company. One of these is the proper purpose rule, now codified in section 171(b) of the Companies Act 2006. This section provides that a director of a company must only exercise powers for the purposes for which they are conferred. Debate about the scope and contours of the proper purpose rule is longstanding and has featured prominently in earlier volumes of this journal.¹ The scope of the rule

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¹ See, eg, J. R. Birds, 'Proper Purpose as a Head of Directors' Duties' (1974) 37 MLR 37; B.V. Slutsky, 'Canadian Rejection of the Hogg v Cramphorn "Improper Purposes" Principle – A Step Forward?' (1974) 37 MLR 457; S. J. Burrige, 'Wrongful Rights Issues' (1981) 44 MLR 40; S. Worthington, 'Reforming Directors' Duties' (2001) 64 MLR 439.

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was the key aspect of the decision of the Supreme Court of the United Kingdom in *Eclairs Group Limited v JKX Oil & Gas plc*.²

This case assumes particular importance in our understanding of the proper purpose rule, especially due to the different interpretations regarding the scope of the rule expressed by the Court of Appeal and the Supreme Court. The majority of the Court of Appeal provided a narrow interpretation of the rule. A much broader interpretation was provided by the Supreme Court. In the words of Lord Sumption,

The rule that the fiduciary powers of directors may be exercised only for the purposes for which they were conferred is one of the main means by which equity enforces the proper conduct of directors. It is also fundamental to the constitutional distinction between the respective domains of the board and the shareholders.³

Our focus is on the implications for the autonomy of directors of different judicial interpretations of the proper purpose rule. We discuss three issues relating to the interpretation of the rule that have important consequences for whether directors have broad or narrow autonomy in their decision making. These are the scope of the proper purpose rule, whether an objective or subjective test is employed in the application of the rule and the test for causation where a director is motivated by mixed purposes.

The structure of this note is as follows. First, the facts and the outcomes at each stage of the litigation are outlined and attention is drawn to notable aspects concerning the source and nature of the proper purpose rule. Our main focus is, however, on the degree of autonomy allowed to directors by the proper purpose rule, particularly in situations of changing control. With this as our theme, we examine the three issues identified above.

FACTS AND DECISION

² [2015] UKSC 71 (*Eclairs* (SC)).

³ *ibid* at [37]. As to whether the proper purpose rule is properly classified as a duty see, eg, D. Kershaw, *Company Law in Context – Text and Materials* (Oxford: OUP, 2nd ed, 2012) 404-405. A. Keay, *Directors' Duties* (Bristol: Jordan Publishing, 2nd ed, 2014) para 5.11.

The background to the decision of the Supreme Court in *Eclairs Group Limited v JKX Oil & Gas plc* was a suspected corporate raid. This is a classic scenario for the engagement of the proper purpose rule, as key cases concern the issuing of shares or other defensive actions by target company directors when confronted with a hostile takeover.⁴

Article 42 of the constitution of JKX Oil & Gas plc (JKX) empowered the board to serve a notice inquiring into interests in shares in the company and also to impose restrictions in relation to voting and transfer of those shares, where information about interests in shares was not accordingly provided, or the response was known to be materially false or incorrect or there was reasonable cause to believe that it was false or materially incorrect.⁵ In 2013, in response to a suspected corporate raid by two shareholders (Eclairs Group Ltd (Eclairs) and Glengary Overseas Ltd (Glengary)), who together held 39 per cent of the shares in JKX, the board of JKX served notices on Eclairs and Glengary and their controllers seeking disclosure of information. The responses admitted the existence of interests in the shares but denied that there was any agreement or arrangement between the shareholders.

The JKX board believed that the responses received were false or materially incorrect and therefore imposed restrictions that prevented the voting and transfer of the Eclairs and Glengary shares. This occurred two days before JKX's annual general meeting (AGM), at which, to the board's knowledge, Eclairs and Glengary were intending to oppose resolutions relating to the re-election of certain directors and approval of the directors' remuneration report. Eclairs had in fact publicly invited shareholders to oppose the resolutions proposed at the AGM via an advertisement in the Financial Times.

The effect of the restrictions was to prevent Eclairs and Glengary from voting to oppose the resolutions. Eclairs and Glengary challenged the restriction notices on the basis of section 171(b) of the Companies Act 2006. It was contended that the only proper purpose for which the power could be

⁴ See *Eclairs* (SC) n 2 above at [37]. Examples include *Howard Smith Ltd v Ampol Petroleum Ltd* [1974] AC 821; *Hogg v Cramphorn Ltd* [1967] Ch 254; *Harlowe's Nominees Pty Ltd v Woodside (Lakes Entrance) Oil Co NL* (1968) 121 CLR 483; *Teck Corp v Miller* (1973) 33 DLR (3d) 288.

⁵ See also Companies Act 2006, ss 793-797, although note that article 42 went beyond the statutory provisions.

exercised was to extract the information, and that the real purpose of the board had been to ensure the passing of the resolutions at the forthcoming AGM.⁶

At first instance Mann J set aside the restrictions on the basis that the predominant purpose of the majority of the board was to prevent the shares being voted in order to maximise the prospects of the resolutions being passed and that this was an improper purpose.⁷ This order was reversed by the Court of Appeal on the basis that the power to impose restrictions in article 42 was not subject to the proper purpose rule.⁸ The Supreme Court restored the order of Mann J, holding that the operation of article 42 was subject to the proper purpose rule and that using the power for the predominant purpose of influencing the outcome of the general meeting was an improper purpose.⁹ Following the Supreme Court decision, a majority of the directors of JXX were removed at a specially convened meeting of shareholders.¹⁰

The Supreme Court affirmed that the proper purpose rule is fiduciary in character and is one of the main means by which equity enforces the proper conduct of directors.¹¹ The Supreme Court also reaffirmed the separation of the proper purpose rule and the duty to act in good faith in the interests of the company (now the statutory duty to promote the success of the company for the benefit of the members as a whole in section 172 of the Companies Act 2006).¹²

⁶ See *Eclairs (SC)* n 2 above at [8].

⁷ *Eclairs Group Ltd v JXX Oil & Gas plc* [2013] EWHC 2631 (Ch) (*Eclairs (HC)*).

⁸ *JXX Oil & Gas plc v Eclairs Group Ltd* [2014] EWCA Civ 640 (*JXX Oil*).

⁹ *Eclairs (SC)* n 2 above.

¹⁰ ‘JXX board toppled by Russian investor’ *The Financial Times* 28 January 2016 (online edition).

¹¹ *Eclairs (SC)* n 2 above at [37]. For differences between the proper purpose rule and the doctrine of fraud on a power see F. J. Ranero, ‘Managed Investment Schemes: The Responsible Entity’s Duty to Act for a Proper Purpose’ (1999) 17 CSLJ 422, 427, 429; R. T. Langford, *Directors’ Duties – Principles and Application* (Sydney: Federation Press, 2014) 128-129.

¹² *Eclairs (SC)* n 2 above at [36]. For discussion see M. Conaglen, ‘Fiduciaries’ in J. McGhee (ed), *Snell’s Equity* (London: Sweet & Maxwell, 33rd ed, 2015) para 10-020; Langford, *ibid*, 120-125.

ARTICLE 42 AND THE SCOPE OF THE PROPER PURPOSE RULE

The main issue before the High Court, the Court of Appeal and the Supreme Court was the scope of the proper purpose rule. At first instance, Mann J was of the view that the only purpose for which the board of directors was permitted to impose restrictions pursuant to article 42 was to ‘provide a sanction or an incentive to remedy the default’.¹³ Mann J found that the primary purpose of the board in issuing the restriction notices pursuant to article 42 was to maximise the prospect of the resolutions that the board had proposed being passed at the forthcoming meeting of shareholders. Although the directors genuinely believed that having the resolutions passed was in the best interests of the company, their purpose in issuing the restriction notices was improper. Mann J set aside the restriction notices and the board resolutions authorising them.

In the Court of Appeal, the majority (Longmore LJ and Sir Robin Jacob) held that the proper purpose rule ‘has no significant place’ in the operation of article 42.¹⁴ Underpinning this conclusion was a concern that to allow the proper purpose rule to operate would mean that article 42 would be unlikely to have much scope for operation and would be ‘emasculated’.¹⁵ They considered provisions of the Companies Act 2006 upon which article 42 is based and stated that they did not believe parliament would have intended that ‘a detailed inquiry into the minds of the directors ... be undertaken before the sanction can be imposed’.¹⁶ This would limit the operation of the statutory provisions and any equivalent company articles ‘in what may often be a rapidly changing scene’.¹⁷ The majority was also of the view that in previous cases considering the proper purpose rule, the powers exercised by the directors were ‘unilateral powers’ whereas in the situation before the court, those who had received the restriction notices could prevent the operation of the notices by providing full and accurate information.¹⁸ In the words of Longmore LJ and Sir Robin Jacob, ‘[w]hy should the

¹³ *Eclairs* (HC) n 7 above at [206].

¹⁴ *JKX Oil* n 8 above at [138].

¹⁵ *ibid* at [142].

¹⁶ *ibid* at [141].

¹⁷ *ibid*.

¹⁸ *ibid* at [136].

law protect [the recipient of the notices] when all he had to do was to tell the truth?’¹⁹ They stated that if the proper purpose rule applied to the operation of article 42, this ‘would only be an encouragement to deceitful conduct and not something which English law should countenance’.²⁰ Briggs LJ dissented, holding that the proper purpose rule applied to article 42, that the purpose of article 42 was that identified by the trial judge, and that given the trial judge’s findings as to what motivated the directors in issuing the restriction notices, they had acted for an improper purpose.

In the Supreme Court, all members of the Court agreed with Lord Sumption that the proper purpose rule applied to article 42. Lord Sumption was of the view that in the context of a battle for control of a company, the directors ‘would naturally wish to have the predators disenfranchised [and that] is precisely why it is important to confine them to the more limited purpose for which their powers exist’.²¹ In differing from the majority of the Court of Appeal, his Lordship stated that it is where there is a battle for corporate control that the proper purpose rule probably has the most valuable part to play.²²

This analysis resonates with those who view the proper purpose rule as a doctrine that regulates the balance of power between directors and shareholders.²³ The analysis also resonates with those who have argued that when applying the proper purpose rule, courts adopt a more stringent standard of review when directors exercise powers that concern the internal regulation of the company, in contrast to powers that concern those outside the company.²⁴ In strong language, Lord Sumption stated that if the proper purpose rule did not apply to article 42, this effectively would give

¹⁹ *ibid.*

²⁰ *ibid* at [143].

²¹ *ibid* at [37].

²² *ibid.*

²³ D. Kershaw, ‘The Illusion of Importance: Reconsidering the UK’s Takeover Defence Prohibition’ (2007) 56 *International and Comparative Law Quarterly* 267.

²⁴ R. C. Nolan, ‘The Proper Purpose Doctrine and Company Directors’ in B. A. K. Rider (ed), *The Realm of Company Law – A Collection of Papers in Honour of Professor Leonard Sealy* (London: Kluwer Law International, 1998).

boards ‘a blunderbuss’ in the context of a battle for corporate control, ‘whose shot is liable to injure the just and the unjust alike’.²⁵

His Lordship largely accepted the view of Mann J that the purpose of article 42 was to provide a sanction or incentive to remedy a failure to comply with the earlier disclosure notice and stated that in his opinion, article 42 had three closely related purposes: (1) to induce the shareholder to comply with the notice; (2) to protect the company and its shareholders against having to make decisions in ignorance of relevant information; and (3) to impose sanctions for a failure to provide the requested information.²⁶ His Lordship referred to the

clear line between protecting the company and its shareholders against the consequences of non-provision of information, and seeking to manipulate the fate of particular shareholders’ resolutions or to alter the balance of forces at the company’s general meetings’.²⁷

These latter issues ‘are no part of the purpose of article 42’ and are matters for shareholders and not the board of directors.²⁸ Because the directors were motivated by the effect that the restriction notices would have on the prospect of the resolutions that had been proposed being passed, this constituted an improper purpose.²⁹

An important issue arises from the very different views expressed by the Supreme Court and the majority of the Court of Appeal regarding the scope of the proper purpose rule. It relates to the role of directors of a target company when confronted with a hostile takeover or, in the words of Lord Sumption, a ‘battle for corporate control’.³⁰ The majority of the Court of Appeal was motivated to empower directors to act vigorously on behalf of the company when, in response to a request for information from a shareholder, the shareholder provides what the directors consider false or

²⁵ *Eclairs* (SC) n 2 above at [39].

²⁶ *ibid* at [32].

²⁷ *ibid* at [33].

²⁸ *ibid*.

²⁹ *ibid* at [41].

³⁰ *ibid* at [37].

materially incorrect information. To apply the proper purpose rule to article 42 would be to restrict the directors, and their decisions in such a context should not be second-guessed by requiring a detailed inquiry into their motivations for issuing a restriction notice. In the context of a battle for corporate control, the directors may need to act swiftly to elicit accurate information about who controls the shares of the company and the directors are the custodians of the company's best interests. Indeed, it is the directors who determine what are the best interests of the company and provided they make their decisions relating to article 42 with a genuine belief they are acting in the best interests of the company, then it is not the role of the court to inquire whether they also acted for a proper purpose.

A different and more sceptical view of the role of directors underlies the decision of the Supreme Court. Rather than empowering directors to act in the interests of the company as determined by the directors, the issue is one of restraining them because of the conflict they may face in the context of a battle for corporate control. If the company is taken over by the hostile raider, the incumbent directors will lose their positions. Article 42 can be used by the incumbent directors to disenfranchise hostile raiders and this is why the operation of article 42 needs to be subject to the proper purpose rule that limits the actions of directors. In the Court of Appeal, Briggs LJ identified this conflict in the following terms

The temptation upon directors, anxious to protect their company from what they regard as the adverse consequences of a course of action proposed by shareholders, to interfere in that way, whether by the issue of shares to their supporters, or by disenfranchisement of their opponents' shares, may be very hard to resist, unless the consequences of improprieties of that kind are clearly laid down and adhered to by the court.³¹

For corporate law scholars, this debate about the role of directors in the context of a battle for control of the company is familiar. The debate in the United States goes back to the early 1980s when scholars disagreed about the autonomy that should be allowed to directors of target companies when confronted with a hostile takeover.³² A later judgment of the Supreme Court of Delaware held that

³¹ *JKX Oil* n 8 above at [122].

³² F. H. Easterbrook and D. R. Fischel, 'The Proper Role of a Target's Management in Responding to a Tender Offer' (1981) 94 *Harvard Law Review* 1161 (proposing a rule that target company directors should remain passive when confronted with a takeover); L. Bebchuk, 'The Case for Facilitating Competing Tender Offers'

target company directors ‘must focus on the primary objective—to secure the transaction offering the best value reasonably available for stockholders—and they must exercise their fiduciary duties to further that end’.³³ This can mean requiring the target board to seek out an alternative bidder and even facilitating an auction for control of the company once it becomes evident that control of the company is likely to change.³⁴

The City Code on Takeovers and Mergers reflects a policy of placing some limits on the actions that can be taken by target company directors. In particular, Rule 21 provides that during the course of a takeover offer, or even before the date of the offer if the board of the target company has reason to believe that a bona fide offer might be imminent, the board must not, without the approval of the shareholders in general meeting, take any action which may result in any offer or bona fide possible offer being frustrated or in shareholders being denied the opportunity to decide the offer on its merits.³⁵

In this area of corporate law there is a tension, on the one hand, between restricting what target company directors can do based on a concern that they have a conflict of interest as they may seek to thwart the takeover and preserve their own positions and, on the other hand, allowing directors the freedom to take actions that may lead to a higher offer for shareholders.

Views on whether the operation of article 42 should be subject to the proper purpose rule reflect this tension regarding the role of target company directors. The majority of the Court of Appeal, in holding that the proper purpose rule did not apply to the operation of article 42, would have allowed directors to issue restriction notices even where they are motivated to have resolutions

(1982) 95 *Harvard Law Review* 1028 (proposing a rule that would allow directors to solicit a competing takeover bid as long as that bid would not thwart the initial bid or any subsequent bid).

³³ *Paramount Communications, Inc v QVC Network, Inc* 637 A.2d 34 at 44 (1994), Supreme Court of Delaware.

³⁴ *Revlon Inc v MacAndrews & Forbes Holdings, Inc* 506 A.2d 173 (1986), Supreme Court of Delaware.

³⁵ Rule 21 contains other limits on the actions target directors can take without the approval of shareholders including issuing any shares or purchasing by the company of its own shares; issuing or granting options in respect of any unissued shares; selling, disposing of or acquiring, or agreeing to sell, dispose of or acquire, assets of a material amount; or entering into contracts otherwise than in the ordinary course of the company’s business. For criticism of Rule 21, see Kershaw, n 23 above.

they have proposed pass at a forthcoming meeting of shareholders. This is a view that sees the directors as both the determinants and the protectors of the company's interests. In playing this important role, directors should not be shackled by an inquiry into their motives when they issue a restriction notice pursuant to article 42. This view both empowers directors and at the same time emphasises that where the control of a company may change, this is precisely when directors need to be permitted to take decisive action. A battle for corporate control is, in the words of the majority of the Court of Appeal, likely to be 'a rapidly changing scene'.³⁶

The Supreme Court, like the Court of Appeal, highlighted the significance of a battle for corporate control for its views on the actions allowed to target company directors. But a very different view is articulated. It is precisely because target company directors may be tempted to pursue actions that alter the balance of power in the company, for example by disenfranchising certain shareholders, that the proper purpose rule serves its most valuable function in restricting the actions of the directors to defined purposes.

DO COURTS ADOPT AN OBJECTIVE OR SUBJECTIVE TEST WHEN APPLYING THE PROPER PURPOSE RULE?

In the previous section we discussed how the majority of the Court of Appeal and the Supreme Court differed on the autonomy given to target company directors in the context of a battle for corporate control. By applying the proper purpose rule to the operation of article 42, the Supreme Court limited the actions that could be taken by the directors of JKK. A related issue is the test that the court adopts when applying the proper purpose rule. A subjective test provides more autonomy to directors than an objective test.³⁷ Unfortunately, some uncertainty is created in terms of the test to be adopted in the judgment of Lord Sumption. He states that the test is subjective.³⁸ However, this statement is contrary to earlier authority. In *Howard Smith Ltd v Ampol Petroleum Ltd*, Lord Wilberforce stated that

³⁶ *JKK Oil* n 8 above at [141].

³⁷ For discussion of this issue in the context of the duty to act in the best interests of the company see R. T. Langford and I. Ramsay, 'Directors' Duty to Act in the Interests of the Company: Subjective or Objective?' (2015) JBL 173.

³⁸ *Eclairs (SC)* n 2 above at [15].

when a dispute arises whether directors of a Company made a particular decision for one purpose or for another, or whether, there being more than one purpose, one or another purpose was the substantial or primary purpose, the Court, in their Lordships' opinion, is entitled to look at the situation objectively.³⁹

The statement of Lord Sumption is also contrary to views of corporate law scholars.⁴⁰

We submit that Lord Sumption meant that the proper purpose rule has both subjective and objective aspects and that his statement that the test is subjective should be interpreted in this way.⁴¹ We support this analysis on the following grounds. First, immediately following this statement, Lord Sumption quotes from *Hindle v John Cotton Ltd*, where Viscount Hindley stated that 'the state of mind of those who acted, and the motive on which they acted, are all important'.⁴² Lord Wilberforce in *Howard Smith* also drew upon this quote.⁴³ What is meant is that in order to determine for what purpose directors made the decision under review, it is necessary to understand their subjective motivations. However, the court applies an objective test in ascertaining as a matter of law the purposes for which a power may or may not be exercised and in determining whether the purpose which the directors say motivated them to make the decision under review is within the category of permissible purposes. Second, it is difficult to reconcile the decision of Lord Sumption (that the directors had acted for an improper purpose) with an entirely subjective test. This is because the majority of the directors were found to have a genuine belief that it was proper for them to issue the restriction notices and thereby disenfranchise the recipients of the notices in order to have the

³⁹ [1974] AC 821, 832.

⁴⁰ See, eg, P. L. Davies and S. Worthington, *Gower and Davies' Principles of Modern Company Law* (London: Sweet & Maxwell, 9th ed, 2012) at [16-46]. See also Nolan, n 24 above, para 7-13.

⁴¹ We note that only Lord Hodge supported this statement of Lord Sumption as the other judges indicate the paragraphs of Lord Sumption's judgment with which they agree and this paragraph is not included: see *Eclairs (SC)* n 2 above at [46] *per* Lord Clarke (with whom Lord Neuberger agreed) and at [47] *per* Lord Mance (with whom Lord Neuberger also agreed).

⁴² (1919) 56 Sc LR 625, 630, quoted in *Eclairs (SC)* n 2 above at [15].

⁴³ [1974] AC 821, 835.

resolutions they proposed passed at the forthcoming general meeting. Yet this genuine subjective belief was not sufficient to protect the directors' decision. They had failed to act for a proper purpose as objectively determined by the court.

Interpreting the statement of Lord Sumption in this way (which accords with previous authority) results in a test which considers the subjective motivations of the directors but which is ultimately an objective test. This test assesses the conduct of directors against what the court determines are the proper purposes for which a particular power can be exercised and thereby places a restraint on directors' conduct and limits their available actions. It is a test that has particular importance in the context of a battle for corporate control.

CAUSATION: THE UNRESOLVED ISSUE

Causation is an important issue in the application of the proper purpose rule given that many cases involve directors acting for mixed purposes. The appropriate test to be applied to determine causation is, however, unresolved due to disagreement among the Supreme Court. Determining the appropriate test in turn has implications for the autonomy allowed to target company directors. Where the court applies a strict test of causation and thereby restricts the circumstances in which a decision of directors is overturned, the result is to allow directors more autonomy in decision-making.

In the Supreme Court, Lord Sumption outlined alternative causative tests.⁴⁴ These alternatives evidence a spectrum in terms of the scope allowed for directors' decisions. First, Lord Sumption stated that an analogy with public law might suggest that a decision which has been materially influenced by an improper purpose should be set aside even if legally relevant considerations were more significant.⁴⁵ Secondly, according to Lord Sumption, the company law proper purpose rule applies a different test – that the directors' decision will be set aside only if the primary or dominant purpose was improper save perhaps in cases where the decision was influenced by dishonest

⁴⁴ *Eclairs* (SC) n 2 above at [17].

⁴⁵ Lord Sumption (*ibid* at [17]) cites *R (FDA) v Secretary of State for Work and Pensions* [2013] 1 WLR 444 at [67]-[69] *per* Lord Neuberger of Abbotsbury MR.

considerations or by the personal interest of the decision-maker.⁴⁶ This second test gives more autonomy to directors in the sense that it is harder to overturn the decision.

Within this second test, views differ as to the appropriate method of determining the primary, substantial or dominant purpose.⁴⁷ Most judgments, drawing upon *Howard Smith v Ampol Petroleum Ltd*,⁴⁸ look no further than an assessment of whether the improper purpose was the primary, substantial or dominant purpose for which the power was exercised. An alternative test, drawn from the Australian High Court case of *Mills v Mills*,⁴⁹ asks whether, but for the improper purpose, the power would have been exercised. The latter approach, which means that the improper purpose will not result in the decision being overturned unless the improper purpose actually caused the decision, gives more autonomy to directors.

Lord Sumption preferred the ‘but for’ test of causation from *Mills v Mills* and subsequently endorsed in *Whitehouse v Carlton Hotel Pty Ltd*, namely

As a matter of logic and principle, the preferable view would seem to be that, regardless of whether the impermissible purpose was the dominant one or but one of a number of significantly contributing causes, the allotment will be invalidated if the impermissible purpose was causative in the sense that, but for its presence, ‘the power would not have been exercised’ ...⁵⁰

It is, however, to be noted that the difference between the ‘but for’ test and the substantial purpose test is more pronounced than real given that even under the ‘but for’ test the improper purpose must be a significantly contributing cause. In Australia the tests have at times been combined so that in order to establish a breach it needs to be established that the substantial purpose is improper and that, but for the improper purpose, the director would not have exercised the power.⁵¹

⁴⁶ *Eclairs (SC)* n 2 above at [17].

⁴⁷ *ibid* at [19].

⁴⁸ [1974] AC 821, 834.

⁴⁹ (1938) 60 CLR 150, 186.

⁵⁰ (1987) 162 CLR 285, 294.

⁵¹ See, eg, *Haselhurst v Wright* (1991) 4 ACSR 527; *Kokotovich v Wallington* (1995) 17 ACSR 478; *Permanent*

A different approach was taken by Lord Mance (with whom Lord Neuberger agreed and with whom Lord Clarke partly agreed). He was of the opinion that it was not appropriate to decide whether a ‘but for’ test should be adopted as this issue had not been the subject of full argument and submissions. His Lordship gave several reasons for not expressing any concluded view on the test for causation. First, his Lordship stated that it would be helpful to clarify the meaning of section 171(b), which provides that directors may use their powers ‘only’ for the purposes for which they were conferred. This would seem to indicate that all purposes must be proper. Yet section 170(4) provides that the previous general law approach should inform the interpretation of section 171(b),⁵² and the general law has adopted a primary or substantial purpose test. In this respect, it is to be noted that an examination of the background documents to the Companies Act 2006 shows that use of the word ‘only’ was not intended to be significant.⁵³ In fact, the Steering Group stated that it had not defined the duty in section 171(b), leaving it for case law development.⁵⁴ The second reason was that adopting the ‘but for’ test would, in Lord Mance’s view, be a new development in company law which should not be undertaken without the benefit of argument and submissions.⁵⁵ The third reason was the need to explore the implications of the different tests for the evidence needed to establish a breach of the proper purpose rule.⁵⁶ The fourth reason was the need, if a ‘but for’ test were adopted, to establish what directors would have to show to prove that they would have reached the same decision even if they had not acted for an improper purpose.⁵⁷ The approach to causation is therefore unsettled as a result of the Supreme Court decision.

Building Society (in liq) v Wheeler (1994) 14 ACSR 109, 137.

⁵² See *Eclairs* (SC) n 2 above at [51], citing *Buckley on the Companies Acts* (Butterworths Law: looseleaf ed) at 3[869].

⁵³ See Companies Act 2006, Explanatory Notes at [323].

⁵⁴ Department of Trade and Industry, *Modern Company Law for a Competitive Economy: Developing the Framework* (URN 00/656, March 2000) at [3.47].

⁵⁵ *Eclairs* (SC) n 2 above at [53].

⁵⁶ *ibid* at [54].

⁵⁷ *ibid* at [55].

The exact extent to which directors' autonomy is constrained by reason of the causation requirement inherent in the proper purpose rule is therefore uncertain following *Eclairs Group Limited v JKX Oil & Gas plc*. The court did not decide whether a substantial purpose test or a 'but for' test is to be applied where a decision of directors is motivated by mixed purposes. It is, however, clear that directors are granted more autonomy under these tests than under the public law test.

CONCLUSION

Given that the proper purpose rule has the potential to restrict substantially directors' autonomy in situations in which a change of control of the company is threatened, we have examined the extent to which certain aspects of that rule impact on such autonomy, as articulated in the recent judgment of the Supreme Court in *Eclairs Group Limited v JKX Oil & Gas plc*. We have shown that in defining the scope of the proper purpose rule the Supreme Court restricted the autonomy of directors. In imposing an objective test in the application of the rule (despite the terminology used by Lord Sumption not being entirely clear) the court also limited this autonomy. The approach to causation favoured by the court does, however, give directors more autonomy than the test applied in public law, although the precise contours of the causative test were not resolved. Resolution by the court of some of the key issues involved in the application of the proper purpose rule is to be welcomed, given the pressures faced by directors in the context of change of control.