Section 51 (xx): No Power of Incorporation

by **Gerard Carney**
Assistant Professor of Law
Bond University

Introduction

The long awaited decision of the High Court of Australia on the validity of certain pivotal sections of the *Corporations Act* 1989 (Cth), delivered on 8 February 1990, has settled at least for the foreseeable future that the corporations power in s 51 (xx) of the Commonwealth Constitution includes no power of incorporation. This decision in *New South Wales & Others* v *Commonwealth of Australia*[1] (hereafter referred to as the *Corporations Act* case) aroused considerable public and commercial interest if not concern, not only in view of its significant impact on Australian commerce but equally in being an uncharacteristic set back for Commonwealth power.

Whether or not s 51 (xx) encompasses the power to provide for the incorporation of trading and financial corporations has been the subject of intense academic debate.[2] Until this year, judicial consideration of the issue was scant and merely *obiter dicta*. The enactment by the Commonwealth of the *Corporations Act* 1989 squarely raised this issue for the first time.[3] The challenge as to the constitutional validity of certain provisions of chapters 2 and 5 of the Act was brought by New South Wales, South Australia and Western Australia and proceeded by way of a stated case to the Full High Court.

The Corporations Act 1989 (Cth)

The stated case posed two questions for the High Court:

1. Are any of ss 114 to 125, ss 155(1), (3) and (4) and ss 156 to 158 of the *Corporations Act* 1989 invalid in so far as they purport to apply to a company registered under Division 1

1 (1990) 90 ALR 355; (1990) 64 ALJR 157. (All page references are to Volume 90 of the *Australian Law Reports*).

2 See J L Taylor, 'The Corporations Power: Theory and Practice' (1972) 46 ALJ 5; Note by P Lane (1972) 46 ALJ 407; O I Frankel and J L Taylor, 'A 1973 National Companies Act?—The Challenge to Parochialism' (1973) 47 ALJ 119; R L Pritchard, 'Corporate Reform & Its Constitutional Impairment' (1975) 49 ALJ 215.

3 The Commonwealth did not proclaim the legislation in view of the High Court challenge.

of Part 2.2 where the statement referred to in s. 153 (1) (e) states as mentioned in s 153 (3) or (5) whether or not the statement also states as mentioned in s 153 (2)?

2. Are ss 112 and 113 of the *Corporations Act* 1989 valid as laws with respect to trading and financial corporations formed within the limits of the Commonwealth within the meaning of s 51 (xx) of the Constitution?

In answering these questions, the Court acknowledged that their resolution depended upon s 51 (xx) being interpreted to include a power of incorporation. On this issue, the Court split 6–1 with the majority of Mason CJ, Brennan, Dawson, Toohey, Gaudron and McHugh JJ delivering a joint judgment and holding that no power of incorporation was to be found in s 51 (xx). Accordingly, they answered question 1 affirmatively and question 2 negatively. The sole dissenter, Deane J, interpreted s 51 (xx) as encompassing a power of incorporation but in view of the majority's decision he declined to examine the constitutional validity of those provisions of the Act cited in the stated case.[4]

Before discussing the Court's interpretation of s 51 (xx), a brief outline of the provisions of the Act in issue is worthwhile.

The first question related to Division 1 of Part 2.2 of the Act which dealt with incorporation by registration. Section 114 prescribed that five or more persons (or in the case of a proprietary company, two or more persons) may form an incorporated company. Sections 120 and 121 empowered the Australian Securities Commission to register a company and certify its registration upon being satisfied that all the requirements for registration were fulfilled. The most significant prerequisite for incorporation was the lodgment of an 'activities statement' which basically stated that the company would carry on trading (defined to include financial) or banking activities within three months of incorporation or after a period of dormancy. Thus, the Act relied upon the activities test developed by the High Court for characterising a corporation as a trading or financial corporation[5]. Corporations registered under the Act were required to lodge annual activities statements[6]. If they ceased to be a trading or banking corporation, they would be wound up.[7]

The second question concerned Part 2.1 which in s 112 prohibited the formation of certain 'outsized' partnerships or associations which might otherwise be formed to avoid the operation of the Act. Section 113 prohibited the incorporation under State or Territory law of corporations which would be trading or banking corporations under the Commonwealth Act.

The Corporations Power: s 51 (xx)

Section 51 empowers the Commonwealth Parliament to make laws with respect to: (xx) Foreign corporations, and trading or financial corporations formed within the limits of the Commonwealth.

4 Above n 1 at 369.

5 See *Fencott v Muller* (1983) 152 CLR 570.

6 s 336.

7 ss 156 to 158.

Both the majority and minority views in the *Corporations Act* case rely principally upon the grammatical construction of the actual words of s 51 (xx), in particular, the phrase 'formed within the limits of the Commonwealth'. The opposing interpretations given to this phrase by the joint majority on the one hand, and by Deane J on the other, determined the outcome of the case. The other reasons given by the joint majority, most of which are strongly challenged by Deane J, are given only in support of the majority's construction. The extent to which one gives credence to these supporting reasons is really of little import. Although the judgment of Deane J exposes their fragile bases, the deciding factor remains the grammatical construction of s 51 (xx).

Grammatical Construction

The two competing constructions of the phrase 'formed within the limits of the Commonwealth' are:

(i) that the phrase is used simply to distinguish trading and financial corporations as local corporations from foreign corporations; or

(ii) that the phrase restricts the power to the regulation of local trading and financial corporations already formed or to be formed under State law or formed pursuant to other heads of Commonwealth power which, within their scope, authorise the creation of corporations.[8]

The joint majority while acknowledging that the phrase 'formed within the limits of the Commonwealth' distinguishes between local and foreign corporations (no. (i) above), interpreted it to mean much more than that (no. (ii) above). In referring to the distinction made in no. (i) above, they said:

> No doubt the words do serve that function but their plain meaning goes beyond the mere drawing of that distinction. ... The distinction based on the place of formation is obvious, but the basis of the distinction is formation. The word 'formed' is a part participle used adjectively, 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. (Clearly enough, the phrase is used to describe corporations formed after as well as those formed before federation). The subject of a valid law is restricted by that phrase to corporations which have undergone or shall have undergone the process of formation in the past, present or future. That is to say, the power is one with respect to 'formed corporations'.[9]

Accordingly, the majority concluded that to fall within the limb of the power relating to trading and financial corporations, two conditions must be satisfied: there must be a corporation already formed within the limits of the Commonwealth and it must be a trading or financial corporation.[10]

However, Deane J was not prepared to construe the phrase 'formed within the limits of the Commonwealth' to mean anything more than that the power over trading and financial corporations was in respect of

8 For example s 51 (i) and s 122.

9 Above n 1 at 358.

10 Ibid.

locally formed corporations as distinct from foreign corporations (no. (i) above).[11] His Honour rejected any significance in the use of the past participle 'formed' in the context of s 51 (xx) since it is 'a use of the past participle as part of an adjectival phrase which is without temporal significance'.[12] It is on this issue that Deane J differs dramatically from the majority who relied on the use of the past participle 'formed' for their conclusion that the power arose in relation to already existing corporations.

Deane J cited in support of his view that a past participle can be neutral in a temporal sense, the comments of Stephen J in *Mikasa (NSW) Pty Ltd v Festival Stores*[13] in relation to s 66B (2)(d)(ii) of the *Trade Practices Act* 1965. That provision defined a person as engaged in the practice of resale price maintenance if as a supplier, the person 'withholds the supply of goods to a second person for the reason that the second person ... (ii) has sold, or is likely to sell, goods *supplied* to him by the supplier ... at a price less than the price specified by the supplier as the price below which the goods are not to be sold' (emphasis added). Stephen J rejected the appellant's argument in that case that para (ii) only applied where goods were previously supplied before there was a withholding of further supplies. The use of 'supplied', according to his Honour, was not the use of 'the past tense but rather a common enough instance of the use of the past participle; it is neutral in temporal meaning and applies equally to the future as to the past'[14]. The same conclusion was reached by Barwick CJ[15] (with whom McTiernan J[16] substantially concurred) and Menzies J[17] (with whom Gibbs J[18] agreed).

Deane J was not the first to apply this grammatical interpretation to s 51 (xx). In *Kathleen Investments (Aust) Pty Ltd v Australian Atomic Energy Commission*[19], Murphy J expressed the view that 'formed' in s.51 (xx) 'does not confine Parliament to laws with respect to corporations which have been formed. Past participles are often used to apply to the future as well as the past ...'[20].

That past participles may, depending on their context, apply to the future and to the past is clear. However, no justification is given by either Deane J or Murphy J for interpreting 'formed' as not intended to be used in the past tense. Further consideration of the context in which it appears would have been desirable before adopting the approach in *Mikasa (NSW) Pty Ltd* v *Festival Stores*[21]. It does not necessarily follow that because the past participle is neutral in the context of the *Trade Practices Act*, that it is also neutral in an express grant of legislative

11 Ibid at 364.
12 Ibid.
13 (1972) 127 CLR 617.
14 Ibid at 661.
15 Ibid at 633—4.
16 Ibid at 636.
17 Ibid at 642.
18 Ibid at 652.
19 (1977) 139 CLR 117.
20 Ibid at 159.
21 Above n 13.

power in the Commonwealth Constitution. The former is dealing with a factual situation—the regulation of trading activities. The latter concerns the scope of a constitutional power which is defined by the language used. It may well be that where a grant of power is concerned that the less restrictive of the two approaches should be adopted. This may have been the view of Deane J:

> A plenary legislative power with respect to particular kinds of corporations extends as a matter of mere language, to laws dealing with both the incorporation and the liquidation of such corporations.[22]

The majority, as noted earlier, does recognise that although the past participle 'formed' is used, the power extends to corporations which are formed in the past, present or future.[23] However, the essential prerequisite to power remains, that a corporation must be formed at some point in time. This differs from the interpretation given by Deane J that 'formed' is neutral in a fundamental sense in that it requires no corporation to be formed at all in order for the power to arise.

The weakness in the joint majority judgment is its failure to consider this approach of Deane J and to justify its rejection in the context of s 51 (xx). The majority merely declared that the phrase 'formed within the limits of the Commonwealth' *clearly meant* that trading and financial corporations only became subject to Commonwealth power under s 51 (xx) if they were already formed.[24] The failure of the majority to acknowledge that an alternative interpretation was possible and to justify their rejection of it renders their decision less convincing. A detailed analysis of the various grammatical arguments raised as regards this issue of incorporation was needed. Instead, the majority concentrated on supporting their interpretation by reference to judicial precedent and the history of s 51 (xx).

Judicial Precedent

In the absence of any decision on point, the majority relied on the obiter view of the High Court in *Huddart Parker and Co Pty Ltd v Moorehead*[25] that no power of incorporation was conferred by s 51 (xx). According to the majority, two related reasons were given in *Huddart Parker* for this view. First, since the Commonwealth clearly derived no power of incorporation over foreign corporations, it derived no similar power over trading and financial corporations. Secondly, if such a power was intended, it would have been granted expressly as in s 51 (xiii) which empowers Parliament to make laws with respect to '[b]anking ... also ... the incorporation of banks'.[26]

In *Huddart Parker*, both of these reasons were given only by Barton J,[27] while Griffith CJ[28] and Isaacs J[29] relied upon the first and second

22 Above n 1 at 363.
23 Ibid at 358.
24 Above n 1 at 363.
25 (1909) 8 CLR 330.
26 Above n 1 at 358—9.
27 Above n 25 at 362—3.
28 Ibid at 348.
29 Ibid at 393—4.

reasons respectively. However, the primary reason given by the Court in *Huddart Parker* was that the power of incorporation was left with the States.[30] Such a statement is susceptible of being either a conclusion or a reason. The majority in the *Corporations Act* case regarded it as a conclusion derived from 'purely textual considerations'[31] whereas Deane J regarded it as the basis for their view.[32]

Even as a conclusion, the view that the power of incorporation was left with the States was qualified by Griffith CJ,[33] O'Connor[34] and Higgins JJ[35] all of whom recognised that trading and financial corporations could be formed under other heads of Commonwealth power, such as s 51 (i) and s 122.

Deane J refuted both of the reasons cited by the majority as the basis for the view in *Huddart Parker* that s 51 (xx) included no power of incorporation. His Honour considered that the limb of the power with respect to foreign corporations allows the Commonwealth '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.'[36] As regards the comparison with the banking power in s 51 (xiii) which expressly includes the power of incorporation, Deane J rejected that argument by referring to the undoubted power in the absence of express provision in s 51 (i) to establish corporations for the purposes of interstate and overseas trade and commerce.[37]

Isaacs J in *Huddart Parker* considered at some length[38] whether or not s 51 (xx) included a power to regulate incorporation and he referred to other factors in addition to those noted above for holding that no such power was to be found in s 51 (xx). First, the phrase 'formed within the limits of the Commonwealth' is meaningless if a power of incorporation is included in the grant of power.[39] Secondly, the nature of a corporation as a legal conception, a creature of law, precluded the inclusion within a power over such corporations, of the power of creation itself.[40]

The second reason superficially appears consistent with the subsequent description given to s 51 (xx) by the High Court as a power with respect to persons or legal entities.[41] However, that description is given in a

30 See Griffith CJ at 349; Barton J at 362—3; O'Connor J at 371; Isaacs J at 393—4; and Higgins J at 412.

31 Above n 1 at 359.

32 Ibid at 365.

33 Above n 25 at 349.

34 Ibid at 371.

35 Ibid at 412.

36 Above n 1 at 363.

37 Ibid at 367.

38 Above n 25 at 393—4.

39 Ibid.

40 Ibid.

41 See *Stenhouse v Coleman* (1944) 69 CLR 457 per Dixon J at 471; *Actors and Announcers Equity Association of Australia v Fontana Films Pty Ltd* (1982) 150 CLR 169 per Gibbs C J at 181 and Brennan J at 216; *Tasmania* v *Commonwealth* (1983) 46 ALR 625 per Mason J at 710; Brennan J at 789; and Dawson J at 851—2.

different context and does not depend upon the characterisation of the power as one over such corporations. Isaacs J, it is submitted, unjustifiably narrowed the scope of s 51 (xx) by describing it as a power over corporations when it is a power *with respect to* corporations.[42] Arguably, the former depends upon pre-existing corporations whereas the latter does not.

Significantly, the majority in the *Corporations Act* case began their discussion of s 51 (xx) by referring to this peculiar nature of the power:

> The power conferred by s 51 (xx) is not expressed as a power with respect to a function of government, a field of activity or a class of relationships but as a power with respect to persons, namely, corporations of the classes therein specified . . .[43]

What significance stems from the nature of s 51 (xx) as a power with respect to a legal entity? It is submitted that it has nothing to do with the existence of any power of incorporation. Rather, it is concerned with the undefined scope of the power with respect to the entity, in terms of the extent and nature of the regulation of that entity permissible under the power. Is every aspect and activity of that entity within the scope of permissible regulation? It has only been in that context that s 51 (xx) has been described as a power with respect to legal entities.[44] The same difficulty arises with s 51 (xix) 'aliens' and s 51 (xxvi) 'the people of any race'.

Therefore, it is not possible to argue, given that s 51(xx) is a power with respect to legal entities in the same way that s 51 (xix) *aliens* and (xxvi) *people of any race* are powers with respect to legal entities or natural persons, that because no power of creation is conferred by the latter two powers that the same result follows for s 51 (xx). Such an argument ignores the fundamental distinction between artificial and natural persons. A power with respect to artificial persons inevitably poses the issue whether that power incorporates the power of creation itself. Deane J not only concluded that it did but regarded the fact that such a power of creation is possible as supportive of its existence in a grant of constitutional power.[45] In support of his view, his Honour compared s 51 (xx) with s 51 (vii) which gives the Commonwealth power over lighthouses—a power which undoubtedly includes the power to construct and destroy such structures.[46]

None of the reasons given by the justices in *Huddart Parker* for their unanimous obiter view that no power of incorporation arises under s 51 (xx) was specifically adopted by the majority in the *Corporation Act* case. But for having to defend the obiter of the former decision from the taint of the doctrine of state reserve powers, the majority appeared content to simply accept the case as a supporting precedent.[47] The majority held

42 Above n 25 at 393.
43 Above n 1 at 357—8.
44 Above n 41.
45 Above n 1 at 367.
46 Above n 1 at 364.
47 Above n 1 at 358—9.

that the view of the Court in *Huddart Parker* was based on 'purely textual considerations, quite apart from the now discarded doctrine'.[48]

Deane J disagreed, holding that the doctrine of state reserve powers which had tainted the interpretation of s 51 (xx) in relation to the scope of regulation permissible under the power, also had influenced the Court (apart from Isaacs J) in stating there was no power of incorporation under s 51 (xx).[49] Isaacs J, on the other hand, who was unaffected by the doctrine of state reserve powers, rejected a power of incorporation, in the view of Deane J, as a result of his different but still restricted view of s.51 (xx).[50] In holding that the power only permitted the Commonwealth to regulate the conduct of trading or financial corporations 'in their transactions with or as affecting the public'[51], leaving to the States exclusive power over the regulation of the internal affairs of these corporations, Isaacs J saw that a federal power of incorporation was incompatible with this field of State power.[52]

Certainly, as noted earlier, the grammatical construction of s 51 (xx) was referred to by the Court in *Huddart Parker* and indeed Griffith CJ[53] and O'Connor J[54] were prepared to hold there was on the face of the paragraph no power of incorporation. But to state that the Court's view depended *only* on textual considerations is, with respect, an over-simplification. The underlying assumption in all judgments is that the States retained the power of incorporation. The interpretation of the phrase 'formed within the limits of the Commonwealth' as meaning formed under State law[55] is consistent with this assumption although it is not conclusive.

The majority[56] also relied upon the obiter comments of Barwick CJ in *Strickland v Rocla Concrete Pipes Ltd*[57] which implicitly accept that s 51 (xx) encompasses no power of incorporation. They concluded that judicial opinion since the *Engineers'* case[58] supported their view.[59]

The History of s 51 (xx)

The majority relied upon both the convention debates and the draft Constitution Bills of 1891, 1897 and 1898 to support their interpretation of s 51 (xx).

They accepted that the convention debates 'may be used to establish the subject to which the paragraph was directed [as] made clear by *Cole*

48 Ibid at 359.
49 Ibid at 365.
50 Ibid at 366.
51 Above n 25 at 395.
52 Above n 1 at 366—7.
53 Above n 25 at 348.
54 Ibid at 371.
55 Above n 30.
56 Above n 1 at 360.
57 (1971) 124 CLR 468.
58 (1920) 28 CLR 129.
59 Above n 56.

v Whitfield[60] . . . see also *Port MacDonnell Professional Fisherman's Association Inc v South Australia*[61]'.[62]

It is important to appreciate the context in which *Cole* v *Whitfield* allowed reference to the convention debates and to keep in mind the caveat it applied to such referral:

> Reference to the history of s 92 may be made, not for the purpose of substituting for the meaning of the words used the scope and effect—if such could be established—which the founding fathers subjectively intended the section to have, but for the purpose of identifying the contemporary meaning of language used, the subject to which the language was directed and the nature and objectives of the movement towards federation from which the compact of the Constitution finally emerged.

The 1891 draft Bill conferred in cl 52 (19) a power to legislate with respect to: '[t]he status in the commonwealth of foreign corporations, and of corporations formed in any state or part of the commonwealth'. The fact it was a power only with respect to the status of corporations indicated according to the majority that the use of 'formed' in the 1891 draft provision must have meant 'which have been formed'.[63] Also during the Convention debates, Sir Samuel Griffith denied any need for a power of incorporation when this issue was raised.[64]

The 1897 draft Bill deleted the reference to 'status' by conferring in cl 50 (xxii) a power to legislate with respect to: '[f]oreign corporations, and trading corporations formed in any State or part of the Commonwealth'.[65] The majority concluded that although 'status' was removed, the meaning of 'formed' was intended to remain unchanged from that in the 1891 draft provision.[66] With respect, such an assumption is difficult to justify. The substantial change in wording between the 1891 and 1897 draft Bills effected a fundamental change in the nature of the power. At the same time, the 1897 draft provision both widened and narrowed the scope of the power under the 1891 draft Bill. Although now no longer limited to the status of corporations, the power was restricted to only those local corporations which are trading or financial corporations. To suggest that there was no intention to change the meaning of 'formed', ignores the effects of and insulates that part of the provision from the radical change in the nature and scope of the power that occurred in the 1897 draft.

The approach of the majority in the *Corporations Act* case in referring to the convention debates 'to establish the subject' to which s 51 (xx) is directed, effectively removes any restraints on the Court's ability to refer to those debates. If this was not intended by *Cole v Whitfield*, what then was meant by 'the subject to which the language [was] directed'?

Here again, Deane J differed from the majority by deriving no assistance from the convention debates or the draft Bills for the interpretation of

60 (1986) 165 CLR 360 at 385.
61 (1989) 88 ALR 12 at 31.
62 Above n 1 at 360.
63 Ibid at 361.
64 *Convention Debates* (Sydney 1891) vol I at 686.
65 Above n 1 at 361.
66 Ibid.

s 51 (xx). His Honour prefaced his judgment with an endorsement of the literalistic approach to the interpretation of the Constitution. In deciding whether s 51 (xx) extends to incorporation, he warned:

> The answer to that question must, of course, be found in the words of the Constitution. It is those words—and those words alone—which constitute the compact made between the people of this country when, by referenda, they authorised the formal enactment of—or, in the case of the people of Western Australia, the proclamation of adherence to—the terms upon which they 'agreed to unite in one indissoluble Federal Commonwealth'. If the words of s 51 (xx), construed in context in accordance with settled principle, extend to authorise the making of such laws, it is simply not to the point that some one or more of the changing participants in Convention Committees or Debates or some parliamentarian, civil servant or draftsman on another side of the world intended or understood that the words of the national compact would bear some different or narrower meaning.[67]

The majority's reliance upon the the history of s 51 (xx) does not conflict with these firm comments by Deane J. There was no attempt by the majority to replace the natural meaning of s 51 (xx) with the subjective motives of its drafters because both of these coincided in the view of the majority.

Consequential Difficulties

In further support of their conclusion that s 51 (xx) provided no power of incorporation, the majority foresaw 'undeniable difficulties' if there was such a power, given that the power in relation to local corporations is confined to trading and financial corporations.[68] What would be the position if a trading corporation incorporated under s 51 (xx) no longer carried on trading activities?

Such difficulties did not concern Deane J for in his view they did 'not provide any legal justification for denying the generality of a plenary grant of legislative power with respect to the designated class of corporation'.[69] His Honour recommended a broad definition of trading and financial corporations as 'companies formed for the purpose or engaged in the pursuit of profit' to help overcome the practical difficulties resulting from a power of incorporation. In the end, though, Deane J regarded the advantages of national companies legislation as outweighing any potential difficulties involved in its implementation.[70]

Conclusion

Although one may agree with the critical assessment by Deane J of the reasons given by the majority in support of their decision, the divergence between the majority and Deane J in their interpretation of the actual words of s 51 (xx), particularly the phrase 'formed within the limits of the Commonwealth' is readily comprehensible. Both interpretations are feasible. Which is the correct one is now for practical purposes only of academic interest.

---

67 Ibid at 362.
68 Ibid.
69 Ibid at 368.
70 Ibid.

The majority decision in the *Corporations Act* case may be viewed as a classic example of what Kitto J in *Airlines of New South Wales Pty Ltd v New South Wales* (no. 2)[71] described as the duty of the High Court in its interpretation of the Commonwealth's legislative powers:

> This court is entrusted with the preservation of constitutional distinctions, and it both fails in its task and exceeds its authority if it discards them, however out of touch with practical conceptions or with modern conditions they may appear to be in some or all of their applications.[72]

71 (1965) 113 CLR 54.
72 Ibid at 622.