

## TUTORIAL EXERCISE NO 1

### Question 1

Explain why the Commonwealth Parliament has the power to make laws relating to companies. Discuss the role that ASIC plays in relation to companies.

ASIC – Australian Securities and Investment Commission

Commonwealth Parliament has the power to make laws relating to companies because the States has given the power to the Federal Parliament under s 51 (xxxvii).

- Set up by ASIC Act, work under the Corporation Act,
  - Enforce the law
  - Ensure compliance
  - Investigate
  - Law reform
  - Public access
- Responsible to establish the existence of companies under [s 119]:
  - Give company ACN (Australia Company Number)
  - Registers company [s 117]
  - Issue certificate

### Question 2

In the absence of specific legislation, courts have, as a general rule, been reluctant to depart from the principle established in **Salomon v Salomon** and lift the veil of incorporation.

Specify with reference to Australian legislation and general common law precedents the exceptional situations in which this veil of incorporation may be lifted.

Company is a separate legal entity:

- Enters into contracts in company's own name
- All powers of a natural person plus 'corporate' powers [s 124]

#### **Salomon v Salomon**

Salomon is a sole trader of shoe business. He sold his business to Company and received 20,001 shares and secures debenture for 10,000 pounds. The corporation had Salomon himself and another six shareholders. The business of the corporation eventually went under and unable to pay the 10,000 debenture. The creditors argue that the Company and Salomon were one and the same, he and shareholders are liable for the debts of the corporation. The court held that Company is a separate entity. Debt is the company's responsibility. Veil protects Salomon in his personal capacity.

Veil may be lifted under Statutory Exceptions

- 1) Insolvent trading s 95A
  - A person is **solvent** if, and only if, the person is able to pay all the person's debts, as and when they become due and payable.
  - A person who is not solvent is **insolvent**. (**not able** to pay all the person's debts)

- **s588G - Director liable** - A director contravenes this section if a company incurs a debt at a particular time and becomes insolvent or would become insolvent because of it, and at that time a person is a director of the company, where that person fail to prevent the company incurring the debt was dishonest.
- **s588V - A holding company** (corporation) contravenes this section if the company is insolvent at that time or would be insolvent by incurring that debt, and when there are reasonable grounds for the holding company/one or more directors from the holding company to suspect that the company is insolvent or would be insolvent. (no offence?)

## 2) Voidable Transaction

- Under **s588FE(3)**, the transaction is voidable if it is an insolvent transaction, and also an uncommercial transaction of the company and it was entered into within 2 years of application for winding up.
- Under **s588FE(4)**, the transaction is voidable if it is an insolvent transaction and a related entity (promoter, director, member, spouse of these persons) is a party to it, which was entered into within 4 years of application for winding up.
  - **s588FB** – commercial transaction can be avoidable transaction

## 3) Company Officer Security Interest

- Under **s588FP**, the interest will be void if it is enforced by officer within 6 months of the creation of the security interest. However may seek court approval.

## 4) Financial Assistance

- Under **s260A**, where company provides financial assistance for the acquisition of its shares of its holding company's shares is in contravention of s260A, if it will materially prejudice the interests of the company or shareholders, or the ability of the company to pay its creditors. Under s260D, the company is not guilty of offence, however the person involved in contravention is guilty of offence.

- Veil may be lifted under Statute and Common Law money was used to pay the Channel Island Company.
- The liquidator of Welsh, the English Company claimed in Darby's bankruptcy for the secret profit made by him as a promoter of Welsh. Court lifted the veil of the Channel Island Company and treated Darby and Glyde as promoters of the English Company.

## 1) Agency/partnership

***Smith Stone & Knight Ltd v Birmingham Corp [1939] 4 All ER 116***

SSK owned factory in Birmingham. **Birmingham Waste Co Ltd (BWC)** was subsidiary of SSK. BWC ostensibly carried on business in SSK's factory

## 2) Avoidance of obligations

***Gilford Motor Co Ltd v Horne [1933] Ch 935***

- Restraint of Trade Clause in employment contract. Horne set up company to carry on business as a way around the clause.
- Court granted an injunction against Horne and his Company.

## 3) Fraud

***Re Darby [1911] 1 KB 95***

- Darby and Glyde formed a company in the Channel Islands as part of a fraudulent plan. The Channel Island company purchased a licence to work a quarry and then floated an English Company, Welsh Slate Quarries Ltd for the purpose of purchasing the licence at a gross overvalue. Welsh issued a prospectus and issued shares to the public. The
- Birmingham Corp resumed factory. SSK claimed compensation for disturbance to its business at the factory. Birmingham Corp argued that it is BWC's business, not SSK's.
- Held: SSK may sue on BWC's behalf as BWC was SSK's agent.

## 4) Benefit of group as a whole

***Equiticorp Finance Ltd (in liq) v Bank of New Zealand [1987] VR 485***

- Bank loan to one company repaid by other companies in group. The liquidator of the transferring companies sought to recover the funds from the bank on the basis that the transfer involved breach of duty by the directors to act in the best interests of those companies. The loan indirectly

benefitted transferring companies. Had the transfer not taken place, companies would have lost the Bank's support for their own funding arrangements.

- Held: As the **transfer was for the benefit of the group as a whole**, there was no breach of duty.

5) [Company knowingly participates in breach of Director's fiduciary duties](#)

***Green v Bestobell Industries Ltd [1982] WAR 1***

- Green was Manager of Bestobell Ltd. He incorporated Clara Pty Ltd. He made Clara Pty Ltd to submit tender prepared by himself for construction works, in competition with his employer. Clara Pty Ltd won the tender. Bestobell Ltd was the third lowest tender.
- Held: Bestobell Ltd could obtain an account of profits from Clara Pty Ltd.

## TUTORIAL EXERCISE NO 2

## Question 1

**Bill**, a property developer, bought a large block of land in Perth for \$200,000 in January. Bill then approached **Jack**, a real estate agent, to help sell some "off the plan" home units. The units were to be developed and sold in two stages by a company called **Propco Pty Ltd**, which had not then been formed.

The plans for the units were prepared and on 20th March **Jack** sold one of the stage two units to **Amy** for \$65,000 under a contract which he signed as "**agent of Propco Pty Ltd**".

**Propco Pty Ltd** was not incorporated until 7th April. The directors are two business colleagues of Bill. There are four shares issued, one held by **Bill** and three held by **Ben**.

In May **Bill** sells the land to **Propco** for \$350,000 and building of the first stage units then commences (start using).

In early June **Propco** discovers the local council will not give planning permission for stage two and that part of the development does not proceed.

**Amy** is furious. She is demanding from **Jack** the return of a \$6,500 deposit paid by her to him and damages. **Ben** is also concerned about the propriety of the sale of the land by **Bill** to the company. Recently, the company held an extra-ordinary general meeting where the original directors were removed and new directors appointed. **Ben** wants the new directors to take action against **Bill**.

Advise Bill and Jack of any liability arising from their actions.

Bill & Ben                  promoters' duty	Jack & Amy                  pre-registration contract
Propco 4 shares - Bell (1 share) - Ben (3 shares)	Bill approach Jack to help selling unit 2stages
Bill sold land to P - \$350k - 1 <sup>st</sup> stage	J sold a unit to A - \$65k
2 <sup>nd</sup> stage not proceed	

Promoter - Someone who is:

- actively involved in formation of a company (arranges for BOD)
- passive shareholder with expectation that she will received profit

## *Tracy v Mandalay*

- A company RSC sold its owned land to a new company Mandalay. The general public bought shares in Mandalay and the money was used to purchase the land and shares from RSC and its shareholders respectively.
- Held: shareholders of RSC are promoters of Mandalay and owed duties to Mandalay.

**Bill** – has share in Propco Pty Ltd

**Jack** – as he sign contract under “agent of Propco Pty Ltd”

## Duties of Promoter

- Duties are owed to the Company
- They are:           no conflict of interest  
                              no secret profit

duty of disclose  
No secret profit (more relevant)

### **There is a contract between Bill and Propco**

- Although Bill is not entirely liable for the stage two development process, Propco have used the land sold by Bill for stage one development.

### **When the company was incorporated, Bill appointed the Directors.**

- *Erlanger v New Sombrero Phosphate Co (not too much relevant to this case)*
  - Syndicate purchased island which has supposed to contain minerals. Company formed to purchase land. Head of syndicate nominated directors of company. Investment not profitable. New Board of Directors sued the syndicate.
  - Held: contract rescinded/cancelled. There must be an independent Board and full disclosure of promoters' interest.
- *Gluckstein v Barnes (most important in this case)*
  - Gluckstein was a member of a Syndicate. The Syndicate bought the mortgage over the property at a discount of 20,000 pounds. The property itself was purchased for 140,000 pounds subject to the mortgage. Syndicate formed the Company Olympia and the property was bought by company from syndicate for 180,000 pounds. Full value was paid for the mortgage. Profit of 40,000 pounds was disclosed in prospectus but the discount of 20,000 pounds (on the mortgage) was not disclosed.
  - Held: The liquidator of Olympia was able to recover the 20,000 **secret profit**. Promoters failed to disclose **all** profits. Disclosure to Board comprised of other members of the syndicate was not sufficient. Disclosure must be to independent board or to ultimate shareholders of company.

### **Common Law Remedies**

1. Rescission
2. Account of profits
3. Constructive trust

In Bill and Ben, there's no independent Board, disclosure would be to shareholders (Bill & Ben). Therefore the contract of the sale of land cannot be rescinded because the owners are not returned to their original position, as the land has already been transformed.

### **Jack & Amy** 3<sup>rd</sup> paragraph

**S 131(1)** – If a person enters into contract on behalf of or for the benefit of proposed company, company becomes bound by the contract if the company is later **registered and ratifies** the contract within a reasonable time.

### ***Bay v Illawarra Stationery Supplies Pty Ltd***

**S 131(4)** - Is Jack liable – Ratification of 2<sup>nd</sup> stage. No issue with 1<sup>st</sup> stage . by taking deposit, contract is already ratifying.

### **S 131(2) & s 131(3)**

Jack is an agent of Bill, sign a contract on behalf of or for the benefit of proposed company which is Propco Pty Ltd. Therefore the company should be liable towards Amy, but not Jack under s 131(1). Unless s 132(1) is used, Amy, the outsider will always be protected.

### **Structure How to answer the question 1**

#### **Classify the parties**

#### **Common Law Corporation Act**

which duty relevant to the question

**A. Bill**

1. Classify
2. Duties – apply?
3. **Application – identify the duty, giving the fact (suggest Bill... However might not apply because.....)**
4. Remedies / Conclusion

**B. Jack**

**Director duties come out with more details**

**Question 2**

**Amanda** built a development of four units. She set up a **proprietary limited company** (called "**Melrose Pty Ltd**") which owned the entire property and issued shares to herself and three others, **Billy**, **Allison** and **Jane**, who were also tenants of the property. All four were appointed directors of the company.

The constitution contains the following two provisions:

- (i) "Each director of the company shall be entitled to rent a unit while a director for personal use, but no director other than Amanda, is permitted to sublet to an outsider without the unanimous[全体一致的] approval of the directors"
- (ii) "No internal walls are to be knocked down or altered[改变] without the unanimous approval of the directors".

The following events have happened:

- (a) **Amanda** proposes to sublet the flat to **Alan**. However, **Billy**, **Allison** and **Jane** do not wish her to do this and recently passed the following special resolution at a general meeting:

"That provision (i) be amended[修订] by deleting the words 'other than Amanda'".

Advise Amanda.

**S 135(1) – Replaceable Rules (RR) does not apply to a proprietary company while the same person is both its sole director and sole shareholder.**

**S 135(2) – RR can be displaced[置换] or modified by the company. It allows the company to change the rules unilaterally.**

**S 136(2) - the company may modify or repeal[废除] its constitution, or a provision of its constitution, by special resolution.**

**S 136(3) – the company constitution may provide that the special resolution does not have any effect unless a further requirement specified in the constitution relating that modification or repeal has been complied with.**

**S 140(1) - Constitution and the replaceable rules have the effect of a statutory contract between:**

- a) Co and each member
- b) Co and director/co secretary
- c) Member and each other member

- (b) **Jane** now wishes to renovate the inside of the unit by knocking down the kitchen wall. **Allison** objects to this.

Advise Jane. (relevant with director)

- Amend the clause through special resolution, Alteration (general meeting 75% majority) (75% of all vote cast)
- Although Allison objects, if another 3 shareholders include Jane herself agree, they still can amend the clause.

**S 136(2)** - the company may modify or repeal[废除] its constitution, or a provision of its constitution, by special resolution.

**S 136(3)** – the company constitution may provide that the special resolution does not have any effect unless a further requirement specified in the constitution relating that modification or repeal has been complied with.

**S 140(1)** - Constitution and the replaceable rules have the effect of a statutory contract between:

- a) Co and each member
- b) Co and director/co secretary
- c) Member and each other member

### Oppression

(hard part be careful)

### Question 3

**Howard Ltd** has a constitution which provides that **John**, who is a shareholder, shall be managing director for life. **Beazley Ltd**, which has acquired 90% of the shares of Howard Ltd, intends to delete this provision and remove John from the Board of Directors altogether.

Discuss whether:

- (a) John can prevent this alteration[修改] of the constitution.

**S 136(2)** - the company may modify or repeal[废除] its constitution, or a provision of its constitution, by special resolution. GM must be pass a special resolution: 75% majority.

**Gambotto v WCP Ltd (1995) 182 CLR 432**

- Majority shareholder owned 99% of Company. Altered Constitution to allow for compulsory acquisition by majority shareholder.
- Held: alteration invalid.

**S 203D(1a)**

Can't prevent because there is 90% of the object vote. Public company

- (b) If the constitution is changed and John is dismissed[解雇] from his post as managing director does he have any form of legal redress[补救]?

**Shuttleworth v Cox Bros (Maidenhead) Ltd [1927] 2 KB 9**

- Constitution provided that Shuttleworth was to be Director for life.
- Constitution amended to allow removal by all directors.
- Held: Dismissal valid and no damages payable

Can't prevent, no breach in constitution, therefore no compensation.