

**LAW5011 –  
PRINCIPLES OF COMPANY  
LAW**

**CHECKLIST  
STREAM 1**

**T3 2017**

# BUSINESS STRUCTURES

D has transformed his business from a \_\_\_\_\_ [partnership] to a company. This can be beneficial for a number of reasons, because:

## A sole trader

Has no limit on personal liability, that is, his personal assets remain at risk

Furthermore, there are tax consequences as the personal tax rate is higher than a co rate

However, a co is a separate legal entity, has a simple and cheap registration process has tax rate benefits

## A partnership

Is not a separate legal entity, so therefore his personal assets may be at risk

However, a co is a separate legal entity, has a simple and cheap registration process has tax rate benefits

# INCORPORATION AND ITS EFFECTS

## Introduction

- A co is registered under the *Corporations Act* (s 9)
- A co is an artificial entity recognised by law as a legal person with its own rights and liabilities, treated like a person (s 124)
- A corporation includes a co, any body corporate and an unincorporated body that may sue or be sued, or hold property (s 57A)

## Process

- The process of registration involves lodging an application with ASIC using ASIC Form 201 (s 117)
- ASIC may then register the co, give the co an ACN and issue a certificate of registration (s 118(1))
  - The certificate of incorporation is conclusive evidence of registration (s 1274(7))
- A co comes into existence at the beginning of the day it is registered (s 119)
- A co continues to exist until deregistered by ASIC (s 601AD(1))

## Company Names

- Must be stated on the application, unless the ACN is to be used (S 117(2)(b))
- Requirements for a valid company name:
  - Name must be available (S 148(1)(a))
    - A name is not available where it is identical to a name held or registered on the Business Names Register: s 147(1)(b) or it is unacceptable for registration under the regulations: s 147(1)(c)
      - A name is unacceptable if, in the opinion of ASIC, it is undesirable or likely to be offensive to members of the public OR it contains a restricted word or phrase
  - Name must contain “Limited” or “Proprietary Limited”, as appropriate (s 148(2) – or the abbreviation, s 149).
- A company must set out its name and ACN on all public documents (S 153)
- A person may reserve a company name for 2 months (with 2 months extensions) (S 152)

***Mention separate legal entity !!!***

# DEBT CAPITAL

Under the capital maintenance doctrine, a co is generally prohibited from reducing its share capital whilst the company is operating, except in the legitimate course of its business (*Trevor v Whitworth*)

## Exception 1: Capital Reductions

- This is a payment to shareholders that involves a return of shares to the company (which may then cancel the shares (like a buyback))
  - Cancels or reduces amount unpaid on partly paid shares
- **S 256D(1)**: A co must not reduce its capital unless it complies with **all** of the requirements in **s 256B(1)** → the reduction:
  - (a) Is fair and reasonable to the co's shareholders as a whole (*Catto*); and
    - If co has diff classes of shares → fair and reasonable test requires the court to consider the fairness of the proposed reduction as between diff classes → look at co's Constitution
    - Any consideration?
    - Court held it was fair and reasonable in *Winpar*
  - (b) Does not materially prejudice the co's ability to pay its creditors (*Re Fowlers*); and
    - Onus is on co to show reduction does not materially compromise its ability to pay its creditors
      - If co has sufficient capital, likely it won't materially prejudice co
    - Under **256C(5)**, co must lodge proposed capital reduction with ASIC – allows creditors to discover details of this (ASIC alert system)
    - Creditors can apply for injunction under **1324(1A)**
  - (c) Is approved by shareholders under **s 256C**:
    - Equal reduction (**256B(2)**): Ordinary resolution suffices (as no threat to minority)
    - Selective reduction: Needs a special resolution (75%) or by all ordinary shareholders
      - *Conclude: Likely to get a special resolution or not*
    - Cancellation of shares (**256C(2)**): Special resolution of all affected shareholders (*Winpar*)

*Unlike a selective buy back, the shareholder can be forced*

**Failure to comply – next page**

# DIRECTOR'S DUTIES

## Owed by directors and officers

- S 9: What is an officer
  - a) A director or secretary of the company
  - b) A person:
    - i. who makes, or participates in making, decisions that affect the whole, or a substantial part, of the business of the corporation; or
    - ii. who has the capacity to affect significantly the corporation's financial standing; or
    - iii. in accordance with whose instructions or wishes the directors of the corporation are accustomed to act (excluding advice given by the person in the proper performance of functions attaching to the person's professional capacity or their business relationship with the directors or the corporation)

Also includes receivers, administrators, liquidator, trustees

- Typically CEO, CFO, general counsel, company secretary, COO, CIO
- A person is not an officer unless they are acting in a managerial position (*Buzzle*)
- *Shafroon*: HC considered General Counsel an officer as he;
  - Participated in making decisions that affected the whole or substantially the whole of the company's business
  - Role was not merely administrative
  - Rejected the argument that you have to be the final decision-maker
    - You need to look at the role they undertook in the decision-making, even if someone else makes the final decision
  - Saw the fact he was an employee and not an external adviser as important

## ASK:

1. What decisions have the director's made?
  - Go decision by decision
    - Eg. Decision to terminate employment
    - Eg. Decision to issue shares
  - Not decisions by shareholders (eg. Resolution of shareholders)
2. Look at each of them, and say has there been a breach of duty
  - Have the directors informed themselves?
    - S 125(1): If Constitution contains an express restriction/prohibition (e.g. co may not borrow more than \$2m), the exercise of such power is not invalid merely because it is contrary to the Constitution

## **Duty Act in Good Faith in the Best Interests of the Company**

Applies to: Directors, officers, secretaries, receivers, administrators, liquidators

*The duty to act in good faith and in the best interests of the co is fiduciary (Bell Group) and statutory (s 181(1)(a)). These duties are essentially the same at general law and statute.*

### **Test**

D was acting in good faith if he believes he is acting in the best interests of the co (subjective) and the belief was reasonable (objective overlay – Owen J Bell Group)

- **‘Interests of the co as a whole’**
- However it may be argued that ‘no reasonable director could have reached that conclusion’ (Adler)
  - Having regard to the surrounding circumstances, it could be doubted that it was made in good faith (Bell Group)
- Can be a criminal offence is committed recklessly or intentionally dishonest (s 185(1)(c))

### **Director’s Arguments**

- How can the director justify the decision – why is it in the best interests?
  - Good opportunity for co [use facts what it is
  - If there is any sensible argument, can't impugn the director
    - Has the director informed himself as to the identity of the shareholder?
  - Eg. D will argue there was a difference in opinion over the proper direction of the co, and it was in the better financial interests of the co to expand/go in a new direction

*Conclude: A reasonable director is unlikely to believe this is acting in the best interests of the co because \_\_\_\_\_*

### **Who do They Owe Duty to?**

#### Individual Shareholders

- Hypothetical shareholder test → Not as individuals (Percival)
  - Must consider existing and future shareholders
- Sometimes ‘special fact’ fiduciary relationship means duties can be owed (Bunninghausen; Coleman)