

CLASSIFICATION OF COMPANIES

TEST 1: CLASSIFICATION ACCORDING TO LIABILITY?

Types of companies - : s 112(1)

Proprietary Companies	- limited by shares - unlimited with share capital
Public Companies	- limited by shares - limited by guarantee - Unlimited with share capital - No liability company

Option 1: Company Limited by Shares

A shareholder need not contribute more than the amount, if any, unpaid on the shares in respect of which the shareholder is liable as a member. s 162

-public companies: defined in s 9

-proprietary companies: defined in s 45A(1)

Option 2: Company Limited by Guarantee

-Does not have share capital – members are not required to contribute capital while the company is operating

-Members have their liability limited to the amounts they have undertaken to contribute to the property of the company in the event of its being wound up: s 517

-Guaranteed amount must be set out in the company's application for registration: s 117(2)(m)

-Disadvantage: does not raise initial or working capital from its members

-Convenient for clubs, charities and other non-trading companies whose capital needs can be met from outside sources, donations etc such as Bond Uni

Option 3: Unlimited Company

-Company whose members have no limit placed on their liability: s 9

Option 4: No Liability Company

- A public company may be registered as a no liability co. under s 162 if it:
 - Has a share capital, states in its constitution that its sole objects are mining purposes, has no right to recover calls made on its shares from a shareholder who fails to pay a call: s 112(2)

TEST 2: CLASSIFICATION ACCORDING TO PUBLIC STATUS?

Option 1: Public Company

- "Public co." means a company other than a proprietary company: s 9

Option 1a): Listed public co.

- Listed public co. are "disclosing entities" and subject to enhanced disclosure requirements (periodic reporting, continuous disclosure to ASX)
 - Also considered a "disclosing entity" where: issued securities to over 100 people and lodged a disclosure document with ASIC

Option 1b): Unlisted public co.

Option 2: Proprietary (Pty) Company

- Pty company must have no more than 50-none/ee shareholders: s 113(1)
- More onerous obligations are imposed on public companies

Option 2a): Small Pty Company

- A company is a Small Pty co. for a financial year if it satisfies at least two of the following three criteria: s 45A(2)
 - The consolidated gross operating revenue of the company and the entities it controls is < \$10 million
 - The value of the consolidated assets of the company and the entities it controls is < \$5 million; and
 - The company and the entities it control have fewer than 50 e'es

Option 2b): Large Pty Company

- A Pty company that does not come within the definition of "small Pty company" is regarded as a large Pty company: s 45A

A BREACH OF OBJECTS CLAUSE:

- s 125(2): an act is not invalid merely because it is contrary to or beyond any of its objects
- s 125(1): The exercise of power is not invalid merely because it is contrary to an express restriction or prohibition under the constitution
- Other options:
 - Legal action for dir breach of duty
 - Order for winding up of co on a just and equitable ground:

s461(1)(k)

A BREACH OF CO.'S CONSTITUTION / RR'S:

- Constitution and replaceable rules that apply to a company have the effect as a contract between: s 140(1)
 - The company and each member; and
 - The company and each director and company secretary; and
 - A member and each other member

Corporate Social Responsibility

The traditional view is that the company's primary goal is profit-maximisation. Dodge v Ford Motor Co (1919) the most famous authority, asserts: "A business corporation is organised and carried on primarily for the

profit of stockholders". Management's primary objective, then, was to maximise profits on behalf of the shareholder. (co funds spent on increased salaries + increase in # e'es = board breached duty; should have declared dividends instead)

Now it is argued that large corporations, in particular, should be sensitive not just to the desire of profits paid to their shareholders, but also to interests of "stakeholders" – E.g. to creditors, the employment security of their employees, the needs of consumers, minority groups and the public interest in, say, the environment. The environment, in particular, has been at the forefront of "corporate social responsibility" initiatives.

Definition: Define "corporate social responsibility" (CSR). It is corporate responsibility, citizenship, responsible business, sustainable responsible business (SRB) and corporate social performance. It is 'enforced' by self-regulation by companies. The 'corporates' become aware of the impact of the company's activities on employees, consumers, communities, the environment, as well as on the traditional stakeholders (the members and the creditors). CSR specifically includes the interests of the public in corporate decision-making – it is sometimes called observing the 'triple bottom line' – "People, Planet, Profit".

Debate: Duties to Shareholders v All stakeholders: The OECD Principles of Corporate Governance (2004) says: "the governance framework should recognise that the interests of the corporation are served by recognising the interests of stakeholders [including employees and creditors] and their contribution to the long-term success of the corporation."

Arguments Against CSR: Breaching s 181, possibly s182? Duties owed to present + future members
Undermines traditional profit goal; 'profit maximisation'
Could not serve 2 goals (shareholders + environment); if you did none would be properly served

Possible barrier to CSR: shareholder right to remove directors from office
ARGUMENTS SUPPORTING CSR:

Focusing on profit maximization may negatively affect the ability of the co to maximize sh'holder value (neglects longer term opportunities and issues)
Owe duties to both present + future sh'holders → future sh'holders benefiting
○ E.g. At some time in the future alternatives that do not produce greenhouse gas emissions may = necessity → investment in ways to reduce greenhouse gas emissions will help long term sh'holder wealth
○ Good publicity, marketing

Europe: Corporate law and the boardroom should pursue overall social efficiency. (This includes a broad range of stakeholders)

Australian and US position: Profit maximization only

Recently in Aus: Parliamentary joint committee found that there should be no amendment to the Corp Act to require the Directors to consider the public interest. Instead should be voluntary self regulation. It was their view that the Act already allows the Directors to have regard to broader stakeholders: Dodge Brothers Case

Likewise the US has not required CSR in its legislation (which is state by state) however the majority of the US states have allowed Directors to broaden the stakeholders. Statutes say that Directors may consider the impact on employees, consumers, communities.

Current UK position

UK has now adopted the European legal system. UK has enacted s172 which requires the directors to have regard to interests of the company's employees, long term consequences, relationships with customers and suppliers, the community, environment and reputation.

Japanese (Netherlands, Germany): Strongly involve employees. Job tenure was a very strong principle.

Netherlands: employees formed the majority of the upper supervisory board.

Globalization: The CSR debate has largely revolved around the conduct of multinational corporations (MNEs) and other large private companies which, due to their size, have the ability to significantly influence domestic and international policy and the communities in which they operate. Examples:

- Nike factories in Asia were criticised for extremely poor working conditions and for employing young children;
- James Hardie has been criticised regarding its failure to provide adequate compensation to people affected by asbestos related diseases resulting from the company's building products;
- Enron manipulated electricity in order to maximize profits at the expense of Californian citizens.

Unsuccessful CSR cases: Dodge v Ford Motor Co: Dodge brothers who were shareholders brought the case (owners of Dodge) against Ford (Henry Ford) to stop the directors spending the funds of the company in increased salaries for the workers and to increase the number of the employees. HELD: Directors breached duty and exceeded the power and the use of funds was to be stopped, and instead a dividend should be declared for the shareholders.

Parke v The Daily News: A company that controlled two newspapers sold one of them. The directors intended to distribute surplus proceeds from the sale among its employees by way of compensation for dismissal. A shareholder

brought an action to prevent these payments. HELD: proposed payments were not reasonably incidental to the carrying on of the companies business. They were gratuitous payments to the detriment of the shareholders and the company as a whole.

Successful Cases: Teck Corporation Ltd v Miller Cdn-SC Berger J.: "classical theory says that directors only consider interests of SH's. But today, the directors of a company CAN consider interests of employees and they will not be in breach of their duty. Directors can also have respect for other interests lying beyond SH (CSR) Facts: directors of Afton Mines issued shares in Afton in part payment for their involvement in the copper deposits of the company. Teck corp had a majority in Afton at the time. If the allotment went ahead their majority would be reduced to a minority below 50. The court held that the primary purpose of the transaction was to in the end to secure a good financial result deal with the copper for Afton mines. Signed contract with another company to exploit the copper, and to pay for new copper exploitation they needed the money. HELD: the directors were acting bona fide and best interests of the company they were not acting for a collateral or improper purpose.

REPLACEABLE RULE

s198A: states that the business of a company is to be managed by, or under the direction of, its directors who may exercise all the company's powers except any powers that the Corporations Act or the company's constitution requires the company to exercise in general meeting. s198(2): directors may exercise all company powers except any powers the Act or consti requires company to exercise at a General Meeting (amending constitution)

s9: A director is a person who is (1) appointed to the position of a director or (2) an alternate director and is acting in that capacity, regardless of the name that is given to their position. (b) Unless the contrary intention appears, a person who is validly appointed as a director if; (i) they act in the position of a director; or (ii) the directors of the company or body are accustomed to act in accordance with the person's instructions or wishes.

Starting with Automatic Self-Cleansing Filter Syndicate Co Ltd v Cuninghame: after the turn of 20th century, the courts have ruled that, if the powers of management are vested in the directors, then only they can wield those powers. The general meeting cannot usurp the board's role.

NRMA v Parker: 1) 200 members signed a petition, called a Requisition to Hold a General Meeting 2) At that meeting their proposed to pass a resolution directing the board to do things that were specifically left to the directors in the constitution. 3) Judge said, the board could properly refuse to call the meeting because of s198A. The comeback by the members could be to fire the board. Wait for the next annual general meeting or call a meeting and fire the board. Or they could change the constitution that had the power provision in it and to do that they would need 75%.

DIRECTOR'S DUTIES-Who are the company

3 Commandments: 1-Be honest 2- be loyal 3 be careful

Directors owe their duties to "the company". Thus the company should be the only party to enforce those duties.

What "stakeholders" should be borne in mind, when we talk of the "company"? Traditional best interest of the company=best interest of the shareholders as a collective group: Greenhalgh v Arden Cinemas

However dir can act best interests of comp as a commercial entity even though it not best interest for short term shareholders: Darvall v North Sydney Brick The Camac report addressed the need for dir to take into account the interests of stakeholders and the broader community when making corporate decisions. Such as environment e'es and corporate groups.

Interests of creditors: The traditional view-when you look at the company you are looking at present and future s'holders: Multinational Gas However in the case of West Mercia Safetywear when a company is insolvent the creditors interests override those of the s'holders.

Directors have a duty to exercise their powers in a way that does not prejudice the company's ability to pay its creditors Walker v Wimborne: In Australia, interests of creditors must be considered by directors, if the company is "near insolvent, or of doubtful solvency, or if a contemplated payment or other course of action would jeopardise its solvency": per Cooke J in Nicholson v Permacraft (NZ) Ltd (in liq)

-Also dir's duty not to prejudice creditors interests also arises in the context of corporate groups. For example one company in a group may lend money to another company in the same group. This happened in Ring v Sutton the lending company is in financial difficulties its dir prejudice the interests of the lending company's creditors if the interest rate on the loan is not on commercial terms or if the borrowing company is or comes insolvent and can't repay.

Sons of Gwalia Ltd v Margaretic Luka Margaretic lost \$26,288 of his retirement savings by buying shares in Sons of Gwalia Ltd, 11 days before it collapsed. Section 563A said: Member's debts are to be postponed until other debts and claims satisfied.

Margaretic claimed the company had breached its continuous disclosure obligations under s 674 and ASX Listing Rule 3.1 at the time he purchased the shares. And, because the non-disclosure of information had a material effect

on the price of the securities, Gwalia had engaged in misleading and deceptive conduct.

HELD: shareholder was right, and was to be regarded as a 'creditor' of Gwalia. And his claim was not postponed behind ordinary creditors of the company.

-Corporations Amendment (Sons of Gwalia) Act 2010 (Cth) amends the Corporations Act - says that in future all such shareholder claims will once again be subordinated.

-Amended s563A says a claim which "arises from a person buying, holding, selling or otherwise dealing in shares in the company [is] postponed [so that only once] all other claims made against the company are satisfied [can the] subordinate claim [be satisfied]".

-As less than 5% of insolvencies end up with a payout to unsecured creditors of 10c on the dollar or more, usually there will be no funds for distribution to shareholder creditors of an insolvent company.

Interests of Employees:

In Australia, directors are not required to pay attention to the interests of employees.

Cases Supporting unsupportive of e'es interests

Parke case: Column one: directors owe no duty to e'es.

Re M&W Raith: Senior manager died gave pension for life to widow- s'holders complained. Court said breach duty from d as interest of company did not include interest of manager and his widow.

Cases supportive: Teck Corporation Ltd v Miller - Berger J.: Directors can observe a "decent respect for other interests lying beyond those of the company's shareholders in the strict sense, that will not ... leave directors open to the charge that they have failed in their fiduciary duty to the company".

International: UK: UK s 172: (1) Duty to promote the success of the company: (b) the interests of the company's employees.

Interests of Corporate Groups:

-every company is a separate entity and its interests must be considered in all transactions, even though it is part of a group

Under s 187 it states that acting for a WHOLLY OWNED subsidiary then it can be considered in good faith to act in that company's interests as long as it does not result in insolvency or the sub is insolvent: Re Spargos Mining NL

Jenkins v Enterprise Gold Mines NL: Australian courts keep a strict approach to separate legal personality in corporate groups – they are reluctant to "pierce the corporate veil" for the benefit of the parent company or of the creditors.

Adams v Cape Industries: subsidiary companies, though creatures of their parent companies, are separate entities.

Walker v Wimbourne:

Issue: Could the funds of one company in a corporate group be used to satisfy the debts of another member of that corporate group.

HELD: Each company in a corporate group is a separate legal entity and therefore the funds of one company cannot merely be shifted as if they are the property of another company in that same corporate group.

DIRECTOR'S DUTIES - LOYALTY & HONESTY

A director or other officer of a corporation must exercise their powers and discharge their duties: in good faith in the best interests of the company, and for a proper purpose → both a statutory duty under s181 and a fiduciary (common law) duty

Best interests of co = best interests of shareholders (present + future: Darvall v North Syd Brick) as a collective group: Greenhalgh v Arden Cinemas

A civil penalty provision: s1317E

A criminal offence if dir is reckless or intentionally dishonest: s184

Duty to act bona fide in the interests of the company CL duty:

Can not be only test though as Bowen LJ explained- bona fides cannot be the sole test, otherwise you might have a lunatic conducting the affairs of the company and paying its money with both hands in a manner perfectly bona fide yet perfectly irrational.

s.181 (1)- duty to act in good faith, in best interest of corporation and for proper purposes.

181 Good faith—

- (1) A director or other officer of a corporation must exercise their powers and discharge their duties:
 - (a) in good faith in the best interests of the corporation; and
 - (b) for a proper purpose.

The courts consider two matters:

1. The objective purpose for which the pwr was granted &
2. The purpose which actually motivated the exercise of the pwr. Howard Smith Ltd v Ampol Petroleum

Objectively:

Pennycuik Charterbridge v Lloyds Bank says when deciding if a director has acted in the best interests of a company you judge it objectively. "whether an intelligent and honest man in the position of a director of the company concerned, could, in the whole of the existing circumstances have reasonably believed that the transactions were for the benefit of the company."