

CORPORATIONS LAW EXAM NOTES

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Conflict of interest:

No conflicts: applies where director has conflicting interests and conflicting duties

No profits: applies where the director usurps a corporate opportunity, as well as where they make a more straightforward profit

Difference between general law and statutory duties

Boardman v Phipps: There is a fundamental rule of equity that a person in a fiduciary capacity must not make a profit out of his trust, which is part of the wider rule that a trustee must not place himself in a position where his duty and his interest may conflict' per Lord Upjohn

No conflicts rule:

Statutory duty:

CA s 191(1) p 250: A director of a company has a duty to disclose a material personal interest that relates to the affairs of the company to other directors

- **CA s 53 p 138:** Affairs of a body corporate
- **CA s 191(3) p 251:** Content and timing of notice
- **CA s 191(1A) p 250:** Strict liability offence (criminal) (may be liable to a fine of \$1,700 or 3 months imprisonment if mens rea is proved BRD)
- **CA s 191(4) p 250:** A contravention doesn't affect the validity of any act, transaction, agreement, instrument, resolution or other things

CA s 191(2) p 250: Circumstances where the director doesn't need to give notice of the interest (even if it is a material personal interest)

- (a) Particular types of interests
- (c) Has already given notice and the nature or extent of the interest hasn't materially increased
- (d) Has given a standing notice under **s 192** and the notice is still effective

CA s 192(1) p 251: Director who has an interest in a matter may give other directors standing notice of the nature and extent of the interest

- May be given at any time, whether or not the matter relates to the affairs of the company at the time it is given, and before the interest becomes a material personal interest
- **CA s 192(2)(a) p 251:** Content of notice
 - Level of detail required was considered in **Camelot v McDonald**
- **CA s 192(2)(b)-(4) p 251:** Method of giving notice
- **CA s 192(5)-(6) p 251:** When standing notice does and doesn't have effect
- **CA s 192(7) p 252:** A contravention doesn't affect the validity of any act, transaction, agreement, instrument, resolution or other things

CA s 193 p 252: s 191 and s 192 have effect in addition to (a) any general law rule about conflicts of interest and (b) a provision in the company's constitution restricting conflicting duties or interests

- Compliance with one set of obligations will not guarantee compliance with the other – if a company's constitution has conflict requirements that aren't complied with, compliance with **s 191** won't prevent the transaction from being voidable

Pty companies:

CA s 191(5) p 250: s 191 doesn't apply to a Pty company that has only 1 director

CA s 191(2)(b) p 250: The director doesn't need to give notice of the interest under **s 191** where the other directors are aware of the nature and extent of the interest and its relation to the affairs of the company

CA s 194 p 252 (RR): If a director has a material personal interest that relates to the affairs of the company and they have properly disclosed it under **s 191** or don't need to disclose it under **s 191**, the (a) matters, (b) transactions and (c) benefits related to the interest may proceed, and (d) the company cannot avoid the transaction merely because of the interest

Public companies:

CA s 195(1) p 252: A director who has a material personal interest in a matter being considered at a directors meeting must not (a) be present while the matter is being considered or (b) vote on the matter

- **CA s 195(1) p 252:** Strict liability offence (criminal) (attracts a fine up to \$850 if mens rea is proved BRD)
- **CA s 195(4) p 250:** A contravention doesn't affect the validity of any resolution
- **CA s 195(1A) p 252:** (1) doesn't apply if (b) the interest doesn't need to be disclosed under **s 191** or (a):
 - **CA s 195(2) p 253:** Participation with approval of other directors
 - **CA s 195(2) p 253:** Participation with ASIC approval
 - **CA s 196(1) p 253:** ASIC power to make declaration that the director may be present and/or vote, but must be (a) less than quorum without that director AND (b) matter must be dealt with urgently
 - **CA s 196(3) p 253:** ASIC power to make order in respect of a class of Public companies, directors, resolutions or interests
 - **CA s 196(2), (4)-(5) p 253:** Procedural requirements
- **CA s 195(5) p 252:** Where (1) doesn't apply because there aren't enough impartial directors to form a quorum

Defining material personal interest:

- Material: something having the capacity to influence the vote of the particular director upon the decision to be made
- Personal: where a director stands to benefit personally from a decision (not conflicting duties ie where the director is also a director of a rival company)

McGellin v Mount King Mining NL:

- The interest must be a substantial interest
- Must be an interest that a reasonable person would believe is likely to influence the director in their decision making
- If it has that effect, it is irrelevant whether the interest is direct, indirect, vested or contingent

Camelot Resources v McDonald

- M operated a private consultancy business, had particular expertise because of this business
- M was invited to join C's board as an executive director
- M agreed on the basis that the company purchase his business through cash and shares
- This required disclosure because there was a personal benefit for M
- At a meeting where M wasn't present, there was a suggestion that C takeover M's consultancy business for a price
- Notice was inadequate under the equivalent provision, therefore M is guilty of breach
- There must be sufficient detail and the director in conflict must actually attend the meeting
- Disclosure must be in sufficient detail for the board as a whole to understand the scope of the benefit and potential profit to the director
- It is insufficient for others to make the disclosure or make suggestions at a board meeting the director didn't attend
- Only then a proper decision can be made as to whether the arrangement should go ahead
- Despite the failure to comply with this obligation being innocent, the disclosure obligations were intended to be strictly adhered to

MEMBERS REMEDIES

Shareholders (especially minority) have difficulties in getting redress when directors breach their duties, because:

- The general law principle is that loss is suffered by the company, and not by an individual member
- It may be difficult to get the company to sue, because the defaulting directors remain in charge
- Majority shareholders may use their voting power unfairly because they are permitted to vote in their own interests (because they have made an investment), even to ratify a breach of their own duties as directors
- Equity provides redress only in narrow circumstances (eg fraud on the minority)

Statutory derivative action:

Source of right	CA s 237(2) p 312: Where court may grant application CA s 237(3) p 312: Where grant is not in the best interests of the company <ul style="list-style-type: none">• CA s 237(4) p 313: Where person is a third party
Standing	CA s 236(1) p 311: A person may bring or intervene in proceedings on behalf of a company if they are (a)(i) a member or former member, or (a)(ii) an officer or former officer, and (b) has leave under s 237 <ul style="list-style-type: none">• CA s 236(2) p 311: Proceeding is brought in the company's name CA s 237(1) p 312: People mentioned in s 236(1) may apply to the court for leave to bring or intervene in proceedings CA s 238(1) p 318: Substitution of another person for the person granted leave
Remedy	<ul style="list-style-type: none">• Remedy is awarded to the company
Advantages	<ul style="list-style-type: none">• Provides officers and former officers with a means to obtain a remedy for the company, in circumstances where the company itself is unlikely to bring the action• The potential to proceed against both directors and third parties (eg for breach of contract causing the company to suffer losses)• Strengthens shareholder rights
Disadvantages	<ul style="list-style-type: none">• Cannot bring when a company is in liquidation or insolvent

Effect of company being in liquidation:

- **Chahwan v Euphoric:** SDA's generally aren't available with respect to a company in liquidation because it's not in the company's best interests, but the court does have an inherent power to authorise a creditor or contributory of a company in liquidation to take proceedings in the name of the company (has been doubted)
- Sections 236 and 237 are silent as to whether the application must be on behalf of a solvent company, so the court had to look at policy and purpose of SDA provisions
- Now, cannot use SDA's when a company is in liquidation for insolvency, because it is not in best interests of the company
- If the company is insolvent or in liquidation, only the liquidator can decide whether the company should take or continue action to recover damages or secure other relief for an injury done to the company
- To allow SDA's to proceed when a liquidator is standing in the shoes of the company would interfere with the liquidators role and with interests of creditors

Effect of ratification by members:

CA s 239(1) p 318: If the members of the company ratify or approve the conduct, it (a) doesn't prevent a person bringing or intervening in proceedings on behalf of a company and (b) doesn't mean the proceedings brought or intervened with must be determined in favour of the defendant of that leave must be refused

- **CA s 239(2) p 318:** But the court may take ratification into account, including (a) how well-informed the members were and (b) whether their ratification was for a proper purpose

Power of the court to grant leave:

CA s 237(2) p 312: To grant leave, the court must be satisfied that:

- (a) Probable that the company won't itself bring proceedings
 - May be discharged by the applicant demonstrating the wrongdoer has a dominant influence on the board
 - May be inferred from contents of administrators report **Charlton v Baber**
 - May be inferred from time elapsed since the company said they would investigate the allegations in deciding whether to take action (see **True Value Solar** for significance of company investigation)
- (b) The applicant is acting in good faith
 - Court needs to be satisfied that the applicant isn't pursuing a private interest as a collateral purpose
 - The applicant may have motives that go beyond mere personal gain ie a sense of responsibility to creditors
Swansson v Pratt, Chahwan v Euphoric
- (c) Leave to sue is in the company's best interests
 - Is as opposed to 'appears to be' – a high standard **Swansson**
 - A company might have sound business reasons for not pursuing a cause of action and its management might legitimately have decided that the best interests of the company would be served by not taking action (eg where nominal loss from a breach)
 - Involves consideration the company's separate and independent welfare **Charlton v Baber**
 - The court should focus on the true nature and purpose of the proceedings
 - Satisfaction may depend upon the company being protected as to costs (that the applicant bear the costs of the SDA and take the risk of an adverse costs order) especially where the company has limited financial resources or personal and derivative claims are intermingled **Charlton v Baber**
 - The fact that the matter may be able to be pursued via proceedings other than an SDA (ie an oppression action) doesn't indicate that the application wasn't made in good faith or the best interests of the company
Chahwan v Euphoric, Ragless v IPA Holdings, True Value Solar Holdings

Rebuttable presumption that grant is not in the best interest of the company:

CA s 237(3) p 312: Where proceedings are against a third party, there is a rebuttable presumption that granting leave isn't in the best interests of the company where (b) the company has decided certain things and (c) all directors participated in that decision properly (same as business judgment rule)

- Court must presume these factors are true unless rebutted by evidence to the contrary (ie that there is a serious question to be tried that these conditions aren't satisfied)
 - Recognises that where the claim isn't against one of the directors, the directors will generally be better placed than a court to determine whether bringing the action against a third party is in the company's best interests
 - **CA s 237(4) p 312:** Definition of a third party
 - A former director will become a third party if the director ceased to hold office more than 6 months before the proceedings begun (the applicant must adduce evidence to rebut this presumption)
 - **CA s 228 p 294:** Definition of a related party
- (d) There is a serious question to be tried
 - Need a cause of action to pursue eg breach of a directors duty
 - Doesn't require the applicant to prove substantive issues, just to show that proceedings should be commenced
 - Similar to the kind of inquiry undertaken by a court on an applicant for an interlocutory injunction **Ragless**
 - Ask whether the applicant is able to identify the legal or equitable rights to be determined at trial **Ragless**
 - The court shouldn't probe the issue of serious question to be tried, it is merely a screening process to exclude cases with insufficient prospects of success (ie frivolous or vexatious claims) **Chahwan v Euphoric**
 - If there are several complaints, each is addressed separately **Charlton v Baber**
 - (e)(i) The applicant advises the company at least 14 days prior to application, or (ii) it is appropriate for the court to grant leave even though notice wasn't given to the company
 - Allows the company time to address the applicant's concerns prior to the court hearing the matter
 - Failure by the company to take action during this time may support the court finding that it is probable the company wouldn't itself institute proceedings

General powers of court:

CA s 241(1) p 318: The court may make any order and give any directions that it considers appropriate in relation to proceedings (procedural, not substantive)

- Power to appoint an independent investigator (d) is similar to the order made under the oppression remedy in **Re Spargos**
- Addresses barrier that shareholders who generally don't have access to board papers, so it is difficult for them to obtain sufficient information about the company's internal decision-making process in order to know whether litigation is warranted
- These court powers may be used to address the conflict of interest the applicant has in bringing proceedings on behalf of the company against a company controlled by the other shareholder, where the liquidator indicates the company may also have claims against a company controlled by the applicant
Ragless

CA s 240 p 318: Proceedings brought or intervened in with leave mustn't be discontinued, compromised or settled without leave of court

- Deals with the possibility that defendants might pay the applicant to settle the proceedings, in circumstances where it would be in the company's best interests for the proceedings to continue

CA s 242 p 319: The court may make any orders it considers appropriate about costs, including a costs indemnification, for (a) the person granted leave, (b) the company, or (c) the other party to the proceedings

- Courts rarely use the power to indemnify the applicant for costs of the SDA
- Usually, undertakings have been offered and orders have been made for applicants to take responsibility for the costs of bringing SDA's and for any adverse costs order that is made if the application is unsuccessful

Swansson v Pratt

- Ms S was director and shareholder of RAPP (family investment company)
 - Shareholders were S, S's mother (M) and S's husband (H), directors were Ms S, H, and S's brother (P)
 - In seeking permission for an SDA, Ms S claimed H arranged with Ms S and M to transfer funds from RAPP to himself for his personal benefit in breach of his fiduciary duties
 - However Ms S had signed the deed for that transactions
 - Court was aware that P and M wouldn't bring proceedings against H
 - P asserted that the purpose of Ms S's application was to get a larger property settlement in her divorce from H
-
- Where there is no obvious benefit to be gained by the company from the suit, the court will scrutinise the applicants reasons
 - If evidence is raised that shows a lack of good faith, the burden is on the applicant (Ms S) to satisfy the court of good faith
 - There is good faith in a shareholder seeking return of property, because that would increase the value of the shareholding, or in a director in the interest of seeing the company well managed
 - The court wasn't satisfied that Ms S had rebutted the possibility that her reason for bringing it was in good faith
 - Where a creditor (who happens to have standing under s 237 in another capacity) brings a derivative action solely to place the company in a financial position to repay the debt to him (rather than to recover property for the company), he isn't acting in good faith
 - Applications where the applicant has no financial interest in the company and no present involvement in its management need to be scrutinised with particular care (cf **Charlton v Baber**: the fact that the applicant was unlikely to benefit financially from a successful action is irrelevant to his bona fides)
 - Palmer J: good faith involves two interrelated factors; (applied in **Charlton v Baber**)
 1. Whether the applicant honestly believes that a good cause of action exists and has a reasonable prospect of success of winning the legal action (cannot drain company's money)
 2. Whether the applicant is not seeking to bring the derivative action for such a collateral purpose as would amount to an abuse of process

Chahwan v Euphoric

- C (a creditor) was seeking to bring derivative proceedings to establish that certain property was held by E on CT for the company, in order to ultimately establish that E held the property on CT for himself
- C's personal interest would preclude the company and its unsecured creditors from benefiting from the proposed action, and the action would accordingly not be in the best interests of the company
- The applicant must suffer a real and substantive injury dependent upon or connected with the applicant's status as such shareholder or director if a derivative action were not permitted
- It might be a positive indication of the good faith of a shareholder if he or she sought to institute a derivative action to restore value to his or her shares in the company
- Opposite to common law cause of action, where the person who suffers loss is the company and any loss suffered by shareholders flowed from the company but didn't concern the courts
- There could be a lack of good faith where the applicant's conduct falls short of an abuse of process, but seeks to further the applicant's personal interests rather than the interests of the company as a whole
- Where a creditor (who happens to have standing under s 237 in another capacity) brings a derivative action solely to place the company in a financial position to repay the debt to him (rather than to recover property for the company), he isn't acting in good faith
- SDA's generally aren't available with respect to a company in liquidation, but the court does have an inherent power to authorise a creditor or contributory of a company in liquidation to take proceedings in the name of the company (has been doubted)

Ragless v IPA Holdings

- R and C were directors, secretaries and only shareholders of IPA
- R and C had their own companies which were JV partners, from which IPA received funds
- Each in charge of the sales division and manufacturing division
- Breakdown in relationship, R applied for permission to run an SDA
- R alleged C's company had used IPA assets without IPA authorisation and hadn't paid IPA funds due for the lease of the assets
- R claimed IPA's action against C would be a recovery of earnings made, interests on earnings and any other damage caused to the company caused by unauthorised use of its assets
- IPA had no creditors, so best interests couldn't be assessed by reference to the potential return to creditors
- The court found it was in the company's best interests to grant leave, because the action would resolve a deadlock between the JV's which was frustrating the capacity of the liquidator to wind up the company
- Court was satisfied R had an honest belief the company had a good cause of action and reasonable prospects of success
- The court has an inherent power to authorise a creditor or contributory of a company in liquidation to take proceedings in the name of the company

True Value Solar Holdings

- F was a shareholder of TVSH, personally and through his company, G was a director of TVSH
- F and his company held a small proportion of shares (minority), G and MW held 60%
- F applied for SDA leave against G and a corporate group associated with G, MW
- F argued TVSH had suffered loss and damage as a result of certain contracts entered into by the company, which had diverted business opportunities away from TVSH or imposed a prejudicial purchasing regime on TVSH, and that the purpose of the contracts was that MW would receive benefits from the arrangement
- G had breached his duties by favouring MW over TVSH
- G and MW argued that because F had sought a s 232 order, he was barred from seeking a s 237 remedy (that they are mutually exclusive remedies)
- F's SDA standing upheld; there is no barrier to seeking an SDA and an order to remedy oppression
- There are different rules of standing and different remedies
- Oppression isn't a claim on behalf of the company, so is inadequate to deal with the complaint fully as remedies only flow to the applying individual
- Granting an SDA for suing a defaulting director was a legitimate role of the SDA process in allowing shareholders to take action and wait for ASIC