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'Piercing the veil' cases

'Piercing the corporate veil'

***** Trying to hold [DIRECTOR] liable rather than the [COMPANY]**

(A) FRAUD / IMPROPER PURPOSE

The issue is whether the corporate veil (**Salomon**) can be lifted due to _____ (fraud / improper conduct) on behalf of [DEFENDANT] (**Guildford Motor**).

Here, [DEFENDANT's] conduct constituted fraud because _____ (apply facts)

- ... analogous to **Gilford Motor**, [DEFENDANT] set up [COMPANY] to **breach or avoid equitable or legal obligations**, those being _____ (apply)
- ... analogous to **Gilford Motor**, [DEFENDANT] set up [COMPANY] to **poach clients from his/her former employer**. This was fraudulent because it allowed [DEFENDANT] to circumvent a restraint clause in an employment contract.

- ... analogous to Jones v Lipman, [DEFENDENT] transferred land to a newly acquired company at significantly lesser sum to prevent an action for specific performance.
- ... analogous to Re Darby; Ex parte Brougham, two undischarged bankrupts promoted a company which derived secret profits on the sale of grossly overvalued assets to another company which it had promoted
- ... analogous to X Bank v G, [DEFENDENT] created an elaborate structure of corporations and trusts to put assets beyond [PLAINTIFF's] reach.

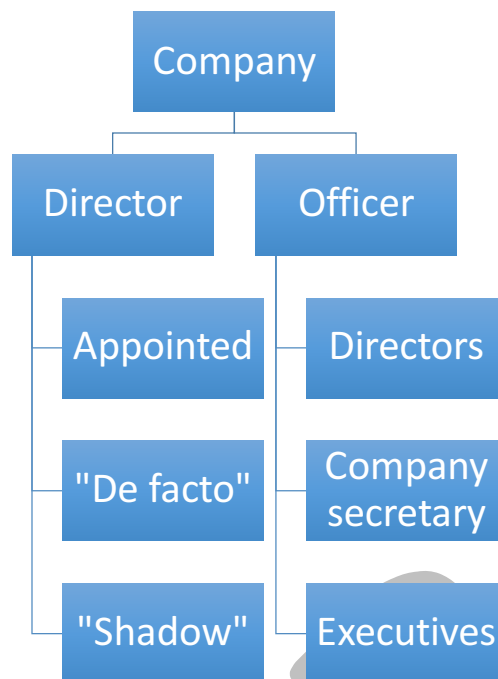
Nonetheless, it could be argued that [DEFENDANT's] conduct is insufficient to establish fraud because:

- ... a fair and reasonable price was paid in the transaction (Salomon)
- ... an independent board of directors was absent (Salomon)

Conclusion

Tentatively, the corporate veil will be pierced due to [DIRECTOR's] fraud/improper conduct. [DEFENDANT] may be held liable for [COMPANY's] conduct.

The “director” or “officer” TEST (useful in most sections)



DIRECTOR / ALTERNATE DIRECTOR

... [DEFENDANT] is a director of [COMPANY] (s 9(a)(i)). [*He/she is therefore subject to director's duties*].
 ... [DEFENDANT] is an **alternate director** of [COMPANY] and acting in that capacity (s 9(a)(ii)).

- ... It is irrelevant that [DEFENDANT's] position is technically a _____ (apply) because he/she is still a director of the company.

DE FACTO DIRECTOR (describes what exist in reality, even if not *legally* recognised)

Whilst [DEFENDANT] is not a director, he/she may be deemed a **de facto director** in the sense that he/she **'acts in the position'** of a director (s 9(b)(i)). The court will look to 'the nature of the functions or powers' exercised by [DEFENDANT], and the extent of the exercise of their powers (*Grimaldi*). Here, _____ (apply factors)

- ... [DEFENDANT's] relationship with [COMPANY] **evolved** over time into that of a director, as evidenced by _____ (apply)
- ... [DEFENDANT] performed the role and functions that constitute him/her a director for a **limited period of time**, as evidenced by _____ (apply)

○ NB: A company can be a *de facto* director

| Likely factors | Unlikely factors |
|--|--|
| [DEFENDANT] held a general and unconstrained consultancy over _____ [DESCRIBE FUNCTION] (<i>Grimaldi</i>). | [DEFENDANT] held a limited and specific consultancy over _____ [DESCRIBE FUNCTION] |

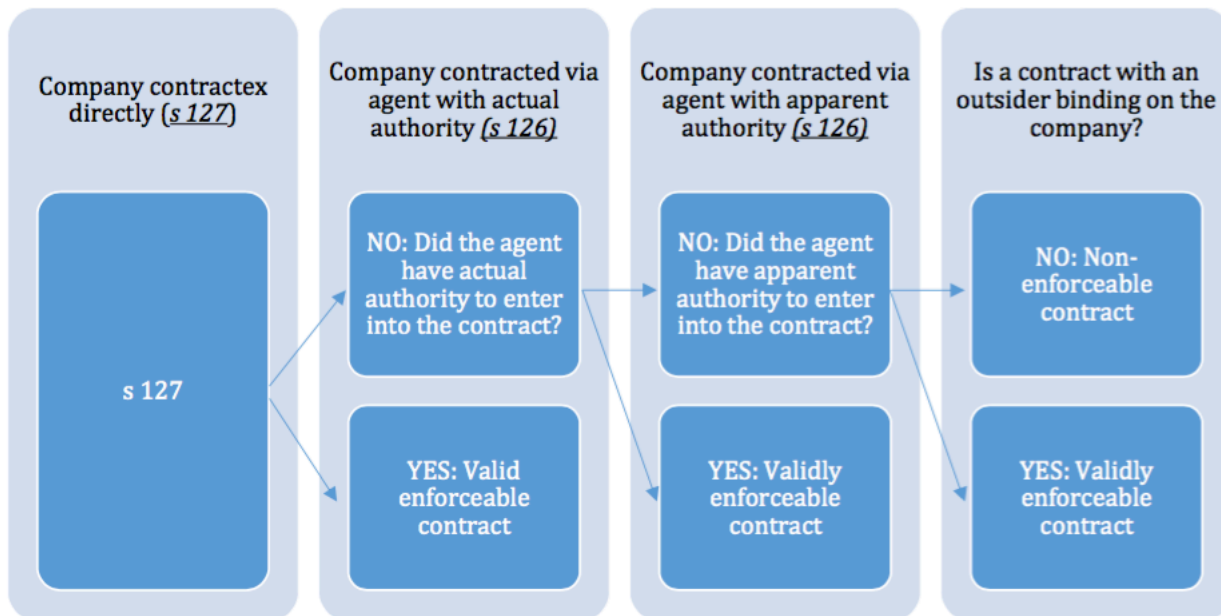
| | |
|--|-------------------------------|
| <p>[DEFENDANT] had been authorised to perform _____ [describe function] (Grimaldi; DCT v Austin). This would lead a reasonable third party dealing with [DEFENDANT] to believe that he/she was acting as a director</p> <ul style="list-style-type: none"> ▪ <i>Eg. negotiating major interests</i> | Grimaldi; DCT v Austin |
| <p>[DEFENDANT] continued to act in a mistaken belief, shared by fellow directors, that he/she was a director, despite their directorship having been terminated (Mistmorn v Yasseen).</p> | |

OFFICER

[DEFENDANT] is not a director and cannot be deemed a de factor or shadow director. However, the issue is whether he/she is an officer in [COMPANY].

| | |
|---|--|
| (a) a director or secretary of the corporation; or | |
| <p>(b) a person:</p> <p>(i) who makes, or participates in making, decisions that affect the whole, or a substantial part, of the business of the corporation; or</p> | <p>THIS IS LIKELY A CEO</p> <p>(1) 'Business of the corporation' First, [COMPANY] is a company engaged in business, that being _____ (describe the business – ie. insurance company).</p> <p>(2) "Making or participating in decisions" Second, [DEFENDANT] has made or participated decisions related to that business. He/she has _____ (eg. made investment decisions), which is part of the business that [COMPANY] runs.</p> <p>(3) Effecting whole / substantial part of business Third, [DEFENDANT] has affected the business, either wholly or partly, as evidenced by the fact that _____ (ie. those decisions were implemented, led to financial reward, etc).</p> |
| (ii) who has the capacity to affect significantly the corporation's financial standing ; or | THIS IS LIKELY A CFO |

Corporate contracting



[COMPANY] signed a contract with [THIRD PARTY]. The issue is whether that contract is binding on [COMPANY] and whether [COMPANY] will be liable _____ (describe the consequences – to pay the \$5m).

From the outset, it is irrelevant that the contract is (allegedly) not in the best interests of the company. It is not relevant to the question of enforceability (**s124(2)**).

(1) DIRECTLY BY THE COMPANY

First, the issue is whether the contract entered into the company directly. A corporation has the legal capacity and powers of an individual (**s 124(1)**) and is a separate legal entity (**Salomon**), which means that it can contract. On the facts, _____ (apply):

<no>

... [COMPANY] **does not appear** to have entered into the contract directly under **s 124(1)**. Even though _____ [AGENT(s)] signed the contract, the contract was not executed in accordance **with s 127**, since:

- it was not signed by 2 directors of the company / director and secretary (**s127(1)**)
- it was not affixed with a common seal, which was witnessed by 2 directors of the company (**s 127(2)**)

<yes>

... [COMPANY] **appears** to have entered into a contract directly under **s 124(1)**. This is because [COMPANY] validly executed the contract in accordance with _____ (apply signature / common seal rules).

- Issue and cancel shares** in company (unless it is limited by guarantee)
- Issue debentures**
- grant options** over unissued shares
- distribute company's financial property** among members
- give security** by charging uncalled capital
- grant floating charge** over company's property

- g) arrange for company to be registered / recognised as a body corporate anywhere outside jurisdiction
- h) do anything that is authorised to do under any law (includes foreign laws)

CONTINUED IN ACTUAL NOTES.....

SAMPLE

Duty of care and diligence

**** when [COMPANY / ASIC] is suing [DIRECTOR's]**

**** if [INDIVIDUAL] wants to sue [DIRECTOR], may be able to bring a derivative action on behalf of [COMPANY]**

The issue is whether [DIRECTOR] has breached the duty to exercise his/her powers with reasonable care and diligence. He/she may be liable for _____ (**describe the conduct – what he/she failed to do**). It is important to note that the mere fact of loss is insufficient to signal a failure of duty.

- ... failing to bring concerns to the board (**ASIC v Vines**)
- ... failing to monitor management (**AWA v Daniels, ASIC v Healey, CBA v Friedrichs**)
- ... failing to prevent the re-occurrence of legal activities (**ASIC v Maxwell**)
- ... publishing the financial accounts without reference to the potential for financial consequences (**ASIC v MacDonald, ASIC v Healey**)
- ... failing to attend board meetings and a contravention duty to be diligent (under **s 180(1)**)

GENERAL LAW

(1) Personnel – [DIRECTOR / OFFICER]

[DIRECTOR / OFFICER] is a director (**s 9**). *****DON'T STATE STATUTE IF APPLYING GENERAL LAW**

... Apply director / officer test (**s 180(1)**).

- ... Even though [DEFENDANT] is not a director or officer (**s 180(1)(a)**), he/she occupies the office held by, and has the same responsibilities within the corporation, as the director or officer (**s 180(1)(b)**). On the facts, [DEFENDANT] _____ (apply facts)
 - ... was specifically delegated the role of _____ by _____ (other director).
 - ... has been given work which is usually **distributed** to an officer or director, that being _____ (describe role). That role carries with it the **expectations and responsibilities** which normally flow from the experience that a director brings.

Since [DEFENDANT] was a _____ (director / officer), he/she owes a duty to the company as a whole to exercise his/her powers with care and diligence (**Greenhalgh v Arderne Cinema**).

- ... Nonetheless, on these facts, since [COMPANY] is _____ (insolvent / partially insolvent), he/she will owe a duty to creditors (**Walker v Wimborne**).

(2) Content / extent of duty

At general law, a director or officer owes a duty to a company to apply reasonable care in the performance of their office (**Vrisakis**). The relevant issue is the content/extent of the duty that [DEFENDANT] owes [COMPANY]. A director is expected to uphold the same degree of skill in

performance of duties as may reasonably be expected for persons of commensurate knowledge and experience, in the relevant circumstances (ASIC v MacDonald).

On the facts, [DEFENDANT] is a _____ (apply below). Consequently, he/she must exercise the degree of skill and diligence of a _____ (ordinary / inexperienced, etc director):

** may also look to the express terms of the contract (Wheeler).

** minimum standard competency usually involves being able to read and understand financial statements

OTHER STEPS SET OUT IN FULL NOTES...

(5) Defences

<apply **business judgement** rule below> → this defence applies to breaches of general law and equity as well

<apply ratification rules if conduct was ratified?>

(6) Conclusion for GENERAL LAW

Tentatively, [DIRECTOR] failed to reasonable steps that a reasonable person would have taken if in the director's position. [DIRECTOR] is liable for breaching the general law duty to act with care and diligence.

Duty to act in good faith and for a proper purpose

The issue is whether [DEFENDANT] has breached the duty to exercise his/her powers in good faith and for a proper purpose when he/she _____ (describe). It is important to note that the mere fact of loss is insufficient to signal a failure of duty.

- ... applied company resources for the purpose of _____ (opposite of aims of company) ([ASIC v Adler](#))

General law – EQUITY

(1) Personnel → director / officer

[DIRECTOR / OFFICER] is a _____ (director / officer).

Since [DEFENDANT] is a _____ (director / officer), he/she owes a duty to the company as a whole to act in good faith and for a proper purpose ([Greenhalgh v Arderne Cinema](#)).

- ... Nonetheless, on these facts, since [COMPANY] is _____ (insolvent / partially insolvent), he/she will owe a duty to creditors ([Walker v Wimborne](#)).

(2) Good faith

In equity, a director must believe they are acting in good faith ([Re Smith and Fawcett](#)). This is a **subjective test**, which largely focuses on the state of mind of the directors. In ascertaining a director's state of mind, the Court must consider the surrounding circumstances and other materials throwing light upon [DEFENDANT's] state of mind.

In the circumstances, it is likely that [DEFENDANT] _____ (believed / did not believe) that he/she was acting in good faith because _____ (apply facts).

- ... Analogous to [Australian Metropolitan Life Assurance](#), **silence per se** is no starting point from which to infer lack of good faith (ie. refusing to register share transfer when absolute discretion is given to the board).

(3) Proper purpose

Second, [DEFENDANT] must exercise his/her powers for the purpose for which they were conferred and not for any collateral purpose ([PBS v Wheeler](#)). Some case law suggests that it is unnecessary to distinguish between 'good faith' and 'proper purpose' ([Metropolitan Life Assurance v Ure](#)), although there is other case law to suggest otherwise ([Howard Smith v Ampol](#)).

The first issue is a **question of law** – for what purpose [DIRECTOR] may / may not exercise his/her power ([Howard Smith v Ampol](#)). Having regard to _____ (ie. company constitution / corps act), [DIRECTOR] appears to have the power to _____ (apply facts).

CONTINUED IN FULL NOTES.....

STATUTE (s 181)

The issue is whether [DIRECTOR] is liable under the statutory duty to act in good faith and for a proper purpose (s 181(1)). The statutory duty of s 181(1) reflects general law doctrines (Explanatory Memorandum).

<apply principles from above>

CRIMINAL (s 184)

The issue is whether [DIRECTOR] is also liable for a criminal offence for breaching his s 181(1) statutory duties.

- ... First, [DIRECTOR] _____ (was / was not) _____ (reckless / intentionally dishonest), as evidenced by the fact that he/she _____ (apply facts).
- ... Second, as established above, [DIRECTOR] failed to exercise their powers and discharge their duties _____
 - ... in good faith in the best interests of the corporation (s 184(1)(c))
 - ... for a proper purpose (s 184(1)(d))

[DEFENDANT] appears to have acted with consciousness that what he/she was doing was not in the best interests of [COMPANY] as evidenced by _____ (ie. he/she knew that they were doing was wrong) and deliberately acted in disregard of that knowledge. Consequently, [DIRECTOR] is guilty of an offence (s 1311(1)) and may receive 5 years imprisonment and/or 2000 penalty units (sch 3).

AT GENERAL LAW

Duty to avoid conflicts of interests (ss 182 and 183)

The issue is whether [DIRECTOR] has breached the duty to avoid positions of conflict. Here, [DIRECTOR] _____ (used his/her position / used information) from his/her [directorship], which may have resulted in a potential breach. It is important to note that the mere fact of loss is insufficient to signal a failure of duty.

GENERAL LAW – EQUITY

**** ASIC CANNOT SUE UNDER GENERAL LAW**

(1) FIDUCIARY DUTY

The issue is whether a fiduciary relationship exists. A status-based fiduciary relationship exists between [DIRECTOR] and [COMPANY] ([Hospital Products](#)). The scope of this relationship likely involved [DIRECTOR] acting in the best interests of [COMPANY] and ensuring that he/she did not promote their own personal interests. Consequently, [DIRECTOR] owes a duty to the company as a whole ([Greenhalgh v Arderne Cinema](#)).

Other relevant status based fiduciary relationships

| [FIUDUCIARY] | [PARTY B] | Authority |
|--|-----------|--|
| Director | Company | Hospital Products |
| Solicitor to trust | Client | Boardman v Phipps |
| Senior officers in positions of responsibility | Company | Hospital Products |
| Managing director carrying on business | Company | Industrial Development Consultant v Cooley |

<Directorship in two competing companies>

Furthermore, the case is difficult on the facts because [DIRECTOR] owes fiduciary duties in multiple directions. Not only does [DIRECTOR] owe a fiduciary duty to [COMPANY 1], he/she also owes a fiduciary duty to [COMPANY 2]. Whilst it is permissible for [DIRECTOR] to be a director of both companies in NSW ([Rosetex v Licata](#)), [DIRECTOR] must ensure that no confidential information is divulged as a result of both positions.

Examples of **BREACH**

The case is analogous to _____ (apply authority).

| | |
|--|--|
| Regal | Receiving secret profits <ul style="list-style-type: none"> [DIRECTOR] offered the opportunity to acquire shares as a result of their position as directors. Shares appreciated in value [DIRECTORS] made profit when shares were later sold |
| Boardman v Phipps | <ul style="list-style-type: none"> [SOLICITOR as TRUSTEE] gained confidential information as trustee to will as a result of his/her position with [COMPANY]. He/she then used this information to purchase the shares of a particular company. |
| Furs v Tomkins | <ul style="list-style-type: none"> [MANAGING DIRECTOR] received a payment from [PARTY B] because his position as a managing director allowed him to negotiate a particular contract with the purchaser. |
| Green & Clara v Bestobell Industries | Diversion of business opportunity from one director |

| | | |
|--|-------------------------------|---|
| | | <ul style="list-style-type: none"> • [DIRECTOR] took a contract opportunity and gave them to another company in which the directors had an interest. They then excluded a fellow director of the original company. |
| | <u>Cook v Deeks</u> | Misappropriating company property <ul style="list-style-type: none"> • [DIRECTOR] approved the sale of a company to another company, whereby [DIRECTOR] had an interest. |
| | <u>Gray v Porcupine Mines</u> | Selling shares to oneself, trading at higher price and selling |
| | <u>Coleman</u> | Contracting to procure debentures. Then as [DIRECTOR], convincing your company to buy shares |

STATUTORY LAW

Duty to avoid conflicts of interests (ss 182 and 183)

- *** Do not need to show actual gain (purpose is enough)
- *** Extends to employees
- *** cannot ratify a breach of statute in a GM under statute

The issue is whether [DIRECTOR / SECRETARY / OFFICER / EMPLOYEE] is liable under the statutory equivalent of the equitable no conflict rule in (s 182 / 183).

- *** Improperly using position (s 182(1))
- *** Improperly using information (s 183(1))

Must distinguish whether the POSITION or INFORMATION caused the loss

(1) Use of position → s 182(1)

[DEFENDANT] may be liable for improperly using his/her position when he/she _____ (apply):

- ... gained an advantage for _____ (themselves / someone else) (s 182(1)(a)) by _____ (apply more specifically).
- ... caused detriment to the corporation (s 182(1)(b)) by _____ (apply more specifically).

A number of elements must be proved.

(A) RELEVANT PERSONEL → applies to director, secretary, officer, employee

First, [DEFENDANT] is a _____ (ie. director / secretary / officer / employee).

Since [DEFENDANT] is a _____ (apply above), he/she owes a duty to the company as a whole and is subject to the duty to avoid conflicts of interest (**Greenhalgh v Arderne Cinema**).

- ... Nonetheless, on these facts, since [COMPANY] is _____ (insolvent / partially insolvent), he/she will owe a duty to creditors (**Walker v Wimborne**).

(B) IMPROPERLY

Second, the test for impropriety is an **objective** one derived from **Byrnes**. [DEFENDANT] must have breached the standards of conduct that would be expected of a person in the position of the alleged offender by a reasonable person with knowledge of the duties, powers and authority of the position and circumstances of the case (**Byrnes**).

Here, a reasonable person in [DEFENDANT's] position as _____ (**director / secretary / officer / employee**) of [COMPANY] _____ (would / **would not**) have _____ (ie. apply facts). He/she would have _____ (describe what should have been done). Since a reasonable person **would not have** _____ (describe again), this indicates that the conduct was improper.

- ... In addition, it is irrelevant that [DEFENDANT] was acting honestly throughout the ordeal. Impropriety does not depend on the consciousness of the person, since it is an objective test (**Byrnes v R**).

In determining whether the conduct was improper, regard must be had to whether there was disclosure / consent. (**[DIRECTOR] may argue that he/she did not improperly use his/her position because he/she made a disclosure**).

PROPRIETARY COMPANIES (PTY COMPANIES)

Since [COMPANY] is a proprietary company and [DIRECTOR] has complied with **s 191**, then:

- ... [DIRECTOR] may vote on matters that relate to the interest (**s 194(c)**). This means that _____ (apply facts).
- ... the transactions that relate to the interest may proceed (**s 194(d)**). This means that _____ (apply facts).
- ... [DIRECTOR] may retain benefits under the transaction, even though he/she has the interest (**s 194(e)**). This means that _____ (apply fact).
- ... [COMPANY] cannot avoid the transaction, merely because of the existence of the interest (**s 194(f)**). This means that _____ (apply fact).

Since [DIRECTOR] made the disclosure **before the transaction was entered into**:

- ... [DIRECTOR] may retain benefits under the transaction, even though he/she has the interest (**s 194(e)**)
- ... [COMPANY] cannot avoid the transaction, merely because of the existence of the interest (**s 194(f)**)

PUBLIC COMPANIES

Since [COMPANY] is a public company, then [DIRECTOR], who has a material personal matter in an interest, that is being considered at a director's meeting:

MUST NOT

- ... be present while the matter is being considered at the meeting (**s 195(1)(a)**)
- ... vote on the matter (**s 195(1)(b)**)

UNLESS

- ... the directors, who do not have a material personal interest, pass a resolution that [DIRECTOR] should not be disqualified from voting (**s 195(2)**)
- ... ASIC makes a declaration that [DIRECTOR] may be present and vote (**s195(3)**).

ADDITIONAL PATHWAY → INTERACTION WITH EQUITY AND CONSTITUTION

[COMPANY's] constitution also specifically restricts a director from _____.

- ... having a material personal interest in a matter; or
- ... holding an office or possessing property.

Since **s 191** has effect 'in addition to', and not in derogation of constitutional provisions (**s 193**), [DIRECTOR] will still be liable for these provisions as well.

ADDITIONAL PATHWAY → IF THERE HAS BEEN BREACH

[DIRECTOR] breached **s 195** by _____ (being present at a meeting; voting on a matter that related to his/her personal interest). This is a strict liability offence (**s 195(1B)**).

- ... Nonetheless, despite [DIRECTOR's] contravention, the validity of the resolution to _____ (apply facts) is not affected.

(1E) Conclusion (for disclosure)

Tentatively, [DIRECTOR] _____ (**has** / has not) satisfied the statutory requirements for disclosing his/her personal interest.

- ... Importantly, despite [DIRECTOR] contravening this section by _____ (ie. **failing to disclose a material personal interest; voting on an issue related to the issue**), this does not affect the validity of any act, transaction, agreement, instrument, resolution or other thing (**s 191(4)**).