

TABLE OF CONTENTS

Chapter 8: Share Capital 1

Chapter 9: Membership 4

Chapter 10: Dividends 5

Chapter 12: Directors 5

Chapter 13: Directors Duties & Corporate Governance 8

Chapter 13.2: Duty of Good Faith & Proper Purpose 10

Chapter 13.3: Conflicts of Interest & Disclosure 12

Chapter 13.4: Duty of Care, Skill & Diligence 15

Chapter 13.5: Directors & Creditors 18

Chapter 13.6: Remedies & Penalties for Breach of duty 21

Chapter 13.7: Exoneration and Relief for Breach of duty 23

Chapter 14: Shareholder Meetings 24

Chapter 17: Members' Remedies 26

Chapter 21: ASIC's Investigation Powers 30

Chapter 22 - 25: Corporate Insolvency; Receivership; Administration; Liquidation; Deregistration 30

Week 4: Chapters 8,

Share Capital, Shares and Shareholders Rights and Remedies

General:

Share capital (equity capital) - co would issue shares to the public, shares would be purchased rising \$\$\$ = share capital.

- Issuing of shares (at formation of company or later)
- Allotment of shares – types: e.g. preference, ordinary.
- Registered holders of shares – become members and have rights and entitlements, e.g. Voting at general meeting; Dividends if declared.
- Form of intangible property – ‘chose in action’
- Shares may be bought and sold, bequeathed and given as security for loans.

Nature of shares

Definition: A share is a proportional interest of a shareholder in the net worth of the company.

Pilmer v The Duke Group: “Once issued, a share comprises a collection of rights and obligations relating to an interest in a company of an economic and proprietary character, but not constituting a debt.”

s 1070A Nature of shares and certain other interests in a company or registered scheme

(1) A share, other interest of a member in a company or interest of a person in a registered scheme:

- (a) Is personal property; and
- (b) Is transferable or transmissible as provided by:
 - (i) The company's, or scheme's, constitution; or
 - (ii) The operating rules of a prescribed CS facility if they are applicable; and
- (c) Is capable of devolution by will or by operation of law.

Share options

A company grants an option when it agrees to issue shares to a person (the “option-holder”) at a future date.

- Fully paid-up shares and partly paid-up shares
- Calls can be made on shareholders to pay remaining part of partly-paid up shares
- If the option-holder agrees to take up the shares, they are said to exercise the option and can require the company to allot the shares. As with any other contract, an option requires the option-holder to provide consideration for being granted the share option.
- An option-holder is **not** a member of the company until the option is exercised.
- A company may issue fully paid shares or partly paid shares: **s 254A(1)(c)**
- A person who holds partly paid shares is liable to pay calls on the shares unless the company is a no liability

company: **s 254M**.

- On a winding up, a member is liable to contribute to the company's property to an amount sufficient to pay the company's debts and the costs of the winding up: **s 515**.
- A shareholder need not contribute more than the amount (if any) unpaid on the shares: **s 516**.
- A liquidator has the power to make a call: **s 477(2)**.
- A liquidator can make calls whether or not calls are permitted by the company's constitution: **Wright v Mansell**.
- The amount unpaid on partly paid shares is called “reserve capital” or “uncalled capital”.

Issuing of shares: Contractual rules apply

- Offer, acceptance and consideration.
- Consideration other than cash per **Re White Star Line Ltd**: consideration for an allotment of shares must be more than “sufficient” consideration required under the law of contract. It must represent money's worth for the allotment.
- The application for registration of a company limited by shares must, among other things, set out the amount (if any) each member agrees in writing to pay for each share: **s 117(2)(k)(ii)**.
- **s 254X** requires a company to lodge a notice of share issue with ASIC, Inc. particulars of any contract whereby shares are issued by a public company for non-cash consideration.
- **s 254X(2)** the company must also lodge with ASIC a certificate stating that payable stamp duty has been paid.

Minimum subscription

Statement in disclosure document:

- Securities will not be issued unless a minimum has been subscribed to

The purpose:

- To protect early subscribers where the company is unable to raise the minimum amount it needs to be a viable concern.

Money held in trust until minimum subscription reached

If the minimum subscription condition is not satisfied within four months after the date of the disclosure document, the company must (**s 724**):

- Repay the money received from the applicants; or
- Give the applicants a supplementary or replacement disclosure document that changes the terms of the offer and one month to withdraw their application and be repaid; or
- Issue the securities to the applicants and give them a supplementary or replacement disclosure document

that changes the terms of the offer and one month to return the securities and be repaid

Validation of improper issue of shares

Wide powers of court to validate or confirm a purported issue of shares which is invalid for any reason or in which the terms of the issue are inconsistent with or unauthorised by any law or the company's constitution (**s 254E**)

Parties who can apply

- The company;
- A shareholder; or
- Creditor of the company; or
- Any other person whose interests are affected by the share

Re Swan Brewery Co Ltd (No 2) (1976) 3 ACLR 168A:

Company issued substantial numbers of shares to several other companies. The holders of these shares had, for several years after they were entered on the register of members, been paid dividends, allotted bonus shares and generally treated as members. It was eventually discovered that these companies were at all material times subsidiaries of the Swan Brewery Co Ltd. The allotments to them were consequently void under a provision corresponding to s 259C, which prohibited a subsidiary holding shares in its holding company. The companies sought to have the allotments validated by the court under a predecessor to s 254E.

Gillard J **held** that in the exceptional circumstances of the case it was “just and equitable” to validate the allotments so as to assist a large number of innocent people who would otherwise be victims of invalid allotments.

Kokotovich Constructions Pty Ltd v Wallington (1995) 13

ACLR 1113 an allotment of shares was validated because the parties had proceeded for 20 years on the basis that shares had been properly issued and an order validating the issue was just and equitable. The court rejected the argument that its discretion under the predecessor of s 254E should only be exercised where the validation was non-contentious.

Classes of Shares

s 124(1)(a): Co's power to issue shares

s 254B(1): Co determine the terms on which shares are issued and right/restrictions attached.

s 246F(1): ASIC must be notified i.e. creation of shares, conversion of shares to diff. class **w/i 14 days of** creation/conversion.

s 254E: court application for validation of shares.

- Where a category of shares enjoys rights, benefits, disabilities or other incidents sufficiently distinct from

other categories of shares = constitute a 'class' of shares: **Clements Marshall Consolidated Ltd v ENT Ltd**

- The rights and entitlements under the shares must not be 'so dissimilar as to make it impossible for the members to consult together' **Re Hills Motorway**
- If not expressly categorized into classes, classes may still exist: **Crumption v Morrione Hall**
- At common law: all shares issued with the same nominal values are presumed to enjoy the same rights and thus the same class: **Birch v Cooper**

The most common ways in which different classes of shares differ are as follows:

- Entitlement to dividend;
- Right to priority in payment of dividend;
- Voting rights;
- Right to priority of repayment of capital on winding up; and
- Right to participate in a distribution of surplus assets on winding up.

Types of Shares:

Deferred, Founder's or Management Shares:

- Right to dividends is deferred until dividends of a particular amount have been paid to other shareholders; usually adopted by company founders as an indication of faith in the profitability of the company.

Ordinary Shares:

- Majority of shares held by members, usually entitled to dividends before deferred shareholders, but after preference shareholders.
- Usually enjoy full voting rights and can exercise a great degree of control over company affairs due to their numbers.
- **s563A**: If a co goes into liquidation the rights of non-member creditors prevails over the rights of shareholders. The rights of ordinary shareholders to declare dividends defer to the rights of preference shareholders to accumulated and declared dividends.

Preference Shares:

- **s254A(1)** Power to issue shares may be used to issue preference shares
- Establishing that shares are preference shares requires that certain rights be specified in accordance with **s254A(2)** (see below)
- Preference shares normally enjoy preferential rights to the payment of dividends over ordinary shareholders: **Re Brighton & Dyke Rwy**. Such rights do not assure shareholders automatic dividends each year; unless

the co makes a profit and announces a dividend, preference shareholders have no right to demand payment of a dividend: **Marra Developments v BW Rofe**.

Rights of Preference Shareholders

S 254A: Power to issue bonus, partly-paid, preference and redeemable preference shares

(1) ...(2) A company can issue preference shares only if the rights attached to the preference shares with respect to the following matters are set out in the company's constitution (if any) or have been otherwise approved by special resolution of the company:

- (a) Repayment of capital;
- (b) Participation in surplus assets and profits;
- (c) Cumulative and non-cumulative dividends;
- (d) Voting;
- (e) Priority of payment of capital and dividends in relation to other shares or classes of preference shares.

Variation of class rights

Definition: A reduction in the dividend rights of holders of particular shares denies a right to that class of shareholders; only those alterations which effect the substance of the class right need to comply with particular procedures: **White v Bristol Aeroplane**.

Unless the constitution provides otherwise, a reduction in share capital is not usually considered a variation in class rights:

Fowlers Vacola Manufacturing

- Distinguished *In the Matter of Village Roadshow Ltd*, involved a buy back scheme; the resolution here would have entitled the co to buy back all pref. shares, this resolution was held to have affected more than the mere enjoyment of preference shareholder rights = the legal rights of the preference shareholders would have been abrogated as a matter of substance.

2 Methods:

Common Law

- Variation that alters the substance, as opposed to the mere enjoyment, of a class right

Corporations Act

- Deemed variation

Common Law: Alteration must affect substance

Only variations that affect the substance of the class right, as opposed to the mere enjoyment or value of the right, need to comply with the class right variation procedure

White v Bristol Aeroplane Co Ltd (1953)

Bonus issue of shares to ordinary shareholders had the effect of diluting the voting rights of preference shareholders

Held not to affect the substance of the preference shareholders rights:

- They still had their voting rights (substance the same)
- Only their enjoyment of their voting power that was affected by the share issue = very conservative interpretation of the common law rule.

Greenhalgh v Arderne Cinemas Ltd

Sufficient shares were issued to Mr. G to enable him to block a special resolution. Members by ordinary resolution voted to sub-divide their shares, thereby increasing the number of votes they had = Effect was to diminish the proportion of shares Mr. G had and meant he could not block a special resolution

- So even though Mr. G's overall voting power has suffered, the shares he held still held the same rights and the issue was held not to be a variation of class rights

Variation by statute:

CA deem a variation s 246(C):

- When a class of shares is divided into further classes
- When rights attaching to some shares are varied
- When new shares are issued and rights of existing shares are different
- When new preference shares are issued

Procedure to vary and cancel class rights

If constitution sets out procedure:

Procedure in the constitution must be followed to vary or cancel class rights (**s 246B(1)**)

No constitution or constitution doesn't set out procedure:

May only vary or cancel class rights:

- By **special resolution** of the company; **and**
- By special resolution passed at a meeting of the holders of the **affected class**; **or**
- With the written consent of members with at least **75%** of the votes of the affected class (**s 246B(2)**)

Challenging a Variation of Class Rights:

s 246D(1) Members with at least 10% of votes in affected class....can

- Apply to court (within one month) to have variation set aside

Test:

- Does the variation unfairly prejudice the members of the affected class?

s 246D: The alteration has no effect until the application is withdrawn or determined by the court.

s 246D(5): If the court believes the alteration unfairly prejudices the members of the class represented by the applicant, it must set aside the alteration. If the court is not satisfied, the alteration must be confirmed.

Other Remedies

- If company fails to follow **variation procedure in constitution** = Breach of the **s 140(1)(a)** statutory contract
- If company fails to follow **s 246B** procedure = Affected members can apply for an injunction (**s 1324**) and apply for damages.
- If variation is oppressive or unfair = Remedy under **s 232** - very powerful section = gives courts massive powers to make changes to co's constitution etc.

Maintenance of share capital: Modern statutory rules:

The rule that companies must maintain their share capital is expressed in the Corporations Act in the following rules:

- Restrictions on a company purchasing its own shares (Part **2J.2**)
- Restrictions on a company giving financial assistance to a person to acquire shares in the company (Part **2J.3**)
- Paying dividends out of capital would result in returning capital to members

Reduction of share capital and share buy-backs allowed, but then Statutory Provisions should be followed: (EXCEPTIONS)

Provided for in **ss 256A-258F** of the CA

Why would companies legitimately like to reduce their share capital or buy-back shares?

- Companies may have more share capital than it needs after selling part of its business
- Returning such surplus may have tax advantages
- Ratio of "share capital: loan capital" not be right – too much "share capital"
- To redeem redeemable preference shares

Core Requirement for reduction of share capital

s 256B Company may make reduction not otherwise authorised

(1) A company may reduce its share capital in a way that is not otherwise authorised by law if the reduction:

- (a) Is fair and reasonable to the company's shareholders as a whole; and
- (b) Does not materially prejudice the company's ability to pay its creditors; and
- (c) Is approved by shareholders under **s 256C**.

Break down of **s 256B** requirements:

(a) Fair and reasonable to shareholders as a whole

Adequacy of consideration paid to shareholders. Whether reduction would have practical effect of depriving some shareholders of their rights E.g. Stripping company of funds that would otherwise be available for distribution to pref. shareholders

- Whether reduction used to effect a takeover and avoid takeover provisions
- Whether reduction involved arrangement that should more properly proceed as a scheme of arrangement

Injunction:

- Shareholder who alleges that a reduction of capital is not fair and reasonable may apply for a **s.1324** injunction
- Company, not the shareholder, has the onus of proving the reduction is fair and reasonable (**s.1324 (1B)**) = reversal of onus of proof. See **Winpar Holdings Ltd**

(b) Ability to pay creditors

Creditors may apply for an injunction to prevent a reduction of capital if the company's solvency is an element of a contravention of **s 256B(1)(b) (s 1324(1A))**

Company has the onus of proving the reduction does not prejudice its ability to pay creditors (**s 1324(1B)**)

ASIC Disclosure: s 256C(5) requires company to lodge details of proposed capital reduction with ASIC to assist creditors in discovering details of the proposed capital reduction

- Creditor protection is key rationale underlying share capital reduction rules

(c) Shareholder approval: is reduction equal or selective? s 256C shareholder approval requirements vary depending on whether reduction is:

- Equal reduction
- Selective reduction

More onerous approval requirements because potential to be unfair

Equal reduction **s 256B(2)** Equal Reduction if:

- Relates only to ordinary shares
- Applies to each shareholder in proportion to number of ordinary shares held
- Reduction terms same for each ordinary shareholder
- See **s 256B(3)** for differences in that may be ignored in defining 'equal' reduction

Selective Reduction: If capital reduction is not an equal reduction, it is a selective reduction

(c) Shareholder approval? What vote is required?

Equal Reduction: Approved by ordinary resolution at general meeting: **s 256C(1)**

Selective Reduction

Approved by:

- Special resolution at general meeting = 75%
- With no votes cast in favour by person (or associate) to receive consideration as part of reduction or whose liability to pay amounts unpaid on shares is to be reduced = those with a vested interest; **OR**
- Unanimous resolution at general meeting; **PLUS**
- If reduction involves cancellation of shares: (Relates to

both scenario's if they both involve a cancellation of shares)

Reduction must also be approved by special resolution of members whose share are to be cancelled

(c) Shareholder approval: Notice Requirements

Notice of meeting must include statement setting out all known information that is material to the decision on how to vote on the resolution to approve the capital reduction: **s 256C(4)**

- Before notice of meeting is sent, company must lodge notice and material information statement with ASIC: **s 256C(5)**
- Purpose is to give shareholders and creditors advance notice of reductions so they may oppose

Prohibition to buy own shares

Common law prohibits a company from buying back its shares from shareholders as part of the rules aimed at maintaining share capital: **Trevor v Whitworth**

Corporations Act: Corporations Act prohibits a company acquiring shares in itself or issuing or transferring shares to an entity it controls (**ss 259A & s259C**) (buy buying back their own shares they are reducing their share capital).

Exception:

Share buy backs under **s 275A:**

Company may buy back its own shares if:

- Buy back does not materially prejudice creditors
- Company follows procedure in Division 2 of Part **2J.1**

The 10/12 limit: Generally, companies may buy back up to 10% of their shares within a 12 month period without shareholder approval and with minimum procedural requirements

Permitted buy back schemes: On-market buy backs

- Conducted by listed company on ASX
- Company offers to buy shares 'on the market'
- Members have equal opportunity to participate
- Member approval only required if over the 10/12 limit
- Equal access buy backs
- Selective buy backs
- Employee share scheme buy backs
- Minimum holding buy backs

Prohibition on a company to financially assist anybody to purchase shares in the company:

Prerequisites for financial assistance: S 260A: (1) A company may financially assist a person to acquire shares (or units of shares) in the company or a holding company of the company **only if:**

- (a) Giving the assistance does not materially prejudice:
 - (i) The interests of the company or its shareholders; or
 - (ii) The company's ability to pay its creditors; or
- (b) The assistance is approved by shareholders under

section 260B (that section also requires advance notice to ASIC); or (c) the assistance is exempted under section 260C.

Approval of shareholders and other requirements S 260B

Exemptions: S 260C

- General exemptions based on ordinary course of commercial dealing
- Special exemptions for financial institutions
- Special exemptions for subsidiaries of debenture issuers
- Special exemption for approved employee share schemes
- Other exemptions.

s 260B Shareholder approval

Approval by company's own shareholders:

(1) Shareholder approval for financial assistance by a company must be given by:

- (a) a special resolution passed at a general meeting of the company, with no votes being cast in favour of the resolution by the person acquiring the shares (or units of shares) or by their associates; or
- (b) A resolution agreed to, at a general meeting, by all ordinary shareholders.

Approval by shareholders of listed Holding Corporation

(2) If the company will be a subsidiary of a listed domestic corporation immediately after the acquisition referred to in section 260A occurs, the financial assistance must also be approved by a special resolution passed at a general meeting of that corporation.

Approval by shareholders in ultimate Australian holding company

(3) If, immediately after the acquisition, the company will have a holding company that:

- (a) is a domestic corporation but not listed; and
- (b) is not itself a subsidiary of a domestic corporation; The financial assistance must also be approved by a special resolution passed at a general meeting of the body corporate that will be the holding company.

Information to accompany the notice of meeting

(4) A company or other body that calls a meeting for the purpose of subsection (1), (2) or (3) must include with the notice of the meeting a statement setting out all the information known to the company or body that is material to the decision on how to vote on the resolution. However, the company or body does not have to disclose information if it would be unreasonable to require the company or body to do so because the company or body had previously disclosed the information to its members.

Documents to be lodged with the ASIC before notice of meeting is sent out

(5) Before the notice of a meeting for the purpose of subsection (1), (2) or (3) is sent to members of a company or other body, the company or body must lodge with ASIC a copy of:

- (a) The notice of the meeting; and
- (b) Any document relating to the financial assistance that will accompany the notice of the meeting sent to the members.

(6) The company must lodge with ASIC, at least 14 days before giving the financial assistance, a notice in the prescribed form stating that the assistance has been approved under this section.

Lodgment of special resolutions

(7) A special resolution passed for the purpose of subsection (1), (2) or (3) must be lodged with ASIC by the company, listed Domestic Corporation or holding company within 14 days after it is passed.

Challenging a reduction of share capital:

s 256B Company may make reduction not otherwise authorised

(1) A company may reduce its share capital in a way that is not otherwise authorised by law if the reduction:

- (a) **Is fair and reasonable to the company's shareholders** as a whole; and
- (b) Does not materially prejudice the company's ability to pay its creditors; and
- (c) Is approved by shareholders under **s 256C**.

To challenge you have to prove that it was contrary to all three components. **s 1324 (injunctions)** is used as "remedy" – good illustration: **Winpar Holdings Ltd**

Factors: taken into consideration by the Court to determine whether the reduction was "fair and reasonable to the company's shareholders as a whole"?

Company carries onus to prove that the reduction was "fair and reasonable to the company's shareholders as a whole"?

Reverse of onus because of **s 1324 (1B)** – concluding sentence Views of properly informed minority plays a role, but court must make its own judgment

- Court will consider whether "special benefits" to the company in reduction of share capital were passed on to minority shareholders: **Melcann Ltd v Super John Pty Ltd (1995)**
- **In casu**, pro rata benefit by higher offer than independent valuation (55 cents instead of 45.7-46.7 cents) Held: That the reduction was "fair and reasonable to the company's shareholders as a whole".

Membership: Chapter 9

Significance of being a member:

Rights & Duties:

- Vote at GM
- Dividends
- Liable to pay calls (**s 254M(1)**).
- Liable to contribute to debts when being wound up (**s 514**).
- Share in surplus assets on winding up.

What is the evidence of shareholding?

Share certificate is only prima facie evidence (not an absolute right = they can be falsified) of the member's title to the share: **s 1070C(2)**. The registration of the member's holding in the **register of members** confers the status of shareholder: CHES = Clearing House Electronic Sub-register System

Rights of members:

Register must be maintained: **s 168**

Location: register must be kept at the registered office, the principal place of business: **s 172(1)**.

Must contain information about shareholders and their shares: **s 169**.

Right of inspection **s 173(1)**: Anyone can inspect, Shareholders can inspect for free.

Shareholder's right to privacy **s 177**: Can't put names on mailing list & can't use for 'improper purposes'

Significance of the register

Proof of matters shown in it: **s 176**

- Person does not become a member until name is entered: **Maddocks v DJE Constructions**.

Only persons registered gain Corporations Act membership rights: **BWN Industries Pty Ltd v Downey**.

Aggrieved persons can apply to have register corrected: **s 175**

Shares certificates

A share certificate is prima facie evidence of the title of a shareholder to the number of shares specified: **s 1070C(2)**

Must state **s 1070C(1)**:

- The name of the company and its jurisdiction of registration;
- The class of shares; and
- The amount unpaid on the shares.

Re Bahia and San Francisco Rail Co (1868) LR 3 QB 584B

Bahia relied on a share certificate that stated A was the owner of a certain number of shares and purchased those shares from him. After B became registered as the holder, it transpired that A was not the true owner. He had forged the signature of the true owner, C, on a transfer and had forwarded this forged transfer together with a stolen share certificate made out in C's name to the company. The company, without negligence or fraud, then issued the certificate to A.

The court **held** that C, as true owner, was entitled to have his

name restored to the register. B could not acquire better title than the defective title of A. As a result, B's name was removed from the register. B obviously had rights against A based on A's fraud. The company was held liable to B for damages because it was estopped from denying to him that A was the true owner. **Daily Telegraph Co v Cohen** (1905) 5 SR (NSW) 520
 Shares were sold under a purported exercise of a power of attorney. The power of attorney and associated transfer of shares were later held to be void. The original owner's name was therefore restored to the register. In the meantime, the transferee had in turn transferred the shares to Cohen. Cohen's name was removed from the register, but the company was held liable in damages to him because it was estopped from denying that his transferor was the true owner as it had previously certified.

Liability of members

Liability to pay on call for partly paid shares: **s 254M**

- If shares in a company are partly-paid, the shareholder is liable to pay calls on the shares in accordance with the terms on which the shares are on issue.
- In a co limited by shares, the liability of members is limited to the amount, if any, unpaid on their shares: **s 516**.
- On winding up of the co, every present and past member is liable to contribute to the property of the co to an amount sufficient for payment of its debts **s 515**.
 - Members who ceased to be a member for more than one year prior to commencement of winding up is NOT liable to contribute: **s 521**.

Dividends: Chapter 10

What are dividends?

Dividends are the distribution of the company's profits to shareholders: **s 124(1)(d)**: A company has the powers of a body corporate including the power to "distribute any of the company's property among the members, in kind or otherwise"

Procedure for payment:

Rules governing the procedure for payment of dividends are contained in either:

- Replaceable Rules
- Constitution

Generally, directors determine that dividend is payable and the amount

Replaceable Rules (if you don't have a constitution) **s 254U**

(1) The directors may determine that a dividend is payable and fix:

- (a) The amount;
- (b) The time for payment;
- (c) The method of payment.

The methods of payment may include the payment of cash, the issue of shares, the grant of options and the transfer of assets
 (2) Interest is not payable on a dividend

s 254W(2) ... the directors may pay dividends as they see fit

Can shareholders force payment?

General rule: No, Shareholders cannot force directors to pay dividend even though a company has available profits

Exception:

- In exceptional circumstances the refusal by directors to recommend a dividend may amount to oppressive or unfair conduct
- Remedy under **s 232** (Members Remedies) (**Sanford v Sanford Courier Service Pty Ltd**).

Effect of declaring a dividend: When does a debt arise?

Once a dividend is declared it becomes a debt owed to the subject matter (**Marra Developments Ltd v BW Rofe**)

s254V (Replaceable rule - only effective if not replaced)

(1) A company does not incur a debt merely by fixing the amount or time for payment of a dividend. The debt arises when the time fixed for payment arrives and the decision to pay the dividend may be revoked at any time before then.

- However, if the company has a constitution and it provides for the declaration of dividends, the company incurs a debt when the dividend is declared.

Declaration of INTERIM dividend: When does a debt arise?

Interim dividends are estimated.

Revocable:

- Declaration of an interim dividend does not give rise to a debt
- An interim dividend may be revoked before payment (**Marra Developments Ltd v BW Rofe**)

Common Law & **s 245T** until June 2010

Pre June 2010 dividends:

- A dividend may only be paid out of profits of the company
- Statutory entrenchment of common law rule in **Re Exchange Banking Co (Flitcroft's case)**

Maintenance of share capital

- Payment of dividends cannot be used as means of returning capital to shareholders contrary to the maintenance of share capital doctrine

What does 'profit' mean?

What are profits: **Re Spanish Prospecting Co Ltd**:

"Profits" implies a comparison between the state of a business at two specific dates usually separated by an interval of a year. The fundamental meaning is the amount of gain made by

the business in the year... If the total assets of the business at the two dates be compared, the increase which they show at the later date as compared with the earlier date ... represents in strictness the profits of the business during the period in question."

New Law: 'Profits test' has been replaced for dividends declared after June 2010:

s 254T(1) A Co may not pay dividend unless:

- (a) Company's asset must exceed its liabilities (balance sheet solvency)
- (b) Payment of dividend must be fair and reasonable to shareholders as a whole.
- (c) Payment of dividend must not materially prejudice company's ability to pay creditors.

Remedies for improper dividend payment:

Unauthorised reduction of capital

Dividends paid other than in accordance with **s 254T** may involve a reduction of capital

If reduction not authorised by **s 256B**, company contravenes **s 256D**

- Dividend payment not invalidated
- Directors involved liable for civil penalty order: **s 256D(2)**

Insolvent trading

Payment of a dividend by an insolvent company may be insolvent trading. Directors contravene **s 588G** if they fail to prevent company from incurring debt when there are reasonable grounds for suspecting company is insolvent
 Directors may be personally liable to compensate company's creditors

Breach of fiduciary duty:

Payment of dividend by an insolvent company may constitute a breach of duty by the directors. Directors who authorise dividend in breach of fiduciary duty may be personally liable to repay the amount of the dividend to the company

Injunction:

Company contravenes **s 254T** if it pays dividend other than out of profits. **s 1324** gives shareholders and creditors right to apply for injunction to restrain company from contravention if company's insolvency is an element of the contravention

Directors: Chapter 12

All companies have directors who are collectively called "the board of directors"

Proprietary companies can have one director: **s 201A (1)**

Public companies **MUST** have at least 3 directors: **s 201A (2)**

Initial directors are those whose names appear on with their consent on the application for registration

A Company consists of 2 components:

1. Board of directors
2. Members in general meeting.

s 9 definition includes person appointed to the position

- “De facto” director
- “Shadow” director

Who is a Director?

s9 definitions: a person who is appointed to the position

OR If not appointed **and**:

- They act in the position of the director – a driving force behind the company=(*de facto director*) **or**
- Not validly appointed/ the other directors are accustomed to act in accordance with the person’s instructions or wishes = (*shadow director*)

s9 a *de facto* director is a person who is appointed to the position of a director but is not described as a director, he or she acts in the position of a director but is not validly appointed as a director but they will be subject to the usual duties of a director.

Chameleon Mining v Murchison Metals (2010)

De facto director (he carried out a large number of tasks that were typical of a director, negotiate mining interests (board authorised), made the content of the prospectus i.e. who would be issued shares, high level management decisions affecting the company’s financial standing.

Buzzle Operations v Apple Computer (2010)

Shadow director = you can be a de facto director and a shadow director, doesn’t matter whether he’s doing everything a director would do, there must be a causal connection between his instructions and the people acting on his instructions. Would not qualify if it’s something that they would do any way, it has to be a specific instruction. It’s not just a one of instance, it has to be habitual = habitual compliance over a period of time, not just a one of and not validly appointed. A person is NOT a shadow director if the actions are something that they feel they have to do; it has to be substantial actions.

Types of Directors:

Managing director (CEO)(MD) - in charge of daily business of the company - responsible for employing senior executives

Chair of Directors - is appointed by other directors to chair meetings who exercise procedural control over a meeting (i.e. who speaks, order of business, declaring resolutions asking for general business and closing meetings).

- The importance of a Chair was verified in: **Colorado Constructions Pty Ltd v Platus** (1966) where it was held that when 2 directors left a meeting after a brawl, the remaining directors purported to pass a resolution. This was challenged and the Court said this was

invalid, as no Chair had been appointed.

- A Chair of a listed company is responsible to a greater extent than any other director to ensure that the Board is properly informed is familiar with the financial circumstances and the Board properly meets its supervisory duties.

Executive directors - takes part in daily management of the company under the direction of CEO. They are the senior management and have substantial control over the company’s activities

Non-executive directors - not directly involved in daily management, only part-time involvement. They oversee the activities of the management team headed by CEO and bring an independent view to the board’s decisions. They must consider the interests of the company and shareholders

Alternate Directors - s 201K(1): a director may, with the approval of the other directors, appoint an alternate to exercise some or all of the director’s powers.

Appointed where a director is unable to attend board meetings or otherwise exercise powers as a director.

Where an alternate director exercises a director’s powers, this exercise of powers is as effective as if exercised by the director:

s 201K(3).

Markwell Bros Pty Ltd v CPN Diesels: held that an alternate director fell within the definition of ‘director’ and is subject to the same fiduciary and statutory duties.

Nominee Directors - Sometimes a director is appointed to represent the interests of a particular shareholder or creditor on the board of directors.

Key Management Personnel - The term ‘key management personnel’ has the same meaning as in the accounting standards: **s 9** are those persons having authority and responsibility for planning, directing and controlling the activities of the entity, directly or indirectly, Inc. any directors.

Functions and Powers of the Board

Board sets the direction of the company and holds management accountable. Powers are determined by replaceable rules, company’s constitution (if it has one) and *CA*.

Shareholders have power to appoint or replace directors

The Board will usually be responsible for:

- Overseeing the company, including its control and accountability systems
- Appointing and removing the chief executive officer, or equivalent
- Where appropriate, ratifying the appointment and the removal of senior executives.
- Providing input into and final approval of management’s development of corporate strategy and performance objectives.

- Reviewing, ratifying and monitoring systems of risk management and internal control, codes of conduct and legal compliance.
- Monitoring senior executive’s performance and implementation of strategy.
- Ensuring appropriate resources are available to senior executives
- Approving and monitoring the progress of major capital expenditure, capital management, and acquisitions and divestitures.
- Approving and monitoring financial and other reporting.

The Power of Management

s 198A Replaceable Rule states that the business of a company is to be managed by directors

It is a broad power which can include changing the direction of a company or selling the only business carried on by it and Directors DO NOT have to get shareholders’ approval to sell *However* shareholder approval is required if a listed company proposes to make significant change to the nature/scale of its activities

Shareholders cannot override management

Shareholders cannot involve themselves in the management of the company:

Automatic Self- Cleansing Filter Syndicate Co v Cunningham

FACTS- Directors were ordered by general meeting of members to sell the company’s property. Directors refused, relying on constitution

HELD- Constitution gave management powers to the board of directors including power to sell property. Members could not interfere as they were contractually bound by the constitution Therefore ownership vests in the shareholders and management resides in the board of directors.

Board Procedure

Director’s meetings: decisions are made and resolutions passed: rules governing meetings are set out in replaceable rules (RR)

RR **s 248G**- resolutions must be passed by a majority of votes cast by Directors. The Chair has the casting vote if necessary(**s 248G(2)**)

Notice of Board Meetings- all directors MUST receive “reasonable” notice that a meeting is to take place BUT if meetings are usually held at regular fixed dates, there is no need for notice

QUORUM- the minimum number of directors required for a valid meeting

S 248F RR and constitution - sets out how many directors