

CORPORATIONS LAW

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Consider before answering a question:

- Who are you advising? Is it ASIC or a shareholder? – this will impact your answer.
 - o Shareholders who are disgruntled → topic 8
 - o ASIC → duties
- Is it a civil penalty provision? (s 1317E)
 - o ASIC can apply for a declaration of contravention: ss 1317E(1); 1317j
 - o Can thereafter be subjective to various other orders
 - Pecuniary: s 1317G
 - Individuals: s 1317G(3)
 - Companies: s 1317G(4)
 - Relinquishment: s 1317GAB
 - Compensation: ss 1317H, 1317J
 - o Can be criminally liable: s 184
- Is it a pty or public company?

- Suspecting - “more than a mere idle wondering whether it exists or not; it is a positive feeling of actual apprehension or mistrust, amounting to a ‘slight opinion’ but without sufficient evidence” - *Queensland Bacon v Rees* (revision)
- (4) Either
 - (a) The holding co or one or more of its directors is or are aware at that time that there are such grounds or
 - (b) Having regard to the nature and extent of the holding co’s control over the subsidiary’s affairs and to any other relevant circumstances it is reasonable to expect that a holding co in the holding co’s circumstances would be so aware or one or more of such a holding co’s directors would be so aware

Consequences - section 588 W

- Recovery of compensation by liquidator - amount equal to the loss or damage
- Not an offence
- The debt must have been wholly/partly unsecured - see s 588Y

Tip: set up a separate paragraph for each director so you don’t miss anything. The problem will probably evince that different people knew different things or should have known different things!

TOPIC 9: DUTY TO AVOID CONFLICTS AND PROFITS

LOOK FOR: When a director or officer may have a conflicting interest (eg, personal stakes), or a conflicting duty (eg, to act as a director of another company or trust).

STATE: D (the director or officer), may be liable for breach of the general law duty to avoid conflicts of interest (*Boardman v Phipps*; *Hospital Products*)

Aberdeen Railway: And it is a rule of universal application, that no one, having such duties to discharge, shall be allowed to enter into engagements in which he has, or can have, a personal interest conflicting, or which possibly may conflict, with the interests of those whom he is bound to protect (Lord Cranworth LC)

Boardman v Phipps:

“Real Sensible Possibility” of conflict

- *Boardman v Phipps* [1967] 2 AC 46 (solicitor to trust gained information while acting as solicitor, used the info to buy shares in a co that the trust was not able to purchase, profit resulted to solicitor and trust)
- Breach of obligation to avoid conflict between personal interest and fiduciary duty
- Liable to account for profits made
- Allowance made for skill and expenses

Is the conflict rule engaged?

STATE: There is no single formulation of the objective test, however, a possible formulation is that from Lord Upjohn’s dissent in *Boardman*. It is whether there is **real sensible possibility of conflict**. In my view it means that the reasonable man looking at the relevant facts and circumstances of the particular case would think that there was a real sensible possibility of conflict

- Modern example: Australian Careers Institute
 - *Sackville AJA*: In my view, an objective observer, having regard to the terms of the Shareholders Agreement, and the scope of Mr Hornsey’s functions and responsibilities as a director of AIF National, the primary Judge was entitled to find that there was a real or substantial possibility of such a conflict
- A director may be able to act despite conflict if:
 - full disclosure to and consent of general meeting (ratification)
 - modification of duty by constitution

Conflicting duties/Holding competing directorships:

Fitzsimmons v R (1997)

Facts:

- Transaction involves **Duke acquiring shares in Kia Ora** and **Kia Ora providing funding to Duke**.
- Applicant was already a **director of Duke** and became a **director of Kia Ora** on the day of the transaction.
- **Problem: Owes a duty to Kia Ora to disclose** the precarious financial position of Duke, BUT if he does that Kia Ora will not do the deal and he has a **duty of confidentiality to Duke**.

Court said: *Owen J*

- F argued positive duty to Duke not to disclose info - could not therefore be under duty to K to disclose info
- At a minimum **F should have disclosed conflict and absented himself** from participation in deliberations/vote. More may be required - **some positive** action to clearly identify the perceived conflict and suggest a course of action to limit damage
- What is required would depend on the subject matter, the state of knowledge of the adverse information, the degree to which the director had been involved in the transaction, whether the director had been promoting the cause, the gravity of the possible outcome, the exigencies and commercial reality of the situation...

Remember also **PBS v Wheeler** from Topic 7

- o The conflicted director (Hamilton) was required to take steps to protect the interests of the company

If it is, what does a director need to do about it/ have they done enough?

STATE: The minimum requirement will be disclosure of the interest (Fitzsimmons). What action above and beyond mere disclosure the person must take is fact dependent.

RELIEF FOR BREACH OF CONFLICT/PROFIT RULE

- General law remedies – mainly rescission, constructive trust and account of profits (could sue in relation to loss instead or seek other equitable remedies).
- Potential allowance for skill, contribution and expenses made in *Boardman v Phipps* and other cases

STATUTORY DUTIES: DISCLOSURE OF MATERIAL PERSONAL INTERESTS:

RULE: Directors have a duty to disclose material personal interests in a matter that relates to the affairs of the company (s 191). Directors must give formal notice to the other directors in a form that satisfies s 191(3), unless the director falls within an exception. [X does not fall within any of the exceptions.]

- Proprietary companies
 - o Section 191: A director of a company who has a material personal interest in a matter that relates to the affairs of the co must give the other directors notice of the interest.
 - “Affairs of the co” - see section 53
 - “Material personal interest” (next slide)
 - exceptions - sections 191(2), 192
 - notice - s191(3)
 - consequences

SO, MATERIAL PERSONAL INTEREST?

STATE: It is something that has the capacity to influence the vote of the particular director upon the decision to be made (*McGellin v Mount King Mining NL* per Murray J). ‘Material’ means a relationship of some real substance to the matter under consideration.

- Could be direct, indirect, vested, contingent
- It’s the substance of the interest, its nature and capacity to have an impact upon the ability of the director to discharge his or her fiduciary duty which will be important
 - o There has been debate as to whether the concept of material personal interest can be equated with the concept of real sensible possibility of conflict – the better view is that these concepts can be equated (see Langford and Ramsay article)
 - o There has also been debate as to whether the concept of material personal interest includes conflicts of duty – the better view is that it does (see Langford and Ramsay)

- **s 191(3)**: Notice required by s 191(1) must:
 - o (a) give details of the nature and extent of the interest; and the relation of the interest to the affairs of the company; and
 - o (b) be given at a directors' meeting as soon as practicable after director becomes aware of their interest.

EXCEPTIONS:

- **s 191(2)(b)**: Proprietary company and other directors are aware of the nature and extent of the interest.
- **ss 192; 191(2)(d)**: Standing notice
 - o **s 192: Standing notice** (even before the interest becomes a material personal interest requiring disclosure, directors can give their colleagues notice).
 - Notice under s 192(1) must give details of the nature and extent of the interest and be given either at a directors' meeting (orally or in writing) or to the other directors individually in writing (s 192(2)).
 - *Camelot Resources Ltd v McDonald*: 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 [Note that this case is not mentioned in Redmond but you can cite it]
 - o s 191(2)(d): Director does not need to give notice if director has given standing notice under s 192.
- **s 192(2)(c)**: Director has already given notice (past notice)
- **s 191(2)(a)(i)**: Interest as a **member held in common with other members** (ie; they have shares in the company and the interest relates to receiving a dividend).
- **s 191(2)(a)(ii)**: Interest arises in relation to **director's remuneration**
- **s 191(2)(a)(viii); s 50**: Interest is in a contract with a related body corporate and arises merely because the director is a director of the related body corporate (s 50: holding company, subsidiary, subsidiary of holding company).

STATE: Therefore, X has a material personal interest which they have not disclosed.

CONSEQUENCES OF BREACH: Fine of up to 30 penalty units (not a civil penalty provisions). A contravention of s 191 does NOT affect the validity of the transaction (s 191(4)).

VOTING BY A DIRECTOR WITH A MATERIAL PERSONAL INTEREST:

- **PROPRIETARY:**
 - o RR allows a director who complies with s 191 (disclosure of MPI) to be present and vote and retain benefits
- **PUBLIC:**
 - o **2 prohibitions:** (1) cannot be present and (2) cannot vote
 - o **Exceptions:**
 - **s 195(1A)(b)**: Interest does not need disclosure under s 191
 - **s 195(1A)(a); s 195(2)**: Other directors are satisfied that the interest should not disqualify the director
 - **s 195(1A)(a); s 195(3); s 196**: Participation with ASIC approval
- **NB:** BREACH OF S 195 fine up to 20 penalty units, general law obligations still apply

DUTY TO AVOID PROFITS

STATE: The general law profit rule applies to directors and senior executives. X is a [director/senior executive] and thus clearly bound by the duty. Directors cannot use their positions in the company to create a **new business opportunity** and then divert it to themselves for personal benefit. A director in breach of the general law profit rule will be liable to **account for the unauthorised profits** made by reason and in the course of their fiduciary relationship (*Chan*).

- Obtaining unauthorised benefit from the relationship
- Also expressed as making profit in connection with office, making profit by reason of and in the course of the fiduciary relationship (Regal)- Deane J in Chan
- Overlaps with conflict rule

STATE: Notably, X's obligations are twofold such that X has possibly also breached the general law conflict rule here.

Regal Hastings Ltd v Gulliver:

- Directors found to be in breach of duty - they made a profit by reason of and in the course of the fiduciary relationship
- Not relevant that directors acted bona fide or that the co could not have taken up the opportunity
- Difficulty of investigation/vulnerability of beneficiary
- Lord Russell of Killowen:

- Nevertheless, they may be liable to account for the profits which they have made, if, while standing in a fiduciary relationship to Regal, they have by reason and in the course of that fiduciary relationship made a profit...

Strict:

- Profit rule applies:
 - Not just to taking money/property but also to information/opportunities
 - Whether or not the co could have made the profit itself
 - Whether or not the co suffered loss
 - Whether or not the directors acted bona fide, intending the co to benefit
- Note that the chairman in *Regal* was not liable under the profits rule for profits made by third parties

Furs Ltd v Tomkies (1936) 54 CLR 583

- The defendant Tomkies was managing director of the plaintiff company and manager of the tanning, dyeing and dressing branch of its business.
- Another company expressed interest in purchasing this portion of the business and Tomkies was directed by his board to conduct negotiations on behalf of the plaintiff. During these negotiations, the potential purchaser told Tomkies that it was interested in acquiring the business only if it was assured of securing his (ie, Tomkies') services.
- After Tomkies had agreed to a service contract with the purchaser which included payment to him of £5,000 in addition to salary, the purchaser's final offer was only for £8,500.
- The board of the plaintiff company accepted this offer. Neither the board nor shareholders were aware of the payment to Tomkies, who took pains to conceal it from them.

Rich, Dixon and Evatt JJ:

- Inflexible rule: except under the authority of a provision in the articles of association, no director shall obtain for himself a profit by means of a transaction in which he is concerned on behalf of the company unless all the material facts are disclosed to the shareholders and by resolution a general meeting approves of his doing so, or all the shareholders acquiesce
- No excuse to say that the co could not have obtained the profit or that, unless Tomkies had agreed to work for the purchaser, the sale would not have gone ahead.

Cook v Deeks [1916] 1 AC 554:

Facts:

- The Toronto Construction Co was formed to execute a tender to construct a railway line for the Canadian Pacific Railway Co (CPR). When that contract was successfully completed, the CPR commenced negotiations with three directors of the Toronto Co, GS Deeks, GM Deeks and Hinds, for constructing another line.
- GS Deeks, GM Deeks and Hinds together held three quarters of the capital in the Toronto Co. The remaining capital was held by Cook. The four were the only directors of the company.
- Cook's fellow directors decided that he should be excluded from any new contract
- Dominion Co then carried out the new contract
- Cook brought proceedings against the other directors and the Dominion Co claiming that they held the contract for the benefit of the Toronto Co.

Where they in breach of duty? YES

- The opportunity was clearly in company's line of business (i.e. it was directly related to the business of the company rather than being something incidental)
- Directors acting in their capacity as majority shareholders cannot use their voting power (75%) to approve the transaction and make a present to themselves (allow a majority to oppress a minority).
- It is immaterial that the company could not pursue the opportunity itself (*Regal Hastings*).

Industrial Development Consultant Ltd v Cooley [1972] WLR 443: resignation to exploit opportunity

Facts:

- The plaintiff company provided comprehensive construction services (namely, as architects, engineers and project managers) to large industrial enterprises. The defendant Cooley, an architect, had been its managing director.
- Cooley wrote on behalf of the plaintiffs to the Eastern Gas Board (Board) offering the plaintiffs' services in designing and constructing new gas depots

- The deputy chairman of the Board, approached Cooley, indicating that the Board was interested in building gas depots and enquiring as to his availability to undertake the work.
- 16 June he represented to the chairman of the plaintiffs' holding company that his health was such as to prevent him from carrying on as managing director. On this basis, he was released from his position as from 1 August.
- On 6 August, he was employed by the Board for a project which was substantially the same work as the plaintiffs had tried to obtain in February 1968.

Roskill J:

- Irrelevant that unlikely IDC would have got contract
- Irrelevant that info communicated to Mr C privately rather than in course of negotiations on behalf of co
- Conclusive point was that Mr C had put himself in position where his duty and interests conflicted by dealing with gas co while still MD of IDC
- While acting as MD it was his duty to pass on to IDC info that came to him that was of concern to IDC
- party with the Eastern Gas Board in direct conflict with his pre-existing and continuing duty as managing director of the plaintiffs → forbidden

IN THE COURSE OF RESIGNING: A director is still precluded from exploiting the opportunity **even after their resignation** where the **resignation has been prompted or influenced by a wish to acquire the opportunity sought by the company** OR where it was **their position rather than a fresh initiative that led them to the opportunity later acquired** (*Canadian Aero Services* per Laskin J).

Allowing the director to benefit/taking the benefit in private capacity:

- Can the general meeting permit the director to benefit?
 - o By constitution, ratification, prior authorization
 - o *Regal Hastings Ltd v Gulliver* per Lord Russell of Killowen: "They could, had they wished, have protected themselves by a resolution (either antecedent or subsequent) of the Regal shareholders in general meeting."
 - o *Furs v Tomkies*: "His one resource, if he was resolved to adopt the unwise course of acting in the transaction on behalf of his company and yet seeking a profit for himself, was complete disclosure to and confirmation by the shareholders."
 - o *Cook v Deeks* - ratification held to be ineffective

ALLOWING THE DIRECTOR TO BENEFIT IN PRIVATE CAPACITY:

STARTING POINT: There seem to be some opportunities clearly outside a company's interests that a director can pursue (eg; *Peso*). On one view, ***Peso* may just be an outlier** as the other cases talk about the strictness of the rule. On the other hand, even *Canadian Aero Services* acknowledges that the **way in which the opportunity arises** must be a factor to consider.

Peso Silver Mines v Cropper:

- Can the board of directors approve a director acting in conflict/obtaining a profit from their position?
- Mr Cropper did not have to account to *Peso* for the opportunity
- He had not obtained his interest by reason of his position as a director of *Peso* or in execution of that office
- Mr Cropper had no special information, the co had rejected the opportunity in good faith - the opportunity was no longer in the co's line of business

Queensland Mines Ltd v Hudson (1978) 52 ALJR 399

Facts:

- Hudson managing director of Qld Mines (formed to acquire uranium mining options)
- With the encouragement of Korman (who controlled Factors), Hudson approached the Tasmanian Government in August 1960 to seek a mining exploration licence for iron ore in the Savage River district.
- Hudson had used the resources and good name of Queensland Mines, the formal application for the licence was made in Hudson's own name
- On 15 March 1961, Hudson resigned as managing director of Queensland Mines to devote his full energies to the iron ore project. (He did, however, remain a director of the company until 1971.) From 1961 he acted entirely on his own and at his own expense in relation to the Tasmanian iron ore project.

Court said: not in breach

- Mr Hudson not liable to account for profits
- Two rationales:
- Co had rejected opportunity so the opportunity was no longer in the co's line of business - outside scope of Mr Hudson's relationship with the co
- Co had given fully informed consent for Mr H to go ahead
- Note long delay in bringing action
- Note also that there was effectively acquiescence by all shareholders
 - o Directors **passed a resolution** that the **company was not interested in the opportunity** so that Hudson could act.
 - o (1) Once the resolution had been passed, there was not a conflict anymore because Hudson's role with the company no longer encompassed anything to do with this opportunity (**directors put the opportunity outside the company's interest**).
 - o (2) Company's **fully informed consent** had been obtained
 - **Special circumstances in *Queensland Mines***: Joint venture company, between 2 companies each of whom had 50% of the shares, **each knew clearly what was going on**.
 - Representatives of the company's shareholders had given their **approval**.

STATUTORY DUTIES: CONFLICTS AND PROFITS (SS C AND 183)

NB: have to show that their purpose was to gain an advantage (does not matter whether advantage is actually obtained/detriment actually suffered). SS. 182 and 183 do NOT require proof that the director actually achieved their purpose in obtaining a benefit for themselves or another person. Rather, the sections require proof that the director believed that the intended result would be an advantage for themselves or for some other person or a detriment to the company (Chew).

MEANING OF IMPROPER:

TEST: We must ask whether the use of position is improper, given the standards of conduct expected by reasonable people with knowledge of the position and the circumstances of the case (*Byrnes* per Toohey and Gaudron JJ).

MISUSE OF POSITION: S 182

STATE: Under s 182, a director, secretary, other officer, or employee of a corporation must not improperly use their position to (a) gain an advantage for themselves or someone else or (b) cause detriment to the corporation.

- **ASIC v Adler**: Mr Adler, Mr Williams and Adler Corp were in breach of s 182 – allowed them to gain an advantage
- Followed Chew- improper purpose to be found objectively- does not depend on defendant's consciousness of impropriety

NB: If X has breached a director's duty (general or statutory), this is extremely good evidence that they have NOT met the standard of conduct expected of a reasonable person in their position.

MISUSE OF INFORMATION: S 183

STATE: Under s 183, a person who obtains information because they are or have been a director or other officer or employee of a corporation must not improperly use the information to gain an advantage for themselves or someone else or cause detriment to the corporation.

BREACH OF THESE: civil penalty provisions; potential criminal liability (s 184(2) and (3))

Section 184(2): A director, other officer or employee of a corporation commits an offence if they use their position dishonestly: (**FOR s 182**)

- o (a) with the intention of directly or indirectly gaining an advantage for themselves, or someone else, or causing detriment to the corporation; or
- o (b) recklessly as to whether the use may result in themselves or someone else directly or indirectly gaining advantage, or in causing detriment to the corporation
- Note also s 184(2A) no defense that intent was to gain advantage for corporation or that the result was direct or indirect gain to the corporation