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Week 1 – Nature and Incorporation of Companies

Overview

• Company law regulates the creation, structure, management, and dissolution of corporations in Australia.
• The Corporations Act 2001 (Cth) is the principal legislation, administered by ASIC (Australian Securities and Investments Commission).
• Company law ensures accountability, transparency, and protection for investors, creditors, and the public.
• The corporate form facilitates economic growth by separating ownership and management, limiting liability, and providing perpetual succession.

Key Features of a Company

• Separate legal entity – distinct from its members and directors.
• Limited liability – shareholders' liability limited to unpaid amounts on shares.
• Perpetual succession – continues despite changes in membership.
• Transferable shares – ownership can be transferred easily.
• Centralised management – directors manage, shareholders own.
• Ability to sue and be sued in its own name.

Legal Personality

• Upon registration, a company becomes a separate legal person (Corporations Act s 119).
• A company can hold property, sue and be sued, and continue independently of its members.
• Members are not liable beyond their share capital unless they provide guarantees (s 516).

Key Case: Salomon v A Salomon & Co Ltd [1897] AC 22

Facts: Salomon formed a company and sold his boot business to it. He held most shares and was a secured creditor. When the company failed, liquidator argued the company was a sham.
Held: The company was a distinct legal person. Salomon was not personally liable for its debts.
Principle: Upon registration, a company is a separate legal entity from its members, even if one person controls it.

Significance

• Foundation of modern corporate law.
• Shields shareholders from personal liability.
• Criticised for potential abuse (use of "corporate veil" to avoid obligations).

Lifting or Piercing the Corporate Veil

Courts may disregard the separate entity principle in limited circumstances:
• To prevent fraud or sham (*Gilford Motor Co Ltd v Horne* [1933] Ch 935).
• To avoid evasion of legal duties (*Jones v Lipman* [1962] 1 WLR 832).
• Where agency exists between company and controlling individual (*Smith, Stone & Knight Ltd v Birmingham Corporation* [1939] 4 All ER 116).
• Group enterprise doctrine – sometimes used where subsidiaries act as agents or alter egos.
• Statutory veil lifting occurs in cases like insolvent trading (Corporations Act s 588G) or when directors incur personal liability for company offences.

Advantages of Incorporation

• Limited liability encourages investment.
• Separate legal personality provides continuity.
• Transferability of shares allows liquidity.
• Access to external capital markets.
• Credibility and regulatory structure.

Disadvantages

• Formalities and regulatory compliance costs.
• Separation of ownership and control may cause agency problems.
• Limited liability can enable moral hazard (risk-shifting to creditors).

Registration Process

• Governed by Chapter 2A of the Corporations Act.
• Requirements under s 117:
– Name of company.
– Type of company (public or proprietary).
– Registered office and principal place of business.
– Share structure and details of members, directors, secretary.
• Upon registration, ASIC issues an Australian Company Number (ACN) and certificate of incorporation.
• Company comes into existence at the beginning of the day on which it is registered (s 118).

Types of Companies

1. Proprietary company (Pty Ltd):
   – Restricted to 50 non-employee shareholders (s 113).

– Cannot raise funds from public.
– Often family or small business structures.

2. Public company (Ltd):
   – May offer shares to public (subject to disclosure rules).
   – Must have at least 3 directors and 1 company secretary (s 201A).
   – Subject to stricter reporting and audit obligations.
3. Companies limited by guarantee (e.g. charities).
4. Unlimited companies (rare).
5. No liability companies (for mining ventures).

Company Constitution and Replaceable Rules

• Internal governance governed by:
– A constitution adopted by members (s 136).
– Replaceable rules under s 141 (default provisions).
• Replaceable rules cover matters like:
– Director appointment/removal.
– Meetings.
– Dividends and share transfers.
• A proprietary company with a sole director/member may choose to operate without replaceable rules (s 135(1)).

Pre-registration Contracts

• Promoters may enter into contracts before incorporation.
• Common law: company could not ratify pre-incorporation contracts because it did not exist (*Kelner v Baxter* (1866) LR 2 CP 174).
• Statutory solution: Corporations Act s 131.
– Person who enters into a contract on behalf of a company before registration is personally liable unless the company ratifies the contract within a reasonable time.
– Court can order company or person to pay damages if contract not performed.

Promoters and Fiduciary Duties

• A promoter stands in a fiduciary relationship with the company being formed.
• Must disclose any profits, interests, or secret commissions.
• Breach may lead to rescission or account of profits (*Erlanger v New Sombrero Phosphate Co* (1878) 3 App Cas 1218).

Corporate Veil and Group Enterprises

• Group of companies are generally treated as separate entities.
• Courts reluctant to treat group as single entity unless agency or sham exists (*Adams v Cape Industries plc* [1990] Ch 433).
• However, statutory provisions can treat group as consolidated (e.g. taxation, insolvency).

Common Law and Statutory Interplay

• Corporate personality doctrine from *Salomon* supplemented by statutory obligations under Corporations Act.
• Directors' duties (ss 180–184) ensure accountability despite limited liability.
• Disclosure and reporting rules protect creditors and investors.

Exam Focus

• Identify when separate legal personality applies.