

## CORPORATE CONTRACTING

### Step 1: Introduction

- [Company] [wants/does not want] to be bound by the K with [X] and may argue there is a corporate contracting issue.
- Companies can enter Ks (s 124(1)) either directly (s 127) [Step 2A] or indirectly through an agent with the requisite authority (s 126(1)) [Step 2B], provided the relevant requirements are met.

### Step 2A: Direct Contracting

- Companies can contract directly with a 3P where a K has been executed by the company:
  - In accordance with s 127. **OR**
  - In accordance with the company's constitution (s 127(4)). No statutory restriction on how a constitution allows a document is executed (including a deed) (ss 127(1)-(2)).
- K was executed [with the company's common seal: Step 2AA]/[without the company's common seal: Step 2AB].

### Step 2AA: Direct Contract without a Common Seal

- A company may execute a document without using a common seal if the document is signed by:
  - 2 directors of the company (s 127(1)(a)); or
  - A director and a company secretary of the company (s 127(1)(b)); or
  - A sole director of a Pty company who is also the secretary (s 127(1)(c)).
- [If not done] The requirements of s 127 have been complied with as the document was not executed by 2 directors or a director and the secretary and the company is not a sole director company.
- [X] may attempt to rely on statutory assumptions [Go to Step 3].

### Step 2AB: Direct Contract with a Common Seal

- A company may execute a document with their common seal fixed to the document and witnessed by:
  - 2 directors of the company (s 127(2)(a)); or
  - A director and a company secretary of the company (s 127(2)(b)); or
  - A sole director of a Pty company who is also the secretary (s 127(2)(c)).
- [If not done] The requirements of s 127 have been complied with as the seal fixing was not witnessed by 2 directors or a director and the secretary and the company is not a sole director company.
- [X] may attempt to rely on statutory assumptions [Go to Step 3].

### Step 2B: Indirect Contracting

- [3P] will argue that [company] is bound to the K as it was entered into by [name], who is an agent for [company], arguing they had actual or apparent authority to do so (s 126(1)).

### Step 2BA: Actual Authority (Cannot have Actual Authority if a Person has been Dismissed)

#### Express Actual Authority

- [Agent] has actual authority if they were expressly appointed by the company to K for a specific purpose (s 198A).
- Requires constitutional provision; board minutes; service K; a deed; oral authorisation; resolution.

- A person with actual authority who purchases over a set amount may have **apparent authority** [Step 2BB].

### Implied Actual Authority (By Position)

- [Agent] may have implied actual authority to enter Ks customarily attaching to their position (*Hely v Brayhead*).
- **Managing Director/CEO:** Implied actual authority to enter ordinary trading transactions (*Hely v Brayhead*).
  - **Includes:** Supervising the daily running of the company, supervising other managers and company business; engaging persons to do work; borrowing money; giving securities over company's property.
  - **Exception:** Can't enter transactions outside scope of ordinary business (buying assets unrelated to the business) or sell the company's main business.
- **Individual Directors:** No authority unless appointed by board as an agent. They must vote as part of the board. Actual authority vested in the board and not a single director (*NAB v Sparrow*).
- **Chairman:** No authority unless appointed by board as an agent (*Hely v Brayhead*).
- **Company Secretary (responsible for keeping records):** Has implied authority to enter Ks that relate to administrative matters such as hiring a car (*Panorama*).
- **Purchasing officer:** Has implied authority to enter Ks for the purchase of goods and services.
- **Head of HR:** Will have implied authority to hire and fire below a certain level of management.

### Implied by Acquiescence

- [Agent] will have implied authority to enter certain Ks if the board has previously consented to the agent entering those types of Ks or engaging in a similar course of dealings (*Brayhead*).
  - Implied authority when signee often enters Ks without board knowledge and reports afterwards.
- [Consider frequency of acquiescence if it relates to minor or major matters].

## Step 2BB: Apparent (or Ostensible) Authority

- To enforce a K entered by an agent with no actual authority, [3P] must establish that a representation was made to them that the agent had authority to enter a K of that kind on behalf of the company. The representation made must be by a person with authority to make it and the contracting party must have relied on the representation (*Freeman*).

### Element 1: Representation

- There must be a representation or holding out (words or conduct) to [3P] that [agent] had authority to make particular Ks on [company's] behalf.
  - Staying silent (*Brick and Pipe*).
  - Company made representation by equipping agent with title status and facilities (*BNP Paribas*).
  - Board made out that the agent was MD when he wasn't (*Freeman*).

### Element 2: Representation made by Person with Authority

- Only a party with actual authority may represent to [3P] that the agent has authority to enter the K (*Crabtree*).
  - Representing oneself as having authority will not be sufficient (*NAB v Sparrow*).
- Failing to abide by constitution or improper appointment won't have actual authority [Go to statutory assumptions].
- Board representation is sufficient as board has actual authority (*Freeman*), unless the 3P knew (or was put on inquiry that the Board revoked this authority).

### Element 3: Reliance on the Representation

- The 3P must rely on the representation in entering the K (estoppel) (*Freeman*).

- If the 3P knows or ought to have known the agent does not have actual authority then there is no estoppel (*Freeman*).
- If there is doubt about the parties' authority, the 3P is put on notice and should make further inquiries to find out the party's authority. Failure to do so will prevent them enforcing the K (*Northside Developments*).

### Step 3: Statutory Rules / Assumptions

- [3P] is entitled to make the assumptions in relation to 'dealings' with a company under s 129 (s 128(1)), unless [3P] knew or suspected that a statutory assumption in s 129 was incorrect (s 128(4)) despite any fraud/forgery by [agent] (s 128(3)).

### Step 3A: Did 3P have "Dealings with the Company"?

- [Did the person who signed the contract have the requisite authority?].
- As [X] did not [comply with s 127] OR [have authority to bind company as an agent] the outsider will have to rely on statutory assumptions to bind the company.
- [3P] must prove they had dealings [in the specific transaction] with [Company] or an agent with **actual/apparent** authority to act on [Company]'s behalf (s 128; *ANZ v Frenmast*).
  - 'Dealings' means engaging with someone who has authority to negotiate on behalf of the company (s 128; *ANZ v Frenmast*).
- Here, dealings can be demonstrated by [X's authority to negotiate: **For authority, go to: Step 2BA – 2BB**].

### Step 3B: Apply Assumptions (Only Apply to Companies)

- **WRITE:** Given dealings with the company is established, the assumptions under s 129 can applied (s 128) even if there has been fraud or forgery in connection with the dealings (s 128(3)).
- The assumptions can be relied on in combination and are cumulative (s 129(8); *Oris*; *Soyfer*).
  - Once 3P can assume that someone is a director/secretary (ss 129(2) or (3)), the 3P can then assume a document is duly executed (s 129(5)) as it has appearance of being signed by director/secretaries (*Sunburst*).
  - The assumptions are independent of each other and can apply even if 3P suspected 1 was incorrect.

### Constitution / RRs

- A person may assume that the company's constitution, and/or replaceable rules have been complied with (s 129(1)), and the 3P is not required to have knowledge of constitution or RRs (*Oris v NAB*).

### Directors/Secretaries

- A person may assume that anyone who appears, from publicly available information from ASIC provided by the company, to be a director or a company secretary of the company:
  - Has been duly appointed (s 129(2)(a)); and
  - Has authority to exercise the powers and perform the duties customarily exercised or performed by a director or company secretary of a similar company (s 129(2)(b)).
- Don't need to know / check the information from ASIC, can assume it.

### Officer/Agent (Codification of CL Apparent / Ostensible authority)

- A person may assume that anyone who is held out by the company to be an officer or agent of the company:
  - Has been duly appointed (s 129(3)(a)); and

- Has authority to exercise the powers and perform the duties customarily exercised or performed by that kind of officer or agent of a similar company (s 129(3)(b)).

### Proper Performance of Duties

- A person may assume that company officers and agents properly perform their duties to the company (s 129(4)), including acting with care and diligence, in good faith and in the best interests of company, and for a proper purpose (*Pico Holdings*).

### Document Duly Executed without Seal (Use if there is a Forgery)

- A person may assume that a document has been duly executed by the company if the document appears to have been signed in accordance with s 127(1) (s 129(5)) even if the signatures are illegible (*Sofyer*).

### Document Duly Executed with Seal

- A person may assume that a document has been duly executed by the company if the company's common seal appears to have been fixed to the document and witnessed in accordance with s 127 (ss 129(6)(a)-(b)). Still valid even if signatures are illegible (*Sofyer*).

### Genuine and True Copy

- A person may assume that a company officer or agent who has authority to issue a document or a certified copy of a document on its behalf also has authority to warrant that the document is genuine or a true copy (s 129(7)).

### Step 3C: Exception: Did 3P Know or Suspect to the Contrary?

- A person cannot rely on statutory assumptions if they knew or suspected the assumption was incorrect (s 128(4)).
- Person not regarded as knowing information just because it was on public record or if reasonable person would have known the information (*Oris v NAB*) or because the information is available to the public from ASIC (s 130).
- Company has burden to establish actual subjective knowledge or suspicion (*Sunburst*).
- The onus of proof lies with the person challenging a party's right to make the assumption (*Sofyer*).

### Suspicion

- Suspicion is more than speculation (*Old Bacon*).
- Suspicion is a positive feeling of actual mistrust (*Oris v NAB*).
- Wilful blindness almost always amounts to suspicion (*Soyfer*).

### Step 4: Indoor Management Rule (Common Law)

- [3P] may argue the IMR will bind [company] to the K. [3P] is not required to know [company]'s constitution and is entitled to assume all internal procedural requirements have been met (*Turquand*).
- [**Consider:** Was the person representing the company acting within the scope of their actual or apparent authority, but some procedural irregularity is present?].
- IMR is not intended to allow a company to hold 3P to Ks which the company itself has failed to authorise or ratify. If the 3P wants to get out of the K, they can withdraw offer before it is ratified by the company's board.

### Exceptions

- IMR **does not** apply where the company alleges forgery in the execution of the document in the narrow sense (fake seal or forged signature).
  - IMR **does apply** where forgery in a wider sense (seal or signatures are genuine but no authority to execute).
- IMR **does not** apply where there a 3P has constructive knowledge of an irregularity in the transaction (*Northside*).

## SHARE CAPITAL, DEBT CAPITAL, AND DIVIDENDS

### COMPANY'S POWER TO ISSUE SHARES

#### Shares

- Shares are personal property that are transferable and capable of devolution by will or law (s 1070A(1)).

#### Types of Shares

- **Preference Shares:** Right to receive dividends ahead of ordinary shareholders.
- **Ordinary Shares:** Receive dividends if company has surplus profits after payment of preference SH dividends.

#### Directors Power to Issue Shares

- Companies and directors have power to issue shares to raise equity for the operation of the company (ss 124, 198A).

#### Share Value

- A share's value is a proportion of the total net worth of the company as per the balance sheet value of net assets.
- Listed company market value shares are valued by the economy / market perception / present and estimated future earnings / prospects of the company's industry.

### Power to Issue and Allocate Shares

#### Pty Company

- Pty companies may offer shares (s 254D (RR)). Before issuing particular class share, directors must offer them to existing SHs in that class (s 254D(1) (RR)) and issue any remaining shares as they see fit (s 254D(3)).
- **Exception:** A company can circumvent the above requirement by passing an ordinary resolution (s 254D(4) (RR)).

#### Issuing Shares on Registration

- A company may issue shares on registration by establishing share capital of a particular amount and then having one or more members subscribe to this initial share capital (s 117(2)(k)). Shares on a registration application are taken to be issued upon registration (s 120(2)). ASIC must be notified of share issues within 28 days (s 254X(1)). Consideration does not need to be cash (*Wragg*).

#### Issuing Shares After Registration

- Companies have the power to issue shares (s 124) with terms (s 254B). Process for issuing after registration:
  - **Step 1:** Intending member applies to board for specified number of shares. If the application is accepted, it gives rise to a K of allotment. Consideration does not have to be in cash (*Wragg*).
  - **Step 2:** K completed by issue of shares when board registers members name or delivers a share certificate.

#### When Shareholder may be Required to Pay Up for Partly Paid Shares

- SHs are liable to pay up for their shares in accordance with their terms of issue (s 254M(1)).
- **Companies Limited by Shares:** Shareholding liability is limited to the amount owing (if any) to the company for the shares bought (s 516). Ltd companies can limit calls for payment of unpaid shares to situations where the company is externally administered. A special resolution is required (s 254N).
- **No Liability Companies (Mining):** SHs cannot be liable on calls for unpaid shares (s 254M(2)). If a call is made and it is unpaid after 14 days, the SH cannot receive dividends and must forfeit their share until the call is paid (s 254Q).


## CLASS RIGHTS

### Step 1: Introduction

- A company may issue different classes of shares under s 124 relating to bonuses, preferences and partly paid shares (s 254A) on terms it chooses (ss 254B(1)).
  - Preference shares can only be issued with certain rights attached (voting rights / repayment of capital), if those rights are in the company's constitution or have been approved by a special resolution (s 254A(2)).
  - If this involves the alteration of the constitution, that may be achieved by a special resolution (s 136(2)).

### Step 2: Determine Whether There Are Class Rights

#### Informal Creation of Class Shares

-  Company treating different shareholders differently.
- If the [company] is treating SHs as if they belong to different classes (different rights attached to named SHs), even if not specified in the constitution, the court will assume the company has different classes of SHs (*Crumpton*).
  - Named SHs had rights to subscribe for additional future shares and power to appoint directors (*Cumbrian*).

#### Formal Creation of Class Shares

- For [Company] to create preference shares for certain matters, it must detail the rights of preference SHs in its constitution OR have the rights approved by special resolution (s 254A(2)). Certain Matters:
  - Repayment of capital (if the company becomes insolvent) (s 254A(2)(a)).
  - Participation in surplus assets and profits (s 254A(2)(b)).
  - Cumulative and noncumulative dividends (s 254A(2)(c)).
  - Voting rights (2 votes as opposed to 1) (s 254A(2)(d)).
  - Payment priority of capital / dividends relating to other shares or classes of preference shares (s 254A(2)(e)).

### Step 3: Is There a Variation / Cancellation of Class Rights?

- The court will consider whether the actions of [company] in [action] is a variation of class rights. While ss 246B, 246D give some protection to the holders of classes of shares against variation of their rights without their consent, these protections apply only if there is a variation or cancellation of rights.

#### Deemed Class Right Variations

- Certain actions constitute a variation of rights (s 246C). In this case s 246C [(1), (2), (5) or (6)] is most relevant because it relates to [explain connection]. Therefore, the amendment contemplated by [Y] is deemed a variation.
  - **Converting Ordinary to Preference Shares:** Company converting ordinary shares into preference shares or vice versa is deemed to have varied class rights (s 254G(1)).
  - **Creating New Classes:** Dividing shareholders into further classes with different rights (s 246C(1)).
  - **Varying Rights:** Where company varies rights attaching to only some shares in a class (s 246C(2)).
  - **Creating Preference Shares:** If new shares have different rights to existing shares and those rights are not provided in the constitution or document lodged with ASIC, this varies rights attached to shares that are already issued (s 246C(5)).
  - **Creating More Preference Shares:** Unless authorised by constitution, a company issuing new preference shares that rank equally with existing preference shares is deemed to have varied rights attached to shares already issued (s 246C(6)).

#### Step 4: Has the Proper Process Been Followed?

- Variations to Class rights are regulated to protect rights of holders against directors or controlling members (s 246B).

##### If Constitution has Procedure

- If a constitution has a procedure for varying / cancelling class rights, the procedure must be followed (s 246B(1)).

##### If No Procedure in Constitution

- Class rights may only be varied/cancelled by special resolution (all members) (s 246B(2)):

##### AND

- Special resolution of class right holders (s 246B(2)(c)(i)).

##### OR

- With written consent of 75% of members of affected class (s 246B(2)(d)).
- Written notice must be given within 7 days after the variation (s 246B(3)). Strict liability offence (s 246B(4)).

#### Step 5: When does the Variation Take Effect?

- A variation takes effect one month after passing unless a court application is made to set it aside (s 246D(3)(a)).

##### OR

- A variation will take effect when the court application is withdrawn or finally determined (s 246D(3)(b)).

#### Step 6: Can the Variation/Alteration be Set Aside?

- Members against a class right variation may apply to the courts within one month of the change to have the change set aside if they consist of at least 10% of that affected class (ss 245D(1)-(2)).
  - If less than 10% of members, consider if the company has complied with the prescribed method of change within the constitution; a breach of statutory K may lead to statutory injunction (s 1324).
- Written notice must be given within 7 days after the variation is made (s 246B(3)) and failing to do this is an offence of strict liability (s 246B(4)).
- The court can then set aside the variation only if satisfied that it unfairly prejudices the applicants (s 246D(5)) but must apply within a month of the variation/cancellation (s 246D(2)).

##### Members Applying to the Courts to Change/Set Aside the Variation/Cancellation of Class Rights

- The court will consider whether the change unfairly prejudices the applicants, however, this does not apply to variation of the enjoyment of class rights (actions that impact % of voting rights) (*Greenhalgh*).
- “Is there a Variation/Cancellation of Class Rights?” above for deemed variation of class rights.



## REDUCING SHARE CAPITAL: SHARE BUYBACKS / FINANCIAL ASSISTANCE / DIVIDENDS

- **Reducing share capital:** When money paid to a company for a member's share is returned to the member.

### Step 1: Introduction

- Companies are generally prohibited from reducing issued share capital (*Trevor v Whitworth*), unless the statutory requirements are met. [Company] must not reduce its capital unless it is in compliance with s 256B(1) (s 256D(1)):
  - Must be fair and reasonable to the company's SHs as a whole (s 256B(1)(a)); and
  - Must not materially prejudice the company's ability to pay its creditors (s 256B(1)(b)); and
  - Must be approved by SHs under s 256C (s 256B(1)(c)).

### Step 2: Identify the Reduction in Share Capital

- Share capital reductions can take a few forms:
  - Buying back shares / Payment to shareholders that involves a return of the shares.
  - Cancelling shares / Cancelling/reducing the amount unpaid on partly paid shares.
  - Reduce the issue price of shares and repay the difference to shareholders.
  - Swaps shares for debentures (shareholders become creditors).
- Cancelling shares without consideration is reducing share capital, but s 256B(1)(b) does not apply (s 256B(1)).

### Step 3: Is the Share Reduction Valid?

- **WRITE:** A reduction of share capital is valid if it satisfies the following requirements.

#### Step 3A: Fair and Reasonable to Members

- **WRITE:** A capital reduction must be fair and reasonable to SHs as a whole (maj & min) (s 256B(1)(a)). The [company] has the onus of proving (s 1324(1B)).
  - Adequacy of the consideration paid to shareholders (fair price) (*Winpar Holdings*).
  - Whether the reduction would have the practical effect of depriving some SHs of their rights (stripping company of funds that would have been dividends for preference SHs).
  - Whether the reduction was used to affect a takeover and avoid the takeover provisions.
  - Must consider what led to the proposed reduction, and events after. \$2.78 return of shares was not fair and reasonable, because shares acquired for \$4 (*Catto v Ampol*).
  - Giving benefits minority and majority SHs that they otherwise would not have gotten is fair and reasonable. Majority got 100% ownership; minority got higher price (*Winpar Holdings*).
  - Reduction of capital that only involved payment to one type of SH is not fair and reasonable. Fairness requires at least "equal treatment between ordinary and preference SH" (*Re Fowlers*).

#### Step 3B: Must Not Materially Prejudice to Company's Ability to Pay Creditors

- **TEST:** The capital reduction must not materially prejudice the company's ability to pay its creditors (s 256B(1)(b)).
- The [company] has the onus of proving (s 1324(1B)).
- **Note:** A company must lodge details of a proposed reduction with ASIC which will alert creditors (s 256C(5)).



- [Assess position before and after reduction and see whether company/creditors are in worse position after].

### Step 3C: Approved by Shareholders

- **TEST:** The capital reduction must be approved by members under s256C (s 256B(1)(c)). [Determine if it is equal or selective reduction].

#### Equal Reduction

- **TEST:** If the reduction relates to ordinary shares, it must be approved by ordinary resolution passed at a general meeting (s 256C(1)). The terms must be the same for each ordinary shareholder and apply to each shareholder in proportion to the number of ordinary shares they hold (s 256B(2)).
  - All shareholders have their holdings reduced proportionally. E.G.: Company with 100 shares reduces the share capital by 50%, each shareholder would have their shareholding reduced by 50%.

#### Selective Reduction

- **TEST:** If the reduction is not an equal reduction, it is a selective reduction (s 256B(2)) and requires a special resolution with no votes cast by members receiving consideration for reduction **OR** every ordinary SH agrees to a selective reduction (s 256C(2)).
  - Reduction of share capital only affecting certain SHs or specific share classes.

#### Cancellation of Shares

- **Additional Requirement:** A special resolution must be passed by the class of SHs whose shares are being taken (s 256C(2)).

### Step 3D: Consequences

- **TEST:** A breach does not affect the validity of the reduction, or any connected transaction and the **company** is not guilty of any offence (s 256D(2)). A stat injunction will be available to SHs/creditors whose interests are affected (s 1324).
- **Civil Penalties:** Person involved (s 79) in the contravention may be subject to a civil penalty (s 256D(3)).
- **Criminal Penalties:** Person involved (s 79) in the contravention may be subject to criminal consequences if there was dishonesty involved (s 256D(4)).
- **Director's Duties:** May be a breach of director's duties even if it is authorised under these sections (s 260E).
- **Note:** Look at insolvent trading if reduction causes company to become insolvent or it was insolvent at the time.

### Step 4: Is it a Share Buy Back (SBB)?

- **TEST:** [company] may buy back its own shares if the purchase does not materially prejudice its ability to pay back its creditors and the correct procedure is followed as set out in ss 257B-J (s 257A). Once the transfer of shares is registered, the shares must be cancelled (s 257H).

### Step 4A: Identify the Type of Share Buyback

- **Equal access schemes:** The company offers to buy back ordinary shares from every person who holds them to buy back the same percentage of shares from each SH on the same terms (ss 257B(2), (3)).
- **On-market buy-back:** A buy back resulting from an offer made by a listed company (s 257B(6)).
- **Employee share scheme:** A scheme where shares can be acquired by / for the benefit of employees (s 9).
- **Minimum holding buy-back:** A buy back of all an SH's shares in a listed Company if the shares are less than a marketable parcel (s 9).

- **Selective buy-back:** A buy back that applies only to some SH's / a selective group of them but more importantly is not one of the above categories (s 9).

#### Step 4B: Are the Requirements Met?

##### Does it materially prejudice the creditors?

- **TEST:** The buyback must not materially prejudice the company's ability to pay its creditors (s 257A(1)).
- Material prejudice occurs where there is material diminution of company assets (*Adler*).
- **Onus:** The company has the onus of proving that the reduction will not prejudice its ability to pay creditors (s 1324(1B)) / onus is on those supporting the transaction (*Adler*).

##### Outline the Procedure

- **TEST:** SBB will exceed the 10/12 limit if the company buys back 10% (or more) of the smallest number of shares held in the company within the previous 12 months (ss 257B(4), (5)).
  - Company has 100 voting shares but within the last 12 months, they only had 50 voting shares, then a buy-back of 5 voting shares would exceed this limit.
  - Only applies to Equal access schemes, On-market buy-back, Employee share scheme.

##### Shareholder Approval Required to Exceed 10/12 Limit

- Terms of SBB agreement must be approved by ordinary resolution by SHs at a general meeting (s 257C(1)).
- Company must include the notice of meeting setting out all the material info to help the SHs make a decision when voting, unless it would be unreasonable to require the company to do so (s 257C(2)).
- **NOTICE:** company must lodge notice of meeting and send to shareholders and ASIC (s 257C(3)).

#### Step 4C: Sub-Conclusion

- A breach does not affect the validity of the reduction or any connected transaction and the company is not guilty of any offence (s 259F(1)). A stat injunction may be available to SHs/creditors whose interests are affected (s 1324).
- **Civil Penalties:** Anyone involved on the contravention may be subject to a civil penalty (s 259F(2)).
- A person is 'involved' in a contravention if, and only if, the person (s 79):
  - (a) has aided, abetted, counselled or procured the contravention; or
  - (b) has induced, whether by threats or promises or otherwise, the contravention; or
  - (c) has been in any way, by act or omission, directly or indirectly, knowingly concerned in, or party to, the contravention; or
  - (d) has conspired with others to effect the contravention.
- **Criminal Penalties:** Anyone involved on the contravention may be subject to criminal consequences if there was dishonesty involved (s 259F(3)).
- **Note:** Look at insolvent trading if reduction causes company to become insolvent or it was insolvent at the time.
- Company will incur debts for the purpose of directors' liability under s 588G when the reduction takes effect/buyback agreement is entered into (s 588G(1A)).

#### Step 5: Financial Assistance

- A company may financially assist a person to acquire shares in the company or its H/C if:
  - Giving the financial assistance does not materially prejudice the interests of the company, its SHs or the company's ability to pay creditors (s 260A(1)(a)); OR

- The assistance is approved by shareholders under s 260B (s 260A(1)(b)); OR
- The assistance is exempted under s 260C (s 260A(1)(c)).
- Assistance includes:
  - **Lending money:** To be used to acquire shares in the company.
  - **Guaranteeing loan repayments:** Where the proceeds of the loan are used to acquire shares in the company.
  - Providing assets as security for a loan.
  - Releasing person from a debt or other obligation already owed to the company; and
  - Acquiring assets at an inflated price.
- The company's transaction can be within the prohibition even if the transaction contains no element of a gift.

### Consider Both Broad and Narrow

- **Broad view:** There will be financial assistance irrespective of diminution (reductions) of company assets.
- **The narrow view:** [what appears to have been endorsed by the courts] is that there will only be financial assistance when the transaction diminishes the company's assets (*Burton v Palmer*).

### Step 5A: Material Prejudice

- Giving financial assistance does not materially prejudice the interests of the company, its SHs or a company's ability to pay its creditors (s 260A(1)(a)).
- Using financial assistance to misrepresent market value of shares / confidence in shares is a contravention of s 260A and materially prejudices the company and its SHs (*ASIC v Adler*).
- **Onus:** The onus is on [company] to show that financial assistance does not materially prejudice the company, shareholders or creditors (*Kinarra*). It is the effect/result rather than the intention that is relevant (*Adler*).
  - Acquiring assets at an inflated price.
  - Affecting company's ability to pay creditors: If it arises, also consider insolvent trading (s 588G).
- **Impoverishment Test (*Adler*):** Involves a conversion of the company's assets into one of a lesser value.
  - A company may be prejudiced by detrimental changes to their financial position / ability to conduct business.
  - A SH may be prejudiced by changes to dividends or a fall in share price.
  - A creditor may be prejudiced by transactions that lead to insolvency/transactions unlikely to be re-paid.

### Step 5B: Instances Assistance is Approved by Shareholders

- The assistance is approved by SHs under s 260B (s 260A(1)(b)). This involves:
  - Special resolution with no votes cast by persons acquiring shares/their associates (s 260B(1)(a)).
  - OR**
  - Unanimous resolution at a general meeting by all ordinary SHs (s 260B(1)(b)).
- **Company that gives FA becomes a S/C:** If the company that gives the financial assistance becomes a S/C of an Aust. H/C immediately after the person acquires its shares, the financial assistance must also be approved by a special resolution passed at a general meeting of that H/C (ss 260B(2), (3)).
- All relevant info for the decision must be provided to shareholders and lodged with ASIC (s 260B(4)-(7)).

### Step 5C: Instances in Which Financial Assistance is Exempt

- Financial assistance is exempt from s 260A if:

- The company's ordinary business consists of acquiring or created liens on partly paid shares or for facilitating payment instalments for shares (ss 260C(1)(a)-(b)).
- The company's ordinary business consists of providing financial assistance (ss 260C(2)(a)-(b)).
- The company is a S/C of a borrower in relation to debentures, the financial assistance is a guarantee / security, the borrower is a borrower in relation to the debentures because it is or will be liable to repay the money; and the guarantee or security is given by the company in the ordinary course of commercial dealing (ss 260C(3)(a)-(d)).
- It is for an employee share scheme approved by a resolution passed at a GM; and if the company is a S/C - a resolution passed at a GM of the listed Aust. H/C; or if the company is an Aust. H/C - a resolution passed at a GM of that H/C (ss 260C(4)(a)-(c)).
- The following types of financial assistance are exempted from s 260A:
  - A reduction of share capital in accordance with Division 1 of Part 2J.1 (s 260C(5)(a)).
  - A share buy-back in accordance with Division 2 of Part 2J.1 (s 260C(5)(b)).
  - Assistance given under a court order (s 260C(5)(c)).
  - A discharge on ordinary commercial terms of a liability that the company (s 260C(5)(d)).

### Step 5D: Conclusion

- A breach does not affect the validity of the reduction or any connected transaction and the **company** is not guilty of any offence (s 260D(1)). A stat injunction may be available to SHs/creditors whose interests are affected (s 1324).
- **Civil Penalties:** Anyone involved on the contravention may be subject to a civil penalty (s 260DF(2)).
- A person is 'involved' in a contravention if, and only if, the person (s 79):
  - (a) has aided, abetted, counselled or procured the contravention; or
  - (b) has induced, whether by threats or promises or otherwise, the contravention; or
  - (c) has been in any way, by act or omission, directly or indirectly, knowingly concerned in, or party to, the contravention; or
  - (d) has conspired with others to effect the contravention.
- **WRITE:** It is suggested the relevant person must have knowledge of all the essential facts (that it caused material prejudice and was financial assistance) and that the knowledge must be actual and not constructive (*ASIC V Adler*).

### Step 6: Dividends

- SHs cannot force companies to pay dividends even if it has sufficient surplus funds to do so (*Burland*).
- **Exception:** Unless it is a small company and the refusal to pay dividends is part of oppressive conduct.

### Step 6A: Rights to a Dividend

- **Constitution:** It is necessary to look at relevant rule in constitution.
- **No Constitution:** Directors have the power to pay a dividend without the prior need for a dividend declaration by shareholders. They the power to fix the amount, time of payment, and method (s 254U(1) (RR)).

### Rights to a Dividend

- **Public company:** Each share in a class of shares has the same dividend rights unless the constitution/special resolution provides otherwise (s 254W(1)).
- **Pty company:** Directors pay dividends as they see fit, subject to shares terms of issue (s 254W(2)).

### Step 6B: Requirements for Paying a Dividend

- A company must not pay a dividend unless all three requirements are met (s 254T(1)) and must do a 'balance sheet' test before declaring the dividend in accordance with accounting standards (s 254T(2)).

#### Requirement 1: Assets Must be Greater than Liability

- The company's assets exceed its liabilities immediately before the dividend is **declared** and the excess is sufficient for the payment of the dividend (s 254T(1)(a)).
  - Declare (s 254V(2)) means recommended by the board and approved by members at a meeting.
  - Directors typically 'fix' the amount/time/method of dividend payment (s 254U(1) RR) which does not incur a debt (s 254V(1)). The debt accrues when payable at the fixed time (can revoke decision prior) (s 254V(1)).

#### Requirement 2: The Payment of the Dividend is Fair and Reasonable to the Shareholders as a Whole

- The payment of the dividend is fair and reasonable to all the SHs (s 254T(1)(b))
  - Consider events leading to proposed reduction, and events after. \$2.78 return of shares was not fair and reasonable, because shares acquired for \$4 (*Catto v Ampol*).
  - Adequacy of the consideration paid to SHs (fair price) (*Winpar Holdings*).
  - Giving benefits minority and majority SHs that they otherwise would not have gotten is fair and reasonable. Majority got 100% ownership; minority got higher price (*Winpar Holdings*).

#### Requirement 3: Does Not Materially Prejudice the Company's Ability to Pay Creditors

- The payment of the dividend does not materially prejudice the company's ability to pay its creditors (s 254T(1)(c)).
  - Dividend payments would materially prejudice the company's ability to pay its creditors if the company would become insolvent because of the payment (Note 1 - s 254T).
  - Material prejudice occurs where there is material reduction of company assets (*Adler*). The onus is on those supporting the transaction (*Adler*).

### Step 6C: Paying a Dividend

- Directors may determine that a dividend is payable and fix the amount, time and method of payment (s 254U(1) RR).
- Interest is not payable on a dividend (s 254U(2) RR).
- The debt arises when the time for fixed payment arrives (revoking decision can be made before this time) (s 254V(1)).
- **If date has not passed yet WRITE:** The board can revoke the dividend any time before [date] and will thereby avoid the dividend being a debt that will trigger insolvent trading by the directors (s 588G(1A)).
- If the company has a constitution and it provides for the 'declaration' of dividends, the company incurs a debt when the dividend is declared (s 254V(2)).

### Step 6D: Consequences

- A breach does not invalidate the reduction or any connected transaction and the company is not guilty of any offence (s 256B(1)). A stat injunction may be available to SHs/creditors whose interests are affected by the breach (s 1324).
- **Civil Penalties:** Anyone involved on the contravention may be subject to a civil penalty (s 245D(2)).
- **Criminal Penalties:** Anyone involved in the breach may be criminal liable if there was dishonesty involved (s 245D(3)).
- **Note:** Look at insolvent trading if reduction causes company to become insolvent or it was insolvent at the time.

## DEBT CAPITAL

- Companies can borrow funds from lenders. Unlike dividends, loans are repayable regardless of whether the company has made a profit. Loans create a debtor and creditor relationship. Loans are governed by the law of contract.

### Step 1: Introduction

- A company can borrow money in the following ways:
- **Issue debentures:** Public debt acknowledgment via certificate including an undertaking to repay debt (s 124(1)(b)).
- **Secured Loan:** Company gives security to creditors who can use the security to recover debt (mortgage).
- **Unsecured Loan:** Creditors without a security risk not getting any funds if company defaults.
  - Raise Funds Publicly via Issue of Bonds to the Public.
  - Grant a Security Interest in Uncalled Capital (s 124(1)(e)).
  - Grant a Circulating Security Interest over Property (s 124(1)(f)).

### Security

- The form of security taken often depends on the nature of the company's assets. Two types of assets:
- **Real property** (land and fixtures):
  - Real property is generally secured by registering a mortgage on the relevant register (state based).
  - A general security interest granted over all the assets of the company will usually also secure real property.
  - This is not a mortgage in a registrable form. It is, in effect, an equitable mortgage and a caveatable interest.
- **Personal property** (everything else).

