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[MID-TERM]

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INTRODUCTION TO CORPORATIONS

PHASES OF CORPORATE REGULATION IN AUSTRALIA

“Corporation”	a legal device or artificial person that gives a fictional legal entity artificial legal personality, separate from those who created it and its members NOTE: the phrase corporation and company are virtually interchangeable)
Shareholders	- Reap financial gains (dividend yield and capital gains) - Do not need to participate (cannot actually manage the company)
- Management is conducted by professional managers with business and or technical skills - A company can sue and be sued in its own name; it can acquire, hold and dispose of assets, and enter into contracts and incur liabilities in its own name - A corporation is a separate legal entity - A corporation can typically do anything that a person can do	
How does a corporation come to exist?	
- A company comes into existence at the point it is registered by ASIC (<i>Corporations Act s 119</i>) following an application for registration which contains the necessary information (<i>Corporations Act s 117(2)</i>) principally of: - Need to select type of company - Need to select name of company - Need office of registration - Need consent of directors - Need to prepare corporations or replaceable rules - Need to complete form 201 - Upon registration ASIC must issue the company with a certificate of registration (<i>Corporations Act s 118</i>). Also, company comes into existence on registration (<i>Corporations Act s 119</i>).	
Corporations Act s 119 A company comes into existence as a body corporate at the beginning of the day on which it is registered. The company's name is the name specified in the certificate of registration	
Who is in charge of a corporation?	
Board of Directors	IN CHARGE - Can delegate their power to managers and executives
	- very relevant for LARGE companies. - larger a company is, the less likely the BOD are going to be dealing with the day to day affairs of the company & the more likely they would be to delegate powers Shareholders cannot be directly involved in the management of the corporation – however, they can influence the Board
SHAREHOLDERS THAT ARE TOO ACTIVE IN MANAGEMENT OF A COMPANY CAN BE DEEMED DIRECTORS - The Corporations Act includes anyone is acting as a director. - If people are getting involved in the affairs of the company, there is a good chance that they will be viewed as a director even if they are not formally appointed.	

Secretary	- only in charge of administration - calls meetings, keeps register of members up to date, can sign documents regarding administration but not management
Who is liable for the debt of a corporation?	
- The company is its own separate legal entity – it is liable for its own debt - The liability of the shareholders will depend on the type of company	
Unlimited liability company:	- shareholders are liable for ALL the debt of the company. - If the company cannot pay its debts then company is liable for all of its debt - These companies are not very popular (companies are generally created for the purpose of protecting people from liability). In Australia there are only about 500 unlimited liability company
Company limited by shares:	- shareholders are generally ONLY liable in the amount of any unpaid portion of their shares - e.g. if you buy shares worth \$10 and you have paid \$10 you can have no further liability
Main source of corporation law in Australia	
Corporation Act 2001 (Cth)	- This applies for all companies Federal law CANNOT make law regarding the creation of the company - This was a problem –e very state had to make its own laws for the creation of companies - There have been many attempts at uniformity across states (essential for foreign investment)
Other source of law	- The Corporations Regulation 2001 (Cth) - ASIC Act 2001 (Australian Securities and Investments Commission Act 2001 (Cth)) - The accounting Standards - ASX listing rules - ASIC exemption and modification
Shares	
- A proportionate interest in the net worth of the business or undertaking of the company. - It confers an interest in the company through a bundle of rights which extends to: - Governance: right to vote at AGM or EGM - Right to receive dividend payments - Generally, to receive the capital proportionate to what was paid and any surplus assets of the company upon winding up	
Share capital is that amount which members agree to contribute permanently to the company in their capacity as members to fund the joint enterprise of activities. - During the life of company share capital may not be returned to its holders, and holders may not be released from obligations they have undertaken. - On a winding up of the company the holders of share capital are the lowest ranked claimants upon the assets of the company. ONLY AFTER creditors of the company have been paid their debts in full are those who have contributed share capital entitled to have it returned to them. - You can have different classes of share where rights to dividends or voting are altered (e.g. preference shares)	

Factors affecting the decision to incorporate

- For a large enterprise the advantage of incorporation is likely to compel registration under the **Corporations Act** however the **case will not be clear-cut for smaller enterprises.**

Advantages	Disadvantages
1. Limited liability - Incorporation provides members/shareholders with limited liability 2. Perpetual succession - A company is an entity distinct from the individuals comprising its members - It can therefore continue to exist even after the death, bankruptcy or so forth of its members such that it can continue to exist, unlike for instance, partnerships.	1. Cost, formality and continuing obligations - Cost, formalities and obligations imposed on incorporated associations far outweighs those on unincorporated associations - Partnerships are <u>flexible in terms of creation, internal structure, withdrawal of capital and dissolving the entity</u> - In contrast the procedure of incorporation involves formalities as does the process of winding up a company - In addition, companies <u>must comply with an array of ongoing obligations</u> and failure to do so attracts penalty
3. Financing Companies have greater access to finance, such as the ability to create a floating charge or raise capital through public issue of shares.	2. Taxation Historically there was a double taxation consequence attached to incorporated however this is <u>no longer an issue due to the dividend imputation provisions introduced in the 1980s</u> which eliminates the double taxation of company dividends.
Changing the type of company	
May be made in accordance with Corporations Act Pt 2B.7	

TYPES OF BUSINESS ASSOCIATION

1. UNINCORPORATED FORMS OF BUSINESS ORGANISATION

Sole Trader

- runs business in their own name as a natural person (maybe 1 or 2 employees)
- The identity of the sole trader in control of the business are merged

The sole trader gets to keep all the profit but also bears all of the liability – if the business goes bust they may lose everything they own

Benefits

- Flexible
- Easily set up (person can set up newspaper stand that says “NEWSPAPERS SOLD HERE”)
- Owner is in control
- Allows owner to keep all profit

Drawbacks

- **Unlimited liability:** sole trader is liable for all debts and liabilities of the business
- Life of the business linked to life of sole trader
- Limited opportunities for tax minimisation –all income received by the business is taxable on a personal income basis
- Sole trader **cannot raise capital on the market**

- **NOTE CORPORATIONS OFTEN PREFERABLE TO BEING A SOLE TRADER:** limited liability and taxation considerations sometimes prompt sole traders to conduct their business through a corporation of which they may be sole shareholder and director

Partnership (General Partnerships & Limited Partnerships)

1) General Partnership

- **Two or more people working together in common** (Usually there is a limit of 20 people except in certain professions which allow more)
- **Not a separate legal entity:** similarly to a sole proprietorship, the identity of the business is intertwined with the partners (usually if a partner dies the partnership is dissolved)
- **Personal liability:** there is personal liability (the partner may risk everything that they own if the partnership is not successful)
- If a court is considering if a business is a partnership, it will **consider its 3 requirements:**

1. People are carrying on a business

- This essentially require **repetition** – people are running the business again and again and again

2. In common:

- **Agency relationship**
- **Fiduciary Duty**

- Requires an **agency relationship** to be made between the partners (e.g. this means any partner can bind all the members of the partnership)
- **Fiduciary duties** are imposed on all of the partners which obliges them to avoid conflicts of interest and try to act in the best interest of the business

3. With a view for profit

- A partnership cannot be created for non-profit

Benefits

- Simple and cheap
- Very flexible
- No disclosure requirements

Drawbacks

- Unlimited liability
- Partner interests are not free transferable
- No separate legal entity
- Limited number of people can be involved
- Continuity problem: death of a partner can mean the end of the partnership
- Capital may be difficult to raise

2) Limited Partnership

- in a general partnership there are the **general partners (that have personal liability)** and the **limited partners** (that have **limited liability**)
- Limited partnerships **require registration as a condition** of the limited liability
- The Limited Partnership must identify itself with **“LP”** in its name

3) Joint Venture

- Agreements by contract to engage in an ad hoc profit project by combining resources, but without binding the other venturers.
 - Examples include exploration for minerals and exploitation of new technologies.

Key Differences with Partnership:	1. No requirement for the venture to be “in common” • JV does not require agency relationship or fiduciary duty 2. JVs share a “product” whereas a partnership shares “profit” (not the profit that comes from a product but the product itself) 3. The liability in a JV is individual rather than joint and several as in a partnership 4. Subject to agreement, the joint venturers are free to dispose of their interest in the JV. This is not the case in a partnership as the change of partners may result in the dissolution of the partnership
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4) Unincorporated Association (Not for Profit, basically clubs)

- a group of people who agree to act together as an organisation and form an association
- Group can remain informal & its members make own rules on how the group is managed
- Not a separate legal entity and can only be used for not-for-profit activities

Wise v Perpetual Trustee Co Ltd (Privy Council)	“...clubs are associations of a peculiar nature. They are societies the members of which are perpetually changing . They are not partnerships ; they are not associations for gain; and the feature which distinguishes them from other societies is that no member as such becomes liable to pay to the funds of the society or anyone else any money beyond the subscriptions required by the rules of the club to be paid so long as he remains a member.”
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Benefits	Drawbacks
• Easy to set up	• Not a separate legal entity • May be a problem with donations – gifts cannot be held in the name of an unincorporated association because these associations have no separate legal existence • May be problems with validity of long term contract • Committee is liable for debt of the association

NOTE: committee members risk being personally liable for the debt of the corporation. When liability starts rising we convert entity to incorporated association

NOTE: for JV or Partnership, business relationship can be forged by any 2 legal entities

2. INCORPORATED FORMS OF BUSINESS ORGANISATION

NOT registered under <i>Corporations Act</i>	1) Cooperative	
	NOTES: can be for profit or not-for-profit	
	- Group of people who pool resources together to achieve a common goal - The features of a cooperative are: - Separate legal entity (limited liability) - Open membership - One vote per member - Commitment to educating members & employees with cooperative principles - Concerns for communities	
	2) Incorporated Association (Not for profit)	
	NOTE: regulated by state legislation	
Companies registered under <i>Corporations Act</i>	3) Proprietary Company	
	- Usually small businesses - Might be subsidiaries of public companies (have “PTY” in their name...)	
	Three requirements for a proprietary company (<i>Corporations Act s 45A(1)</i>):	- Must be limited by shares or be an unlimited liability with share capital - Max 50 non-employee shareholders - Cannot do anything that would require disclosure to investors under Chapter 6D (raising funds) but may offer shares to existing shareholders & employees (CA s 113)
	There are 2 types of liability the company can have:	Liability limited by shares: liability limited to the unpaid amount of shares Unlimited with share capital: liability of the members will be unlimited, and they will be liable for all the debt of the company (Benefit: not bound by “capital maintenance”; company would find it easier to raise debt)
	There are 2 classifications of proprietary company (<i>s 45A Corporations Act</i>):	Small proprietary companies: you need two of three criteria – consolidated gross revenue <\$25m, value of assets <\$12.5m, less than 50 employees Advantage - do not require annual reports (except in certain cases) Large proprietary companies: if $\neq$ satisfy 2 of above criteria (require annual reports)

	KEY FEATURES	• Cannot raise capital on market • Requires 1 director, no secretary • Registered not open to public • May be comprised of one member/shareholder (CA s 114) • No AGM required
	4) Public Company	
	• A public company is anything that is not a private company (Corporations Act s 9) & is subject to greater regulation than a proprietary company in order to protect the public	
	• (if you do not see “PTY” in the name, it is a public company) • (if the company is limited by shares OR guarantee, “LTD” must be in the name – lets creditors know) • (if the company has no liability it needs “NL” in the name)	
	There are 4 types of liability the public companies can have:	1. Liability limited by shares: liability of members limited to unpaid amount of shares 2. Limited by guarantee: liability of members is limited. However, it is different to limited by shares. When members initially join, they do not pay any capital. Instead, members give a guarantee (e.g. the object for the purposes of the guarantee might be a sum of \$\$\$, property or shares). Liability will be limited to the guarantee ○ These are more popular in charities since there is no start-up capital 3. Unlimited with share capital: liability of the members will be unlimited & they will be liable for all the debt of the company ○ Can be used to protect creditors – ensures they can get their capital back 4. No Liability Company: no-one is liable (only available in the mining industry)
	KEY FEATURES	• Ability to raise capital on the market ○ Listed public companies can raise capital on ASX ○ Unlisted public companies can raise capital from private investors • Require a minimum of 3 directors & 1 company secretary (s 204A) • Unlimited number of shareholders • Registered office needs to be open to the public • Annual general meeting is required (otherwise strict liability offence)