

## I REGISTRATION

### A Features of a company

#### 1 Limited liability

- One of the main benefits of operating as a company – means shareholders are not personally liable for the company's debts. Extent of liability depends on the type of company – see s 112 for different company types;
- Reason liability is limited – the company is a separate legal entity;

#### 2 Separate legal entity

- The company is regarded by law as a separate legal entity i.e. a legal (but artificial) person;
  - Company's 'eyes, limbs and brain' are the people who people who perform tasks on the company's behalf;

#### ***Saloman v Saloman & Co Ltd [1897] AC 22***

- 'The company is at law a different person altogether from the subscribers to the memorandum; and, though it may be that after incorporation the business is precisely the same as it was before, and the same persons are managers, and the same hands receive the profit, the company is not in law the agent of the subscribers or the trustee for them.'

- As a SLE, the company can contract in its own right and enforce those contracts:

#### ***Lee v Lee's Air Farming Ltd [1961] AC 12***

- Consequence is that shareholders, even in a one-person company, do **not** have a legal or equitable interest in the company's property, and the company can own property in its own right: ***Macawra v Northern Insurance Co Ltd [1925] AC 619***
  - Hence is theoretically possible for a shareholder in a one-member company to be found guilty of stealing company (another person's) property: ***Macleod v The Queen (2003) 214 CLR 230***

#### 3 Veil of incorporation

- ***Effectively defunct with the passing of the Corporations Act 2001***
- When a company is incorporated and becomes a separate legal entity, a 'veil' descends in front of the company and 'shields' it (its members and officers) from public scrutiny;

- Idea is that the company should be allowed autonomy as long as it is not breaking the law;
- The veil is lifted or pierced if the company abuses its legal personality i.e. if the company is being used for an illegal purpose;
- In effect, the veil is permanently lifted by the *Corporations Act* e.g. s 588G insolvent trading, liability for debts of a trustee company, etc.

### III INTERNAL MANAGEMENT OF THE COMPANY

- A company may be governed by the replaceable rules or a constitution or a combination of both: **s 134**

#### A Replaceable rules

- The replaceable rules apply to:
  - Each company registered after 1 July 1998: **s 135(1)(a)(i)**
  - Any company registered before 1 July 1998 that has repealed or repealed its constitution after that date: **s 135(1)(a)(ii)**
- Note the replaceable rules do **not** apply to a limited proprietary company with a single shareholder who is also the sole director: **s 135(1)**
- A replaceable rule may be displaced or modified by a company constitution: **s 135(2)**
- Failure to comply with the replaceable rules where they apply is not by itself a contravention of the *Corporations Act* **s 135(3)**, although an injunction may be sought by a party on the basis of a breach of the statutory contract in **s 140**: ***Smolarek v Liwszye* [2006] WASCA 50**
- A table of replaceable rules is contained in **s 141**;

#### B Company constitution

- ASIC may direct a company to lodge a consolidated copy of its constitution with ASIC: **s 138**
- A company must send a copy of its constitution to a member within 7 days if the member asks the company in writing for a copy **s 139(1)(a)** and pays any fee required by the company **s 139(1)(b)**

## 1 Adopting of a constitution

- A company adopts a constitution:
  - **On registration** if all persons specified in the application for registration as persons who consent to becoming members agree in writing to the terms of the constitution: **s 136(1)(a)**; or
  - **After registration** if the company passes a **special resolution** or a court order is made under s 233 requiring the adoption of a constitution

### s 9

**special resolution** means:

(a) In relation to a company, **a resolution**:

- i. Of which notice as set out in paragraph s 249L(1)(c) has been given; and
- ii. **That has been passed by at least 75% of votes cast by members entitled to vote on the resolution.**

- A constitution is adopted, if the result of special resolution:
  - On the date on which the resolution is passed if no later date was specified: **s 137(a)(i)** or
  - On a later date specified in the resolution if the date is later than that on which the resolution is passed: **s 137(a)(ii)**
- A public company which adopts or modifies a constitution must lodge a copy of it with ASIC within 14 days: **s 136(5)(a)-(b)**
  - Failure to do so is a strict liability offence: **s 136(6)**

## 2 Modifying a constitution

- A constitution may modify or repeal its constitution or part of its constitution by special resolution: **s 136(2)**
- The constitution may provide that a vote of more than 75% is necessary to modify or repeal the constitution/provision ('entrenching provision'): **s 136(3)**
- The entrenching provision may itself be entrenched: **s 136(4)**
- A constitution is modified or repealed, if the result of special resolution:
  - On the date on which the resolution is passed if no later date was specified: **s 137(a)(i)** or
  - On a later date specified in the resolution if the date is later than that on which the resolution is passed: **s 137(a)(ii)**

### 3 Interpreting a constitution

- Constitutions are regarded as business documents and courts interpret their provisions in a similar way to commercial contracts to give them a 'business-like interpretation';

#### ***Dome Resources NL v Silver* [2008] NSWCA 322**

- A provision in the constitution which conferred power on directors was given as broad an interpretation as reasonably available on language so as not to impose procedural constraints on the directors.
- As such, courts are reluctant to imply further terms or permit evidence of an intention to depart from or add to the written provisions as this increases uncertainty and detracts from the entitlement of shareholders and others to rely on the written constitution as containing the full and complete constitution: ***Lion Nathan Australia Pty Ltd v Coopers Brewery Ltd* [2006] FCAFC 144**

## VI MEETINGS

- Two organs – the board and the general meeting;

- **Board**

- Directors may be executive directors (paid by the company) or non-executive (independent of the company);
- Board may appoint a managing director whose role is to carry out the board's will;

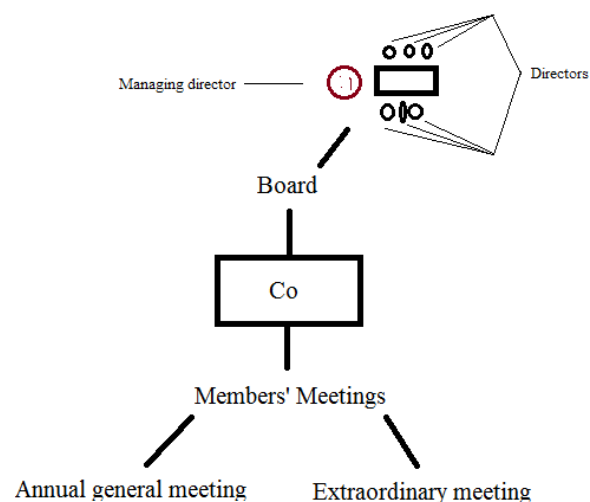


Figure 1: Company organs (sans company secretary)

- **Members' meetings**

- Members' chance to talk directly to the board;
- Note members cannot challenge decisions of the board, merely hope the board will carry out the members' will;
- A meeting outside the annual general meeting is called an *extraordinary meeting*;

## A Directors' meetings

### 1 Introduction

- Directors exercise their power by making decisions and passing resolutions at board meetings;
- The rules governing directors' meetings are set out in the replaceable rules, the constitution or by the board itself;
- Directors may elect a director to chair a meeting: **s 248E(1)**
  - A chair **must be elected where:**
    - A director has not already been elected to chair the meeting: **s 248E(2)(a)** or
    - A previously elected chair is not available or declines to act for the meeting or part of the meeting **s 248E(2)(b)**
- The directors does not have to be physically present at one place – may use any technology consented to by all directors: **s 248D**
  - Consent may be standing;
  - The consent may be withdrawn within a reasonable period before a meeting;
- A board meeting of a company with more than one director requires more than directors meeting together informally to discuss the company's affairs;

#### ***Petsch v Kennedy* [1971] 1 NSWLR 494**

- A discussion between directors will not amount to an effective directors' meeting unless the directors are aware it is a directors' meeting.

#### ***Poliwka v Heven Holdings Pty Ltd* (1992) 6 WAR 505**

- An informal meeting at a cafe of two people who were directors of a company was held not to be a meeting of directors.

### 1 Resolutions

#### *(a) Ordinary resolutions*

- **A resolution must be passed by a majority of votes cast by directors** entitled to vote on the resolution: **s 248G(1)**

- The chair has a casting vote if necessary, in addition to any vote they have in their capacity as a director: **s 248G(2)**

*(b) Circulating resolutions*

- Directors may pass resolutions without a meeting by passing a circulating resolution;
- Resolution is passed if all directors sign a document containing a statement that they are in favour of the resolution set out in the document: **s 249A(2)**
  - Separate copies of the resolution may be used for signing by directors if the wording of the resolution and statement is identical in each copy: **s 249A(3)**
- The circulating resolution is passed when the last member signs: **s 249A(4)**

*B Share capital reduction*

1 Requirements

- A company must not reduce its share capital unless it complies with the requirements in **s 256B(1): s 256D(1)**

**s 256D**

- (1) The company must not make the reduction [of share capital] unless it complies with s 256B(1).
- (2) If the company contravenes s 256D(1):
  - (a) The contravention does not affect the validity of the reduction or of any contract or transaction connected with it; and
  - (b) The company is not guilty of an offence.
- (3) Any person who is involved in a company's contravention of s 256D(1) contravenes this subsection.

**Note s 256D(3) is a civil penalty provision – see s 1317E**

- A company may reduce its share capital under **s 256B(1)** if the reduction:
  1. **Is fair and reasonable to the shareholders as a whole: s 256B(1)(a);** and
  2. **Does not materially prejudice the company's ability to pay its creditors: s 256B(1)(b);** and
  3. **Is approved by the shareholders under s 256C: s 256B(1)(c)**

**s 256B**

- (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.

A cancellation of a share for no consideration is a reduction of share capital, but s 256B(1)(b) does not apply to this kind of reduction.

2 'Fair and reasonable to shareholders': s 256B(1)(a)

- 'Is fair and reasonable to the company's shareholders as a whole': **s 256B(1)(a)**
- Explanatory memorandum identified following factors as relevant considerations:
  - Adequacy of consideration paid to shareholders;
  - Whether the reduction of capital would have the practical effect of depriving shareholders of their rights;
  - Whether the reduction was being used to effect a takeover and avoid takeover provisions;
  - Whether the reduction involved an arrangement that should more properly proceed as a scheme of arrangement;
- What is **fair and reasonable** to shareholders **as a whole does not mean** that the reduction must be **fair and reasonable to each individual** shareholder;

A reduction may be fair and reasonable if it gives shareholders a benefit they would not otherwise have obtained:

***Winper Holdings Ltd v Goldfields Kalgoorlie Ltd* [2001] NSWCA 427**

Facts:

- GKL called a general meeting to approve a selective reduction of capital involving the cancellation of shares held by minority shareholders;
- The cancellation was in consideration of a payment of 55c per share, 8c higher than at what they were independently evaluated;
- Effect of the reduction was to give the majority shareholders 100% of the shares;

- Winper, a minority shareholder, argued the reduction was not 'fair and reasonable' as it gave the majority shareholder a 'special benefit' of a reduction of head office costs;

Ruling:

- Winper's argument rejected;
- The capital reduction was fair and reasonable as it gave both minority and majority shareholders a benefit they would not otherwise have obtained.

***Re Fowlers Vacola Manufacturing Co Ltd [1966] VR 97***

- A reduction of capital involving payment of consideration only to ordinary shareholders was held not fair to the company's preference shareholders;
- Fairness in this case required equal treatment between different classes as the constitution gave preference shareholders priority in return of capital in the case of winding up.

3 Ability to pay creditors: s 256B(1)(b)

- 'Does not materially prejudice the company's ability to pay its creditors': s **256B(1)(b)**
- [No additional information]

4 Shareholder approval: s 256B(1)(c)

- 'Is approved by shareholders under s 256C': s **256B(1)(c)**
- The approval requirements vary depending on whether the reduction is an equal reduction or selective reduction;

**s 256B(2)**

The reduction is either an equal reduction or a selective reduction. The reduction is an **equal reduction** if:

- (a) It relates only to ordinary shares; and
- (b) It applies to each holder of ordinary shares in proportion to the number of ordinary shares they hold; and
- (c) The terms of the reduction are the same for each holder of ordinary shares.

Otherwise, the reduction is a **selective reduction**.

- **Equal reduction:**



- Must be approved by a resolution passed by a general meeting of the company: **s 256C(1)**
- **Selective reduction** either:
  - Special resolution passed at a general meeting with no votes being cast in favour by anyone who would receive consideration as part of the reduction or whose liability to pay amounts unpaid on the shares would be reduced: **s 256C(2)(a)** or
  - A[n ordinary] resolution passed at a general meeting by all ordinary shareholders: **s 256C(2)(b)**
- The shareholder meeting must comply with the usual notice requirements discussed on **page 32** and also include, under **s 256C(4)** :
  - Information about the effect of the reduction on particular shareholders and other shareholders;
  - The interests of the directors in the reduction;
  - The correction of any misapprehensions held by shareholders;

## 5 Failure to comply with the reduction requirements

- A contravention does not affect the validity of the reduction or any connected transaction: **s 256D(2)(a)**
  - **The company is not guilty** of an offence: **s 256(2)(b)**
- **Any person involved in a contravention** by a company breaches the Act and **may be liable** under either:
  - The civil penalty provisions in **s 1317E: s 256D(3)**
  - [If they acted dishonestly] commit an offence: **s 256D(4)**

## B *Criminal liability*

### 1 Organic theory

- When the organs of the company (the board of directors and members in general meeting) act within their powers as conferred by the constitution and replaceable rules, are said as acting as the company itself;

- The acts of the organs of the company are the acts of the company itself, and their state of mind is the state of mind of the company;
- Organic theory (direct liability) can only be applied 'in areas in which the ends of justice has been thought to require the attribution of mental state to corporations':

***Smorgon v Australia and New Zealand Banking Group Ltd (1976) 134 CLR 475***

***Lennard's Asiatic Petroleum Co Ltd [1915] AC 705***

- 'A company is an abstraction. ... Its active and directing will must consequently be sought in the person of somebody who for some purposes may be called an agent, but who is really the directing mind and will of the corporation, the very ego and centre of the personality of the corporation.'

***H L Bolton (Engineering) Co Ltd v T J Graham & Sons Ltd [1957] 1 QB 159***

- 'A company may in many ways be likened to a human being. It has a brain and nerve centre which controls what it does. It also has hands which hold the tools and act in accordance with directors from the centre.'
- 'Some of the people in the company are mere servants ... who are nothing more than hands to do the work ... Others are directors and managers who represent the directing mind and will of the company...'

## 2 Common law liability – Tesco and Meridian

### (a) *Tesco and Meridian – main authorities*

- There are two authorities on who represent 'the directing mind and will' of the company at common law – will depend on the circumstances of the case as to which should be applied;
  - **The board** represents the mind and will of the company:
    - ***Tesco Supermarkets Ltd v Natrass [1972] AC 153***
  - The question of whose act represents the mind and will of the company **depends on the purpose of the [provision of the] legislation:**
    - ***Meridian Global Funds Management Asia Ltd v Securities Commission [1995] 2 AC 500***

***Tesco Supermarkets Ltd v Natrass [1972] AC 153***

- 'But here the board never delegated any part of their functions. They set up a chain of command ... but they remained in control.'

- 'There was no such delegation to the manager of a particular store. He did not function as the directing will of the company ... He was one who was being directed. ... He was a person under the control of the company ... [He was not] within what was called the "brain area" of the company.'

***Meridian Global Funds Management Asia Ltd v Securities Commission* [1995] 2 AC 500**

- '[T]here will be many cases in which ... insistence on the primary rules of attribution would in practice defeat intention. ... [Therefore it is] a matter of interpretation: given that it [the provision/section] was intended to apply to a company, how was it intended to apply? Whose act ... was *for this purpose* intended as an act etc of the company?'

(b) *For Tesco, who else may constitute the 'brain area' of the company?*

- The company secretary may be regarded as an organ of the company and therefore his or her acts may be regarded as the acts of the company *when what he or she does is related to the company's day-to-day administration*: ***Donato v Legion Cabs (Trading) Co-operative Soc Ltd* [1966] 85 WN (Pt 1) (NSW) 242**
- More than one person may be regarded as the company's directing mind and will;

***Brambles Holdings Ltd v Carey* (1976) 15 SASR 270**

- '[I]t is a fallacy to say that any state of mind to be attributed to a corporation must always be the state of mind of a particular office alone and that the corporation can never know or believe more than that one [person] knew or believes.'

- Separate pieces of information held by several people may be aggregated and attributed to the company: ***Brambles Holdings Ltd v Carey* (1976) 15 SASR 270**

