

Legal Entity Question

The legal issue here is whether the customers can lift the corporate veil to make John, Peter and Plasto Australia Pty Ltd liable for the damages caused by Plasto Pty Ltd.

Generally, based on the decision in the case of *Solomon v. Salomon & Co Ltd*, we can state that company is a separate legal entity. Therefore, customers cannot make John, Peter or Plasto Australia Pty Ltd liable for the damages caused by the plasterboard that Plasto Pty Ltd manufactured. However, based on the decision in the case of *Creasey v Breachwood Motors Ltd*, the corporate veil can be lifted when a company is created as a sham to avoid a legal obligation under a contract or statute. The court decided to lift the corporate veil and held that Breachwood Motors Ltd was liable for Welwyn's debt to Creasey when Welwyn had transferred its business and assets to Breachwood Motors Ltd to avoid paying Creasey's claim. Similar to Creasey's case, in this case, Plasto Australia Ltd is created to avoid a legal obligation. The company is created because John and Peter were afraid that their company, Plasto Pty Ltd, could lose the legal actions and they did not have enough money to pay for the damages claim. As a result, all assets of Plasto Pty Ltd and its business were transferred to Plasto Australia Pty Ltd so the company had no money and assets to pay for the customers' claim. Applying the principle in Creasey's case, Plasto Australia Pty Ltd is liable for the damages caused by Plasto Pty Ltd.

The two shareholders and directors, John and Peter, and Plasto Ltd are all separate legal entity so generally they are not liable for the damages caused by the company (*Salomon v. Salomon & Co Ltd*). However, according to s 588M, directors are personally liable for company's debts if they fail to prevent the company from incurring those debts when there are reasonable grounds for suspecting that it is insolvent. In this case, John and Peter transferred all money and other assets of Plasto Pty Ltd to their new company so the company could be insolvent if the customers took legal actions against it. Both John and Peter were aware that Plasto Pty Ltd could be liable for customers' claim and incurred debts but they did not do anything to prevent it, they even left the company with no money and assets to pay its debts. Therefore, the corporate veil is lifted and John and Peter are liable for Plasto's debts under s 588G and s 588M.

In conclusion, Plasto Australia Pty Ltd is liable for the damages caused by Plasto Pty Ltd because it was created as a sham to avoid legal action while John and Peter are liable for that damages because they breached a duty contained in s 588G in the Corporations Act.

S140 contract, 75% special resolution, s203C, s203D

The first issue is whether Osborne Production Pty Ltd can fire Kelly from her position as senior music video producer by changing the constitution.

Usually contracts cannot be altered without the consent of all parties. This is not the case in s140(1) contracts. Based on the decision of *Shuttleworth v Cox Bros & Co (Maidenhead)*, the clause appointing Shuttleworth as a director for life was subject to the statutory power of the companies to modify their constitution. S136(2) provides that a company may modify or repeal its constitution, or a provision of its constitution by special resolution. "Special resolution" can be defined in s9 as a resolution passed by at least 75% of the votes cast by members entitled to vote on the resolution. As long as the procedure is followed correctly, the alteration will bind even those members who vote against the modification. This means that if 75% of the votes representing 75% shares of Osborne were passed, Kelly's dismissal would be effective. However, the fact that Kelly owned 30% shares, or 30% votes equivalently, prevented the company from firing her as a senior music video producer, because the maximum total percentage the company would get without her consent was only 70% - not enough to pass a special resolution. Therefore, Osborne Production Pty Ltd cannot fire Kelly from her position as a senior music video producer.

The question indicated that the company decided to fire Kelly (obviously without the consent of Kelly). Kelly can base on this to argue that the company may have improperly altered the constitution. To solve the issue, Kelly had better vote against the alteration so that the constitution would not be modified without her 30% shares.

The second issue is whether Kelly can enforce the constitution between her and Osborne Production Pty Ltd, which provided that she was to be the senior music video producer for the company.

Corporations Act section 140(1)(a) provides that a company's constitution and any applicable replaceable rules have contractual effect between the company and each member. As a result, the company can take action against its members to force them to comply with provisions in the constitution or applicable replaceable rules where they are unwilling to do so voluntarily, according to *Hickman v Kent or Romney Marsh Sheep-Breeders' Assoc* case. As given in the question, Kelly owned 30% shares of Osborne Production Pty Ltd. This ownership led to Kelly's membership to the company. Therefore, the company's constitution may be a valid contract between Kelly and the company.

However, not all provisions in a company's constitution have contractual effect. Based on the decision from *Hickman v Kent or Romney Marsh Sheep-Breeders' Assoc* case, members

may enforce only those provisions that confer rights on members in their capacity as a member. For example, members can enforce provisions giving them the right to vote at general meetings according to the *Pender v Lushington* case or they may enforce payment of declared dividends as in the *Wood v Odessa Waterworks Co* case.

Another case to analyze is that of *Eley v Positive Government Security Life Assurance Co*. Eley was a member of the company because he received an allotment of shares of the company. The constitution of the company provided that Eley was to be its permanent solicitor and could only be dismissed for misconduct. When the company ceased to employ him, he made a claim against the company for breach of contract but failed. The court held that the constitution conferred no rights on a member who seeks to enforce a right in a capacity other than as a member.

Kelly's situation is quite similar to the case of Eley. Here in our case, the constitution provided that Kelly was to be the senior music video producer for the company. If Kelly argues that the constitution was a contract between her and the company, she is seeking to assert a right in her capacity as senior music video producer of the company. This position is outside her capacity, Kelly as a member is not supposed to be the company's senior music video producer as well. Therefore, the court would reject her argument.

The situation would be different and Kelly could have secured her position as a company's senior music video producer if she has entered into the separate contract independent of the constitution. Then the company would not be able to avoid its contractual obligations by altering the constitution based on the decision of *Allen v Gold Reefs of West Africa Ltd* case. S203C and s203D confirms that even when a company has the power to remove a director, or a senior music video producer as in our case, this does not deprive that officer of any rights to compensation or damages.

In conclusion, Osborne Production Pty Ltd cannot fire Kelly from her position as a senior music video producer because the inadequate percentage for a special resolution. Kelly as a member of the company cannot enforce the provision in the company's constitution that purports to give her the right to be the company's senior music video producer. Therefore, Kelly cannot argue that the constitution is a contract between her and the company. To solve the problem, Kelly should have entered into a separate employment contract, or in a more feasible way, should vote against the alteration of the constitution.