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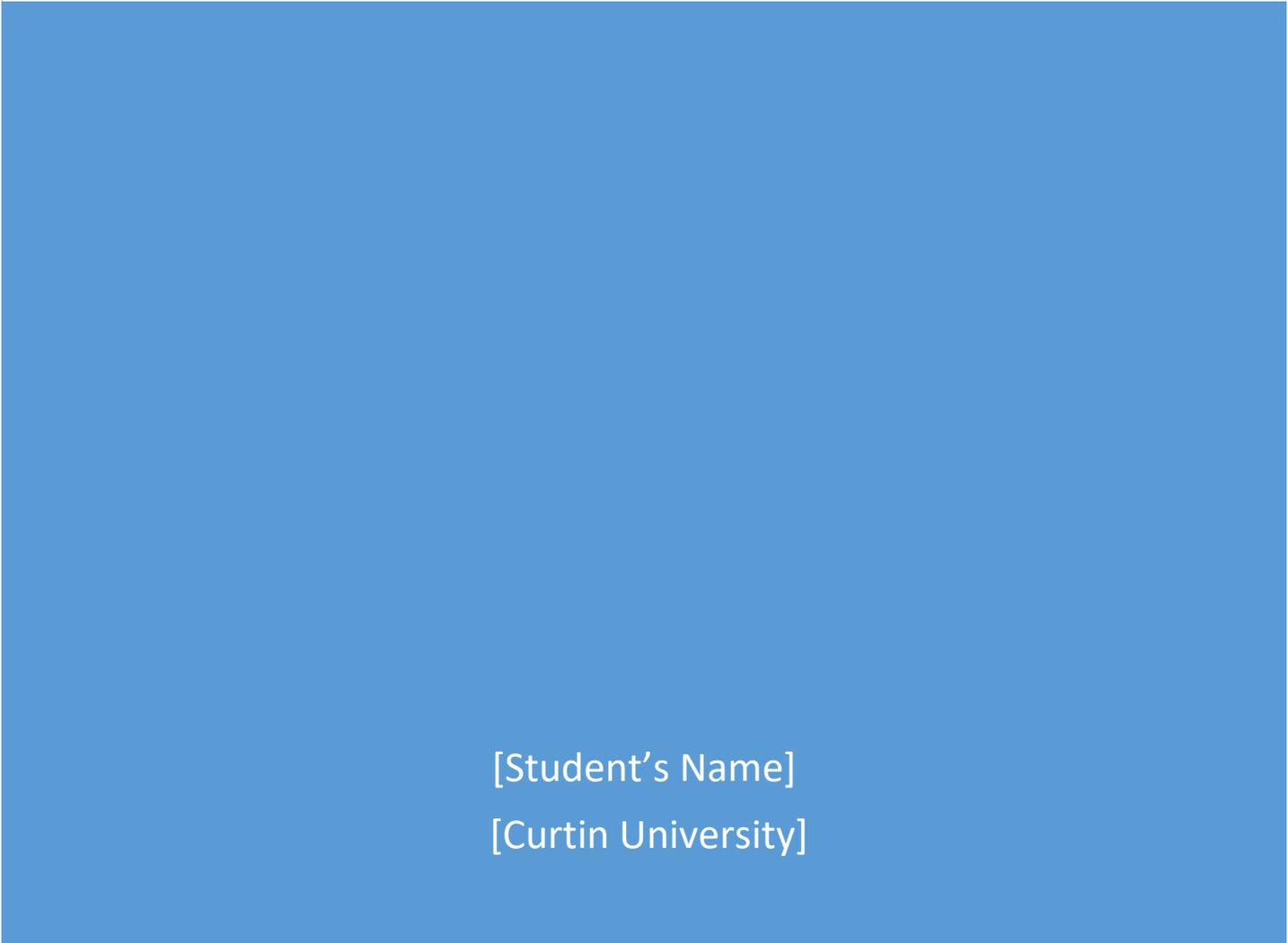
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BLAW 2006 COMPANY LAW ASSIGNMENT



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Answer 1 – Type of Companies

Step 1: Butch needs to register an appropriate type of company to undertake gold mining operations. It is a critical decision in the early promotion stage of a company as small proprietary companies have less financial reporting and regulatory requirements.

Step 2: There are two major types of companies that can be registered under the Australian Corporations Act 2001, proprietary companies and the public companies. These are explained below.

Proprietary Company

A proprietary company is a company which has the following restrictions:

1. Limits the maximum number of its shareholders to 50, not including the persons who are, or were, in the employment of the company.
2. Does not invite the general public to subscribe for its shares, or other equity or debt instruments, which would normally require disclosure to the investors in the form of prospectus, except right issue to the current shareholders or employees of the company.¹

A proprietary company is further divided into small proprietary company and large proprietary company with following restrictions:

	Small Proprietary Company	Large Proprietary Company
Consolidated revenue for the financial year	Less than \$25 million	\$25 million or more
Value of consolidated gross assets	Less than \$12.5 million	\$12.5 million or more
Employees at the end of financial year	Less than 50	50 or more

¹ Corporations Act 2001 (Cth) s 45A.

Public Company

A public company does not have the aforementioned restrictions. As such, a public company can have unlimited number of shareholders, can get listed on ASX and can have unlimited number of employees. A public company has to remain more vigorous and comply with more regulatory and legal requirements compared to a proprietary company.

Step 3: Incorporating a proprietary company would be suitable for meeting Butch's interest as he wants to retain the significant influence and control over the company's operations as its Managing Director. Registering as a public company, Butch may lose control in the event any shareholder acquires significant holding in the Diamond Pty Ltd.

Furthermore, Butch also wants to keep the affairs of the company confidential. A public company has to make public disclosures of certain information beneficial for the knowledge of general public by virtue of several provisions of the Corporations Act 2001. A public company also has to have at least 3 directors,² so Butch cannot stay the sole person entitled to manage the business affairs of the company.

However, being registered as a private company Butch cannot raise capital from the general public and cannot register more than 48 wealthy members of the golf club as shareholder of the new company as it would cross the 49 members limit including himself.

Step 4: To conclude, it is recommended that Butch register the company as a proprietary company and retain more than 50% of the total equity to retain control over its management of affairs. Butch may approach 48 or lesser number of the golf club members to contribute to the share capital of the company and meet the capital deficiency in the \$10 million required in initial exploration phase. Later, being the Managing Director of the company, he may issue further shares to the same shareholders by means of right issue as per section 254D of the Corporations Act 2001.

² Corporations Act 2001 (Cth) s 201A.

Answer 2 – Nature of Legal Relationship between the Parties

Step 1: The nature of relationship between the company and its members, directors and agents is determined by the constitution of the company. So what might be the relationship between the company and Butch and company and Ralph is determined by what is agreed between them and the constitution of the company.

Step 2: According to Section 126 of the Corporations Act 2001, a company may appoint a person to act as its agent and grant him the power to make, modify, ratify or discharge a contract on behalf of the company. Such power is granted to the individual by an express or implied authority of the company and the acts of such power so far as stated in the document authorizing him, shall bind the company without the use of company's common seal.³

The relationship between a company and its member commence upon the adoption of the constitution of the company in which such member agrees in writing to the terms of the constitution before lodging the application for the registration of constitution.⁴

Step 3: In this case, Butch has entered into contracts on behalf of the company as its agent, before the adoption of company's constitution. Hence the nature of relationship between Butch and Diamond Pty Ltd is that of a principal and agent. All the acts done by Butch will continue to bind the company. But so far as the company has not adopted its constitution or not registered under the Act, the relationship may be called into question on the grounds that an agent of a principal that does not exist at the time of making the contract cannot be justified. So the company will have to ratify the contracts entered by Butch after its registration. If the company does not ratify such contract, Butch will be personally liable to pay damages to the aggrieved party.⁵

Ralph being the member of the company after its incorporation would be entitled to a share in profits and right to vote and attend meetings as per the constitution of the company.

Step 4: Hence, it may be said that the relationship between the company and its agent or members is said to be provisional only until it gets fully registered and adopts its constitution.

³ Corporations Act 2001 (Cth) s 126.

⁴ Corporations Act 2001 (Cth) s 136.

⁵ Corporations Act 2001 (Cth) s 131.

After registration all the duties and powers as per the relevant provisions of Corporations Act 2001 shall apply.

Answer 3 – Analysis of the Proposed Rules

Step 1: The issue here is that the Corporations act empowers the members of the company to remove a director from his office before the completion of his term.⁶ The directors of Diamond Pty Ltd are however considering including a clause in the company's constitution that members cannot remove any director from their offices.

Secondly, the directors also intend to create a rule by which members may only appoint a person as director of the company through proxies to general meetings, effectively limiting their powers to cast votes in the election of directors. This rule seems to prejudice the members and the rights given to them by the Corporations Act 2001.

Step 2:

Director Removal Rule

Section 203C and 203 D empowers the members of the company to remove any of its directors and appoint another person to fill the resulting casual vacancy. A public company may remove any director by passing a resolution in general meeting irrespective of any provision in the constitution of the company or agreement between the company and directors or an agreement between the company and its members.⁷ However, removal of director by members of a proprietary company is recognized as one of the many replaceable rules,⁸ meaning that such removal will be subject to any provision in the constitution or an agreement duly accepted by the affected persons.⁹

⁶ Corporations Act 2001 (Cth) s 203C.

⁷ Corporations Act 2001 (Cth) s 203D.

⁸ Corporations Act 2001 (Cth) s 141.

⁹ Corporations Act 2001 (Cth) s 140.

Proxy Rule

The appointment of a proxy on behalf of the member is only valid if it is signed by the member stating the information specified by section 252Y of the Corporations Act 2001.

Step 3: Based on the above provisions, being a proprietary company, Diamond Pty Ltd may include a proposed clause in its constitution limiting the power of its members to remove the directors. However, if it intends to be registered as a public company this proposed rule cannot be enforced as it would then be contrary to the legislation.

A company cannot bound a member to appoint proxies for the purpose of voting at a general meeting in which directors are proposed to be elected. Therefore, the directors of Diamond Pty Ltd cannot enforce this rule as it is contrary to the statute. However, being a proprietary company the directors may frame the constitution to alter the replaceable rule of appointment of director by the company in a general meeting.¹⁰ If so, then only the directors as empowered by section 201H of the Corporations Act 2001 would be entitled to elect new directors. Alternatively the company may also issue shares of a particular class to the members with limited rights, such as no rights to attend the general meeting of members. In this case the shareholder will not have the right to vote in general meetings.

Step 4: Hence, the proposed rule of removal of director can be enforced as effective being a proprietary company, whereas the second rule relating to proxies is invalid and needs to be replaced by an appropriate alternative as mentioned above.

¹⁰ Corporations Act 2001 (Cth) s 201G.

Answer 4 – Enforceability of Contract on Adoption of Proposed Constitution

Step 1: The issue here is the enforceability of the pre-registration contract. A person entering into a contract on behalf of the company that is not registered at the time of making of such contract attracts a liability as an agent of the non-existent principal. If the director or agents of Diamond Pty Ltd enters into contract with Golden Pty Ltd, the question as to whether the company would be bound by the contract is addressed by section 131 of the Corporations Act 2001.

Step 2: Section 131 narrates the provisions for allocating the liability on pre-registration contracts. It applies “if a person enters into, or purports to enter into, a contract on behalf of, or for the benefit of, a company before it is registered”.¹¹ According to the provisions of this section, such contract would be enforceable if the company gets registered and ratifies the contract. If the company does not ratify the contract or does not get registered within the time stipulated by the agents/directors, then the other party would be entitled to claim damages against such agents/directors.¹¹

High Court has held in a decision that when a person purports to enter into a contract as an agent of a non-existent principal, the question of his personal liability on such contract depends on his intention. Directors of the company wouldn't be liable, whereas person acting as “agent of Diamond Pty Ltd” would be personally liable on such contract.¹²

Step 3: In this case, if Diamond Pty Ltd enters into contract for the purchase of gold mine from Golden Pty Ltd before its registration, Golden Pty Ltd could enforce the contract if the company is registered and ratifies such contract. If not, then Golden Pty Ltd would be entitled to receive damages from the officers of Diamond Pty Ltd depending on their presumed intention (as decided by the court), if:

- The company is not registered
- The company is registered but does not ratify the contract, or enter into a substitute for it.¹¹

¹¹ Corporations Act 2001 (Cth) s 131.

¹² Black v Smallwood (1996) 117 CLR 52.

Step 4: To conclude it may be said that the contract would be enforceable against the company if it is registered, and enforceable against the officers of the company if the company does not register or does not ratify the contract.

Answer 5 – Procedure to allow the company to start mining gold

Step 1: Diamond Pty Ltd is engaged in the business to operate a diamond mine. A company cannot go beyond the objects of its constitution and in order to carry out business of mining gold appropriate steps need to be taken by the company.

Step 2: The constitution of the company empowers it to conduct business in accordance with the objects of the company and not go beyond the powers conferred on it by the constitution. A company may, however, modify its constitution by passing a special resolution in a general meeting of members.¹³

Step 3: If Diamond Pty Ltd intends to start mining gold it needs to follow the following steps:

1. Call a general meeting of members by issuing notices.
2. Pass a special resolution constituting not less than three-fourth majority approving the business of mining gold and alteration in the constitution
3. Register the new constitution
4. Lodge with ASIC a copy of special resolution modifying the constitution within 14 days after it is passed, along with a copy of modified constitution.¹³⁶

Step 4: After modifying the constitution the company may start the business of mining gold.

Answer 6 – Liability to the Mining Engineers upon Failure to Comply with the Terms of Contract

Step 1: The question of liability of a person who is an agent of a non-existent principal is raised in this case.

Step 2: In *Black v Smallwood*, High Court held that when a person enters into a contract as an agent of a non-existent principal, the question of his personal liability on such contract depends on his presumed intention. Directors of the company wouldn't be liable, whereas person acting as "agent of Diamond Pty Ltd" would be personally liable on such contract.

¹³ Corporations Act 2001 (Cth) s 136.

In another popular lawsuit, one of the judges Erle CJ held that, “where a contract is signed by one who professes to sign "as agent", but who has no principal existing at the time, and the contract would be altogether inoperative unless binding upon the person who signed it, he is bound thereby.”¹⁴ In another case, *Newborn v Sensolid* the judge held that only by making a person acting ostensible as agent of a non-existent principal, can any effect be given to the contract.¹⁵ Since a company that was not in existence at the time of making the contract cannot be held responsible to enforce the contract, it has been widely accepted that the liability must instead be attached on the human signatories.¹⁶

Step 3: Butch, representing himself as the “agent of Diamond Pty Ltd” presumes the intention of being bound by the acts done in his capacity as an agent of the company. Therefore he would be liable to pay damages to mining engineers if he fails to comply with the contract with them.

On the other hand, Diamond Pty Ltd would not have any liability as it was not registered as a corporate body at the time of entering into contract with the Diamond Pty Ltd.

Step 4: Therefore, Butch needs to make sure that the company gets registered and ratifies the contract if he wishes not to be personally liable to the mining engineers. These provisions of the Corporations Act protect the parties entering into pre-registration contracts with the companies.¹⁷

¹⁴ *Kelner v Bexter* (1866) LR 2 CP 174, 183.

¹⁵ *Newborne v. Sensolid* (1954) 1 Q.B. 45, 47

¹⁶ Law Reform Committee of South Australia, *Reform of Company Law Relating to Pre-Incorporation Contracts*, 1980, 3-6, (Justice Zelling et al).

¹⁷ Roman Tomasic, Stephen Bottomley, and Rob McQueen, *Corporations Law in Australia* (Federation Press, 2nd ed, 2002).

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