TYPE OF OWNERSHIP

Company. This is a body corporate which is a separate legal entity whereby ownership, management and profit taking are all indirect. The company is owned by the shareholders and management is vested in the board of directors. The commercial risk is taken by the company and not the owners.

A company may diversify and become a complex of several different companies, their risks thus isolated from one another.

Sole Trader. This is single person ownership where one investor directly participates in the ownership, management and profits of the business.

Partnership. This is direct participation by two or more entities or persons in the ownership, management and profit of the business.

A Trust. It may be a unit trust, fixed trust or discretionary trust. Ownership and management are vested in a trustee; ownership and profits are written into the trust deed. Details can be advised by your solicitor.

MORE ABOUT COMPANIES BECAUSE THEY ARE THE MOST COMMON

A very high percentage of businesses today are incorporated. There are many advantages to be gained by using a company instead of a partnership or some other structure. In particular a company offers limited liability, an ownership that can be changed by means of transferring shares, tax advantages and so on.

As the vast majority of businesses are operated by companies, it is appropriate here to highlight some of the more important features of companies and their operation.

There are three major parts in a company structure. They are:

- the company itself
- the shareholders
- the directors

The company itself - is a concept which has the legal capacity to enter into contracts and to do nearly all things that any person can do. It can be

known by a name plus a number, or simply by a number with the word "Limited", "Propriety Limited" or "No Liability" following and is responsible for contracts and actions taken in its name.

The shareholders in small companies are usually be the directors as well. In larger companies, whether they are companies whose shares are listed on the stock market or unlisted public companies, or proprietary (private) companies partly or wholly owned by a public company, the majority of shareholders generally will not be the directors.

In a company listed on the Stock Market, the owners will not usually have a relationship with the company, other than through their shareholding. Shareholders who hold a large parcel of shares may have the right to elect a representative to the Board or be appointed one. In some companies, shareholders may be divided into different classes and each class may be given particular representation on the Board as defined in the Articles (Constitution).

Shareholders will generally not be able to interfere with the decisions of the directors about the running of the company on a day-to-day basis. However, the role of the shareholders is important, especially when it comes to reviewing actions of directors, and in assessing how the directors

have behaved in the light of their responsibilities and the law.

The Board of Directors is the group of people appointed to run the company on a day-to-day basis and to supervise or initiate the activities carried on by persons employed by or in the company's name.

Within the Board there are different types of directors - the Chairman of the Board, the Managing Director and other individual directors. These may be employed full time by the company and be responsible for specific management activities within it. They are usually called "Executive Directors". In more substantial companies, they are usually directors appointed to the Board from outside of the company because of their reputation, skill and independence. These are usually called Non-Executive Directors.

Servicing the Board are the principal Executive Officer/Managing Director, in his managerial role, or if there is no Managing Director, or as sometimes occurs, the Chairman if he is the Chief Executive as well, and the Secretary or Secretaries.

Besides these three components, there are many other interests or persons integral to the operation of the company. Without employees,

most companies cannot operate. Creditors will also be important. They may be trade creditors or lenders. They will have a significant influence on the way in which the company operates. There is also the general community and environment in which the company operates and of course customers who are essential to the existence of most companies.

HOW DO YOU FORM A COMPANY?

Persons who wish to form a company, i.e. to bring to life the concept of a non-existent person and to establish the three parts of its structure, must comply with certain basic formal requirements. Under the Corporations Law any five or more persons, if it is to be a public company, or two or more persons in the case of a private company, may form a company by completing and forwarding an application form to any one of a number of providers.

The body with whom such a company must be registered is the Australian Securities and Investment Commission (ASIC). Being the National Companies Authority.

The Memorandum and Articles are a contract between the company and each shareholder, between the company and each officer and between a

member and each other member. Therefore, the provisions of the Memorandum and Articles legally bind the parties. The company comes into existence upon the issue of a Certificate of Incorporation by ASC.

ABOUT THE MEMBERS/ SHAREHOLDERS

Once the company has been formed, the original subscribers/shareholders plus any additional persons taking up shares become the "Membership" of the company. Their liability in the case of collapse of the company is limited to the original face or par value of their shares. If the shares have been issued- partly paid up, the Members will be liable for the difference between what has been paid and its face value.

This principle of limited liability is one of the features of company law. Should the company become insolvent the creditors will, as a result, have no recourse against shareholders. There are a few exceptions to this rule. In certain circumstances the court will look behind the company to see if there are special reasons for making its members liable. This might occur if the shareholders are committing fraud or trying to establish liability by a company for the debts of other companies in a group.

ABOUT THE DIRECTORS

Public companies must have at least three directors. Proprietary companies must appoint at least one director. In addition, companies are required to appoint other officers and a Secretary.

The legislation lays down some guidelines as to how directors are to be elected, but by and large this is left to the Articles of Association of the Company

Directors as Officers

There is no doubt that "Officers" are generally speaking the persons bound by the legislation and "Officer" is defined by the law to include a director, secretary, a receiver and manager, an official manager a liquidator. It does not include a receiver, if not a manager, a receiver and manager appointed by the court or a liquidator appointed by the court.

It is important to understand that the insolvent trading provisions in the legislation catch directors or those who are involved in management.

Definition of Directors and Their Status

A company director is a person who occupies a position of trust. That trust results in a responsibility towards the company. However, there has not been either in the case law or in the Statutes a single satisfactory definition of a company director which can apply to every situation. However, may include:

a) Any person occupying or acting in the position of director of a corporation, by whatever name called and whether or not validly appointed to occupy or duly authorised to act in the position; and

b) Any person in accordance with whose directions or instructions the directors of the corporation are accustomed to act.

Directors of companies have rights that are set down in the Articles of Association. They will vary from company to company. There are, however, important rules which apply across the board:

1. The directors have the right to receive all internal information concerning the company's affairs.

2. Directors have a right to be indemnified by their colleague directors

in respect of obligations under the law. This will arise in cases where a particular director or directors are sued for breaches of duty.

3. If a director has shares in the company he or she has the right to be a shareholder as well.

Duties of Directors/Shareholders

The broad obligations of the directors are that they:

1. Act honestly and in the best interests of the company.

2. Act in good faith on behalf of the company.

3. Must not use their powers for improper purposes.

4. Must not allow their interests to conflict with those of the company.

The particular duties and obligations imposed on directors are as follows:

*To the shareholders

As the shareholders have appointed the directors to direct the affairs of the company of which they are the proprietors, the directors owe a fiduciary duty to them as a group. Not to any particular shareholder or group of shareholders but to the shareholders as a whole, or to put it another way to an "average hypothetical shareholder".

*To the Creditors

The directors must take into account the interests of the creditors of the company. Any failure by the directors to take account of the interests of creditors will have adverse effects for the company as well. The creditor of the company must look to that company for payment. If the company is insolvent or near insolvent or of doubtful solvency or if a contemplated payment or other course of action would jeopardise its solvency, the directors of the company owe a duty to the creditors.

A director is required to exercise a reasonable degree of care and diligence in the exercise of his/her powers and in the discharge of his/her duties

For example: a company carried on the business of advertising to find persons who wished to establish home nurseries to grow plants for sale and ran into financial difficulties. A Deed of Arrangement was signed with

the consent of the directors, under which the company transferred its name and stock to a Mr X, its managing director and founder. In return, he agreed to accept all the company's debts and to carry out its obligations and services due to clients. MR X said he did this to protect his director/son from liability in case the company was liquidated. Receivers and Managers were appointed to the company. A Court held that the directors had failed to act with reasonable care and were in breach of their duty.

Directors cannot make improper use of information, acquired by virtue of their position as directors to gain an advantage for themselves or for any other purpose or which brings about a detriment to the company. Directors are not allowed for example to use special knowledge which they may have gained by reason of their contacts with the company's affiliates to pass on to a relative who is setting up a business in competition with the company.

A director of a company who is in any way directly or indirectly interested in a contract or proposed contract with the company must reveal the fact to the board of the company, as soon as practicable after the director becomes aware of the situation. The director should disclose the interest by revealing the information to the next meeting of directors.

Any director who holds any office or who has any property which might lead to a conflict of duties and interests in respect of the company shall, as soon as possible, declare at a board meeting the nature and extent of the conflict. In relation to the company's accounts, a director has am obligation to ensure that the company maintains proper books of record to enable annual accounts to be prepared, to be submitted at the general meeting and to be lodged with the ASC or its agent.

SOME IMPORTANT SPECIAL SITUATIONS

Signing of Cheques, etc.

The name and registration number of a company must appear in legible characters on various documents issued by the company, including order forms, cheques, business letterheads, etc.

Failure to comply may not only involve criminal penalties but can also make the directors personally liable.

NOTE:

In privately owned companies the proprietors and directors who are usually one and the same quite often with knowledge of these duties, conclude that because they are in total control of the company their breach of any of these duties will not be discovered and therefore the consequences will not arise. Leaving aside the fact that compliance with those duties is necessary in terms of compliance with the law, it should also be remembered that if the company fails and is placed in the hands of a liquidator, the liquidator will then be in control of the company and will, amongst other things, have an obligation to investigate the affairs of the company. This quite often results in prosecution of directors for breaches of duty.