**Question 1:**

**Facts:**

Callie and Marie Seymour, two musically talented sisters, started a private limited music company. Both of the sisters hold 30% each of the share capital in the company. The remaining 40% is held by three fans named Pearl (10%), Marina (10%), and Octavio (20%). Both of the sisters are also directors of the company. As per the Corporations Act 1989,[[1]](#footnote-1) a small proprietary company is the one that has less than 5o employees, a consolidated revenue of less than 25m, and 12.5m in assets.

**Part A:**

The sisters desired to start another company but did not want to invest the share capital themselves. For this reason, they decided to raise the capital from within the company. However, for this purpose, they had to alter the constitution of the company. Under the provisions provided in the Act, a company’s internal affairs are managed either by Replaceable Rules[[2]](#footnote-2) by default or its constitution, which comprises of Articles and Memorandum of Association, or both.[[3]](#footnote-3) Primarily, the Replaceable Rules of a company can be modified or altered through the constitution.[[4]](#footnote-4) It indicates that the constitution of a company can alter or change all or some of the Replaceable Rules.

Therefore, the sisters called for a Special General Meeting. As per the Corporations Act 1989,[[5]](#footnote-5) the notice must be served 21 days prior to the meeting, and the notice must set out the time and venue of the meeting, general agenda of the meeting, and the fact that if a member is entitled to a proxy.[[6]](#footnote-6) The meeting was attended by all five of the shareholders, i.e., the quorum was met.[[7]](#footnote-7) In the meeting, it was put forward that the shareholders holding less than 15% share capital will be required to repay the initial amount of their shares as additional capital each year. Callie, Marie, and Octavio voted for the alteration, that makes it more than 75% of the votes.

Under the Act,[[8]](#footnote-8) a company’s constitution can be altered by a special resolution of members. The Act[[9]](#footnote-9) further explains that a special resolution takes effect if 75% of the votes are cast by the members entitled to voting. Since all of the five shareholders of the company are allowed to vote, and one share equals one vote. Thus, Callie, Marie and Octavio collectively cast 80% of the total votes. Therefore, the constitutional alteration was passed. Furthermore, alteration made meeting all of the criteria is applicable on all members of the meeting despite the fact that if they opposed the special resolution.[[10]](#footnote-10)

Hence, under this condition, this would be concluded that Pearl and Marina would have to repay the initial price of their shares each year. The only option left with them is to sell their shares and free their capital from the company. However, they chose to maintain their shareholding at the company as they continued to be loyal fans of the musically talented sisters. However, the situation is different. The decision taken in the Special Resolution Meeting cannot be enforced against them because under the Corporations Act, no member can be enforced to pay money to the company or increase his number of shares.[[11]](#footnote-11) Therefore, the first alteration of constitution, i.e., Pearl and Marina must repay their initial amount of shares to the company, is not valid, and cannot be enforced against them.

**Part B:**

The copyright of the songs, imagery, and branding of Callie and Marie Seymour is owned by another company named Ink Records Ltd. The sisters had been using this material to promote their own company. For this reason, Ink Records Ltd demanded the sisters’ company for license to use this material. They came to the terms that the company will allow the sisters to promote their store using this material only if they maintain 80% of shareholding (either individually or collectively) in their company. Furthermore, the agreement was to take effect after 10 days.

Due to the short period, Callie and Marie called Octavio to their store for a Special General Meeting. Since they called the meeting on an urgent basis, they did not serve notice of meeting to the remaining shareholders, i.e., Pearl and Marina. They also did not complete the notice period in this regard. As explained earlier, the notice must be served 21 days prior to the meeting.[[12]](#footnote-12) Therefore, there exists an irregularity in the process of the meeting. Moreover, the remaining shareholders were not even informed of the meeting. Thus, they did not know that such a meeting was being held. They

Under the Corporations Act, the parties can apply for breach of contract for non-compliance of the company with the terms and conditions provided in its constitution.[[13]](#footnote-13) However, the appropriate remedy of such a situation is not damages but a court injunction or declaration, which enforces compliance with the Replaceable Rules or the constitution of a company. Also, the members can sue the company to enforce their rights. But, these rights can only be enforced in the capacity in which they are provided to them, and they cannot be enforced in a capacity outside of it. For instance, a member cannot enjoy the rights that a solicitor or a promoter of the company unless he acts like one.

As an example, in a 1875 case of outside capacity,[[14]](#footnote-14) the constitution of the company was drafted by Eley, and he was the permanent solicitor of the company that could not be removed on the grounds of misconduct. However, no separate contract for the same was ever made between the company and Eley. Later, he received some shares within the company for the work he did for its formation. Subsequently, the company ceased to have him as its permanent solicitor. As a reaction, Eley sued the company for breach of contract. His action was failed on the ground that the constitution of the company did not confer any rights for a member where he seeks to enforce a right in a capacity outside of a member.

Continuing with the discussion, the remedy for the breach is not damages but injunction of court. Although the decision made in the Special Resolution Meeting is binding on all the members despite the fact that they voted against the decision but under the Corporations Act, a member is not bound by the modification in the company’s constitution if it supports entrenching provisions. Under the Act,[[15]](#footnote-15) if the decision of a Special Resolution Meeting imposes or increases a particular member’s ability to transfer the shares already held by him, the member is not bound by such a decision. Moreover, such modifications that are particularly prejudiced towards some of the shareholders of a company are also not binding upon them.[[16]](#footnote-16)

Therefore, in the case of Pearl and Marina, with regard to the second modification, a large number of factors are playing their role. Firstly, the directors of the company, i.e., Callie and Marie did not meet the requirement of sending the notice of the meeting to all members of the board. Secondly, the quorum of the meeting is not met, i.e., Pearl and Marina did not come to the meeting, and the member attending it did not meet the 2/3 requirement of quorum. Lastly, the decision taken is highly prejudiced towards Pearl and Marina. Thus, the second alteration to the constitution for expropriation of their shares is not valid.

**Question 2:**

**Facts:**

Kenta and Ryota are two identical twins. They are executive managing directors of a company named Genki Ltd, which is a public company that deals in selling high-tech medical equipment and machines to hospitals. Although the brothers are identical in physical appearance, Ryota is not much fluent in English due to his long-term stay in Japan whereas Kenta has great fluency in speaking the language due to staying in Australia.

**Part A:**

Ryota, due to his lack of good fluency of English language, landed the company in to a big trouble when he signed a contract without fully understanding it. After this incident, the company made it mandatory for Ryota to get any contract more than the value of $10,000 AUS by one of the directors first. He was not happy with this development. Kenta realized the situation, and sent Ryota to West Bank to apply for a loan of $50,000 AUD for the company. Ryota also called the bank beforehand.

Ryota reached the bank, signed the loan agreement for a total of $500,000, and forged his brother Kenta’s signature on the contract to meet the requirement of having two directors’ signatures on any contract of value more than $10,000 AUD. He did not stop here, and get the loan issued in the name of unrelated company, which happened to be a proprietary shelf company made by the twin brothers and had never been used ever since. Ryota told the bank that it was the wholly owned subsidiary of the company he is the managing director of.

In a recent 2016 case,[[17]](#footnote-17) the defendant (the company) entered into two loan agreements with the plaintiff (the bank), who relied on the existing personal guarantees from two of the directors of the company. The agreements were signed in 2004 and 2009. One of the directors refused to be held liable for the loan payment because the signatures on the loan agreement of 2009 did not belong to him. The bank did not argue but relied on the Corporations Act[[18]](#footnote-18) to enforce the guarantee.

This case identifies the point that if an agreement has correctly been executed, the people dealing with the company can assume that the director has properly been appointed, and had complete authority to act in this regard. However, the people dealing with the company are not entitled to make these assumptions if they get suspicious of a wrongdoing at the time of the formation of a contract. In the scenario under discussion, the clerk of the bank became suspicious of the fact that the identical twins were the directors of the subsidiary company, and owned 50% of the share capital each. Moreover, none of the brother ever mentioned the company. However, based on the position of Ryota in the present company, he allowed the loan agreement to go into the process. Also, he never suspected that Kenta did not sign the agreement. Therefore, Genki Ltd is bound by the loan agreement with West Bank.

**Part B:**

 A subsidiary company is controlled and ran by another company. A subsidiary runs the day-to-day affairs of the organization and may incur the parent company into a liability. Under the Corporations Act 2001,[[19]](#footnote-19) a company is considered a subsidiary of another company primarily when the other company controls the composition of the board of directors, have more than 50% of the votes, and hold more than 50% of the issued share capital. In Australia, a parent company is seen as the shadow director of the subsidiary company. Thereby, it attracts liability in this regard.

 The facts of the scenario under discussion make it clear that the so-called subsidiary company is a proprietary shelf company. It was formed in the early days of the twin brothers’ career when they began doing their own business. However, the company was never used. Both of the twin brothers are listed as the directors of the company, and each of them shares 50% of the share capital in it. Apart from this situation, the company has no direct links with Genki Ltd except for one, i.e., both Kenta and Ryota are the executive managing directors of Genki Ltd. Therefore, it can be argued that Business Brother Pty Ltd is a subsidiary company. However, in reality, it does not involve in any of the day-to-day activities of Genki Ltd.

 In a recent Canadian case of 2013,[[20]](#footnote-20) it was decided that under certain circumstance, the subsidiary company will not hold the parent company responsible for its liabilities, and the corporate veil will be pierced. One of the situations is when the parent company completely dominate or control the subsidiary company and uses it as shield for fraudulent or improper conduct. Therefore, even if the company named Business Brothers Pty Ltd is taken as a subsidiary of Genki Ltd., the latter must not be held responsible for its actions.

 Moreover, under the Act,[[21]](#footnote-21) a holding company becomes liable for the liability incurred by the subsidiary company when it is the parent company at the time of incurring a debt, is insolvent at that time or have reasonable grounds to suspect so, and one or more of the directors of the holding company is aware of the debt. In a 2016 case,[[22]](#footnote-22) Mr. and Mrs. Perrine were also the shareholders and directors of Perrine Pty Ltd, which held 39 out of 49.5 million issued shares in Perrinepod Pty Ltd. The company was declared insolvent in 2012. Perrine Pty Ltd was blamed for not foreseeing the upcoming insolvency of its subsidiary. The court held that Perrine Pty Ltd had no clue about the insolvency.

 From this discussion, it is clear that Business Brothers is a subsidiary of Genki Ltd because two of the executive managing directors of the latter had 50% each share capital in the prior company. They were also listed as the directors of the company however, the company does not run any day-to-day activities of Genki Ltd. Therefore, it can be concluded that Business Brother Pty Ltd is a subsidiary company of Genki Ltd. Also, it is worth mentioning here that a subsidiary is a separate legal entity that does not make the parent company liable or responsible for its debts. It is the basic rule. However, under certain particular conditions, this corporate veil is pierced, and the directors are held responsible for the liability incurred by the subsidiary company of the holding company.

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2. Section 141 [↑](#footnote-ref-2)
3. Section 134 [↑](#footnote-ref-3)
4. Section 135(2) [↑](#footnote-ref-4)
5. Section 249HA(1) and (3) [↑](#footnote-ref-5)
6. Section 249L (a)(b)(c) and (d) [↑](#footnote-ref-6)
7. Section 249T [↑](#footnote-ref-7)
8. Section 136(2) [↑](#footnote-ref-8)
9. Section 136(1)(b) [↑](#footnote-ref-9)
10. NRMA Ltd v Snodgrass (2001) 37 ASCR 382 [↑](#footnote-ref-10)
11. Section 140(2) [↑](#footnote-ref-11)
12. Section 249HA(1) and (3) [↑](#footnote-ref-12)
13. Section 141(1)(a) [↑](#footnote-ref-13)
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