# CHAPTER 1

# THE CORPORATION: INTRODUCTION AND OVERVIEW



## Chapter synopsis and links to Workbook Chapter 1

This Textbook Chapter deals with five topics:

1.1 Studying corporate law

1.2 The corporation: an overview

1.3 A brief history of companies

1.4 Constitutional foundations of Australian corporate law

1.5 The context and culture of the corporation.

Each of these topics is constructively aligned with, and linked to, the same topics in Chapter 1 of the Workbook.

## Outcomes

By the end of this Chapter, you should be able to:

- understand the role of the corporation as a key component of the modern market economy
- appreciate some of the key common features of corporations as globally relevant and commonly chosen business entities
- re-familiarise yourself with foundation issues of case law analysis and statutory interpretation, and other aspects of basic legal learning
- analyse the basic history of the corporation internationally and in Australia
- appreciate the link between the Australian Constitution and the corporate law arrangement between the six states, the two territories, and the Commonwealth.

## Key knowledge

In this Chapter, you will learn about:

- the basic concept of the corporation
- the key milestones involved in the history of companies and of company law
- the main sources of company law
- the requisite skills for studying corporate law.

## Key legal study skills

By the end of this Chapter, you should be able to:

- locate the Company Law unit within the broader suite of Priestley 11 (or core) units and understand its relationship to other units in the LLB and JD (including the Priestley 11 units and elective units)
- appreciate the main historical markers of companies and of company law
- demonstrate familiarity with the main sources of company law
- gain an overview of, and introduction to, the study of contemporary corporate law, including primary and secondary sources of law.

## Linkages to prior learning and other topics

This Chapter provides the foundation context to the study of corporate law.

- Chapter 2 looks at the other types of business entities as compared with companies, and provides an overview of not-for-profit entities.
- Company Law is a Priestley 11 compulsory subject in both the LLB and JD degrees, and is necessary for admission as a legal practitioner.
- Company Law is relevant to many other areas of law and practice, including family law (where, for instance, asset division will be critical), taxation and financial planning, superannuation and employment. This is because the company is a common vehicle for doing business.
- A company can be a one-person business with one shareholder and one director; that is, one person may assume several roles.
- Companies range in size, so they can also be large, public corporations with many shareholders.
- Understanding the various reasons for the popularity of the company as a business vehicle is a pervasive part of this unit of study.

## List of relevant legislation

- *Australian Securities and Investments Commission Act 2001* (Cth)
- *Corporations Act 2001* (Cth)

## Key terminology

**Business**—the means or manner of conducting commerce—buying, selling and leasing goods and services—including via a corporation

**Business entity**—a broad and somewhat generic term that includes business structures, organisations or 'vehicles'; these, in turn, include corporations, partnerships and so forth

**CA2001**—see ***Corporations Act 2001* (Cth)**

**Company**—effectively the same as a **corporation**, and the terms are co-extensive; an incorporated business entity; a separate legal entity registered with ASIC (Australian Securities and Investments Commission)

**Company law**—effectively the same as **corporations law**; collectively, the statute, case law and suite of rules, principles and guidance making up the broad-based project of Australian corporate law; the body of law relevant to companies; includes the CA2001, as well as general law

**Corporate culture**—see **culture**; the CA2001 makes no reference to the term 'corporate culture'; the term is, however, found in the criminal commercial context, and the *Criminal Code Act 1995* (Cth) s 12.3(6) defines it as follows: 'an attitude, policy, rule, course of conduct or practice existing within the body corporate generally or in the part of the body corporate in which the relevant activities [take] place'

**Corporate social responsibility**—see **CSR**

**Corporation**—effectively the same as a **company**, and the terms are essentially co-extensive; however, the CA2001 s 57A(1)(a) provides that '[s]ubject to this section, in this Act, ***corporation*** includes: (a) a company …', so for the purposes of the CA2001, 'corporation' is the broader of the two terms

***Corporations Act 2001* (Cth)**—the main statute dealing with the registration, regulation, and oversight of Australian companies; often referred to in the Textbook and Workbook as 'CA2001'

**Corporations law**—effectively the same as **company law**

**CSR**—corporate social responsibility; in simple terms, a theory which recognises that companies have a degree of discretion that extends beyond providing returns to shareholders/owners, and they may view other factors and influences—such as the

society, the environment and sustainability—as being just as important to the work and role of the contemporary corporation

**Culture**—a challenging and difficult concept,[1] and one that the internationally renowned sociologist Raymond Williams grappled long and hard to pin down when he wrote comprehensively about key words that are critical to understanding post-Second World War society; in his seminal work *Keywords: A Vocabulary of Culture and Society*,[2] Williams devoted no fewer than seven pages to seeking to define the term 'culture'; he noted at the outset of his overview that: 'Culture is one of the two or three most complicated words in the English language. This is so partly because of its intricate historical development, in several European languages, but mainly because it has now come to be used for important concepts in several distinct intellectual disciplines and in several distinct and incompatible systems of thought'

**General law**—defined in CA2001 s 9 to include common law and equity case law

**Profit maximisation**—a theory that promotes the interests of shareholders, and links company profits to the payment of dividends to shareholders

**Shareholders**—the owners and members of a company

**Stakeholders**—parties (both internal and external to the company) with a stake or interest in the company's performance; stakeholders can include a wide array of parties including employees, customers and the like



## 1.1 STUDYING CORPORATE LAW

Studying corporate law involves the usual suite of legal skills—close reading, careful writing, detailed legal analysis, and client (or audience) advising—whether it is an exam or involves a practice-based scenario. These are also, usefully, generic professional services skills relevant to business, accounting, the private sector, not-for-profits and the public sector.

The usual sources of law are also directly relevant to corporations law. These are legal principles discerned from the case law, and process, courses of action and a great amount of detail provided by the relevant statutes; in particular the *Corporations Act 2001* (Cth) (CA2001). As such, statutory interpretation is a critical skill in the armoury of the commercial and corporate lawyer. A modern feature of Australian law in general has been the rise and rise of statute. This is also the case in terms of corporate law. Since the enacting of the CA2001, corporate law has reflected the practical need for proficiency in terms of statutory interpretation and analysis. Law schools play a part in this ongoing process of legal education, and corporate law is a good example of the need for a mindset of curiosity and life-long learning, given the centrality of the legislative provisions.

As such, the study of the modern-day corporation is also co-extensively a study of key provisions in the CA2001.

1 See e.g. Raymond Williams, *Culture*, Fontana New Sociology Series, Collins, 1981.

2 Raymond Williams, *Keywords: A Vocabulary of Culture and Society*, Fontana New Sociology Series, Routledge, 2011 (first published 1976).

## Concepts: the study of company law

The study of company law involves three distinct phases—its location and scope, analysis of the key principles and provisions, and application of the relevant law to the particular context.

Each of these requires the development of legal skills. We can think of these in terms of legal study skills and legal practice skills, which sit on a continuum and can overlap. In broad terms, they can be seen as comprising:

- fundamental or foundation skills
- intermediate level skills, and
- advanced and applied skills.

Given that *Corporations Law: Concepts, Cases and Culture* is designed as a student text for the LLB/JD Company Law unit, the focus is on foundation skills and, in particular, legal reading and legal writing.

## Concepts: defining and locating company law

Modern Australian company law can be approached from several angles. It can be located in large part in the main legislation, the CA2001. This legislation, however, is more of a manual than a contextual overview. Hence, a textbook is very useful in this area of the law for providing background, context, historical perspective and contemporary perspectives. This helps to makes sense of the company as a crucial part of the modern economy.

Legislation and case law provide the 'hard law' upon which company law is based. Textbooks and journal articles can provide background and context in general, and also research depth.

The CA2001 dominates the corporate lawyer's day-to-day practice. Reading it, making sense of it, and giving advice on the basis of the lawyer's analysis is the key ingredient of much legal practice in this area.

## Content: the unit Company Law

The content of a typical Company Law unit covers the following aspects of the corporation:

- the history and business context of the corporation
- the architecture and structure of the corporation—including the roles by which people act on its behalf
- the practicalities of, and the transactions undertaken by, the typical small corporation
- the litigious aspects of the corporation's activities—its ability to issue legal proceedings and to be sued
- the theory of corporations law
- critiques of corporate law and theory
- the context in which corporations operate.

The study of each of these content elements relies on the two primary sources of law: statute and case law. In the modern era, statute is the first point of reference. It is clarified by the case law.

## Content: *Corporations Act 2001* (Cth)

The CA2001 uses the term 'general law' to encompass common law and equitable principles. This is in line with the fact that modern courts hear cases involving legal principles that are informed historically by the principles of both common law and equity.

The term 'general law' is defined in the Dictionary of the CA2001.

### CORPORATIONS ACT 2001 (CTH) s 9

#### Dictionary

Unless the contrary intention appears:

…

***'general law'*** means the principles and rules of the common law and equity.

An example of where the term 'general law' is used in the CA2001 is in s 179(1):

### CORPORATIONS ACT 2001 (CTH) s 179(1)

#### Background to duties of directors, other officers and employees

(1) This Part sets out some of the most significant duties of directors, secretaries, other officers and employees of corporations. Other duties are imposed by other provisions of this Act and other laws (including the general law).

## Case law: the *ratio decidendi* and the development of legal principles

Case law, or common law, lies at the historical heart of the development of legal principles generally, and corporations law in particular. It involves the slow, gradual growth of legal principles via judge-made law. It relies on precedent and the identification of the *ratio decidendi* (reason for the decision). That said or written 'by the way', or in addition to matters pertaining to the *ratio decidendi*, is *obiter dictum*. As such, an *obiter dictum* is of a different character to the *ratio decidendi*; it is useful and informative to successive courts, but in terms of the relevant legal principles, it is not binding.

There are many cases that make up the fabric of the common law in the case of corporations law.

## Case law: key cases

Given the very large number of cases stretching back two centuries, *Corporations Law: Concepts, Cases and Culture* takes the deliberate approach of focusing on key or important cases. Such cases provide the current basis of principles and remain important in interpreting and adding detail and texture to the legislation. Every key case is provided with consistent treatment in this book, and there are five distinct parts to the coverage of each:

- case name and citation
- court
- facts
- issue
- decision.

In some instances, a judgment extract and/or a comment on the case is also included.

These key cases are typically from the most senior—or apex—courts within their jurisdictions, including the High Court in Australia, and the House of Lords (now the Supreme Court) in the UK. The cases

typically clarify key principles, and crystallise developments that have come before them in what may prove to be preliminary or lead-up cases. Alternatively, the cases may involve novel points of the law and landmark decisions that constitute part of the 'general law'.

Of course, there are many other cases, and some of these will be mentioned; but the focus of this book is on the key cases and the key principles relevant to such cases.

## Case law: apex courts and the principles of *stare decisis*

In broad terms, there are two formal ways by which the law will change:

- by new legislation enacted by parliament, or
- by an apex, appellate or senior court with capacity to overrule a previous decision of its own (or, naturally, of another court). For example, within the Australian context, the High Court of Australia possesses this inherent ability. It is why the High Court is referred to as the 'guardian' or overseer of the Australian common law. This ability of an apex court to essentially change its mind on a previous decision of its own making is referred to as *stare decisis*.

While *stare decisis* exists in theory, its exercise in practice will generally be proscribed.[3] That containment goes to a balancing or calibration of two competing issues, namely:

- the issue of the 'certainty' and predictability of the law (its 'fabric'), and
- the common law's due development as adjudged by a relevant apex court (including the ability to deliver justice according to the law).

## Context and culture

It is axiomatic to assert that studying law is a matter of understanding the wider operating context (including economic, cultural, social and even political dimensions) as well as the current legal rules and principles themselves. Law is symbiotically connected to the society it serves, regulates and informs. By its nature, law changes and responds to societal changes. This is also the case in the context of corporations law, just as it is in torts law, or family law.

While the content provides the theory and principles of corporations as a vehicle for business, the wider context may include the critique of how companies may be able to 'improve', and to be more aware of wider social and environmental issues. This raises the issue of corporate social responsibility, known by the familiar acronym, CSR.

CSR represents a way of positioning and examining the role and work of the corporation in a wider setting. We look at this further in Section 1.5 below.

**LINK TO WB ACTIVITY**

Refer to Table 1.1 in the Workbook to identify where your particular interests lie.

# 1.2 THE CORPORATION: AN OVERVIEW

The corporation is a flexible, adaptable and, thereby, useful invention of commerce and the law. It has been around for a long time, as far back as the Roman Empire, which commenced in the year 27BCE and continued to the mid-1400s. The company has therefore been long associated with human creativity, ingenuity for money making, and for risk sharing and mitigation. We look at the history of companies in Section 1.3 below.

3 See e.g. DC Pearce and RS Geddes, *Statutory Interpretation in Australia*, 7th ed, LexisNexis, 2011.

The modern corporation is a global phenomenon. That is, it is used as a business vehicle all over the world, subject to the laws of the land in which it operates, or the laws of international contract that govern particular transactions.

By the term 'modern corporations', we mean companies from the past 120 years or so. This period includes two significant events:

- confirmation of the separate legal status of the company in the UK House of Lords case of *Salomon v A Salomon & Co Ltd* [1897] AC 22, and
- the advent of the Australian Constitution in 1901.

Corporations are very common across the world, especially in legally advanced and highly regulated economies such as Australia, the UK, New Zealand and the USA. Corporations have been studied at both national and international level. At an international level, five particular characteristics have been found to be present across many jurisdictions adopting corporate laws. These five markers of a corporation[4] are:

- *Legal personality:* the corporation is a legal entity in its own right with powers equivalent to those of an adult person. As such, the company has the power to enter contracts, to be bound by promises, and to assume liability. This breadth of legal autonomy gives the company the ability to grow as a business entity. The corporation is a legal construct (and a 'creature of statute') or vehicle, which acts through and by its directors—hence the point that follows.
- *Delegated management under a board structure:* as noted above, the company as an artificial legal entity needs to be activated by people. Key to this is the board of directors. The board has responsibility for the legal and ethical acts of the company. A company may have just one director.
- *Limited liability:* a key reason for the popularity of the company as a business entity is that ownership of the company, which rests with the shareholders, involves limited liability on their individual part. That is, if a shareholder owns one $1 share and it is fully paid, the shareholder has no further liability to the company in their capacity as a shareholder. Ownership, coupled with limited liability, is an attractive investment option for the would-be investor.
- *Transferable shares:* the shares held by the owner/member/shareholder are transferable. This is a quick and simple process if the shares are publicly tradable on the stock exchange. It may be slower and more cumbersome to find a buyer and agree a price in a small Pty Ltd company, but the point remains—it is a theoretical possibility and a practical feature common to virtually all companies that the shares can be transferred.
- *Investor ownership:* this is a device for increasing the number of owners, spreading risk, and raising a particular form of investment capital—in this case, share capital. In a large public company, many shareholders may want to invest. This gives a great many people access to membership. It also means the company, as a business vehicle, has the advantage of raising two types of capital—from shareholders, and from lenders; share capital and loan capital respectively.

  We re-examine these concepts in Chapter 2.

## Concepts

Companies are each and all of the following things:

- Vehicles or entities by which people run businesses: that is, they are set up for the purpose of conducting a business, and they range in size and scale.
- Small private firms involving just one or two people: a corporation can involve just one person—who will be its only shareholder, its only director, and its only employee.

4 Reinier R Kraakman, Paul Davies, Henry Hansmann, Gerard Hertig, Klaus J Hopt, Hideki Kanda and Edward B Rock, *The Anatomy of Corporate Law: A Comparative and Functional Approach*, OUP, 2005.

- Publicly listed large businesses: in Australia, the largest corporations usually are public in nature; that is, their shares can be traded on the S&P/ASX 200 index. This refers to the 200 largest listed corporations. Many corporations are not listed and choose to be private.
- Multinational firms: these may be covered by Australian law if their head offices are in Australia, or they have branch offices in Australia.
- Separate legal entities that are able to sue and be sued in contract, and tort: a company can enter into contracts just as an adult person can.
- Bundles of contracts: companies are comprised of many contracts. The company may have contracts with suppliers, employees, and others.
- Creations, or creatures, of statute: companies exist by and large because of the legislation which creates, controls and oversees many of the things they can, and cannot do. As noted, the main legislation is the CA2001.
- Complex entities operating in a broad and changing context: this context includes economic, social, political and environment settings. Companies have competitors, and they answer to regulators. They have owners (the shareholders), they may have many employees, and they have customers.

Units on Company Law may cover the following basic areas. These include the following.

## The structure and architecture of companies

This area includes the company as an entity in its own right; the company as a shell through which others must act; protections, and for whom; the different types of companies; the registration process; documents (such as a constitution and/or replaceable rules); and tax payable.

## Stakeholders—the legal actors involved with companies

Stakeholders include:

- the promoters who establish the firm, and who may—on the assumption that the company will come into being—contract in anticipation of it doing so
- the owners—the shareholders or members
- the directors—the entrusted insiders; different types of directors
- the managers and employees (who are contractually bound to the company), and the officers of the company
- the creditors, or lenders of risk capital (and note the relevance of the *Personal Property Securities Act 2009* (Cth))
- the emerging stakeholders, such as the community and the environment.

## Contracts, transactions and deals—companies doing business

This area includes:

- contracts (including the idea of a company as a bundle of contracts)
- assets of the company; in particular, the share capital, and its maintenance or protection
- suppliers providing goods and services
- buying and selling equipment, inventory and stock-in-trade etc
- borrowing capital from third parties and the provision of security.

## Regulation—the law and regulation overseeing companies

Australia has a complex federal system of government and a correspondingly complex system of regulation. The regulators and regulations relevant to corporations include:

- ASIC: Australian Securities and Investments Commission
- APRA: Australian Prudential Regulation Authority
- ACCC: Australian Competition and Consumer Commission
- ASX (Australian Stock Exchange) Listing Rules
- Takeovers Panel
- ASX Corporate Governance Principles.

The regulation of Australian corporate law is considered in Chapter 6.

## Formal reviews

Formal reviews are quite often carried out by government and by various regulators:

- An example of a review by a regulator is the review of the Commonwealth Bank of Australia by APRA in 2017–18.
- An example of a government-led review is the recently concluded Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry.

Both of these reviews examined issues of corporate governance, risk management and corporate culture. These are examined in more detail in Chapter 6.

## Content: legislation

The terms 'company' and 'corporation' are dealt with in the CA2001.

### CORPORATIONS ACT 2001 (CTH) s 9

#### Dictionary

Unless the contrary intention appears:

…

'***company***' means a company registered under this Act and:

(c) in Parts 5.7B and 5.8 (except sections 595 and 596), includes a Part 5.7 body; and

(d) in Part 5B.1, includes an unincorporated registrable body.

…

'***corporation***' has the meaning given by section 57A.

### CORPORATIONS ACT 2001 (CTH) s 57A

#### Meaning of corporation

(1) Subject to this section, in this Act, ***corporation*** includes:
   (a) a company; and
   (b) any body corporate (whether incorporated in this jurisdiction or elsewhere); and
   (c) an unincorporated body that under the law of its place of origin, may sue or be sued, or may hold property in the name of its secretary or of an office holder of the body duly appointed for that purpose.

(2) Neither of the following is a ***corporation***:
   (a) an exempt public authority;
   (b) a corporation sole.

(3) To avoid doubt, an Aboriginal and Torres Strait Islander corporation is taken to be a ***corporation*** for the purposes of this Act.

The concept of Aboriginal and Torres Strait Islander corporations is dealt with in Chapter 3, Section 3.5.

## Case law

Many of the modern foundation principles in corporate law arise from 19th-century UK case law. A key case in terms of affirming the structure of all companies, whatever their size or scale, is *Salomon v A Salomon & Co Ltd* [1897] AC 22 (HL). It confirms the separate nature of the corporate entity, with perpetual succession beyond its members. This case—the first and most famous 'family company' case—led to the enormous growth of the corporate form in small and start-up high street businesses, across the 20th century and into the 21st century, particularly with online businesses.

The confirmation of the corporation as an entity in its own right is now a fundamental dimension of corporate law and of corporate structures. The year 1897 therefore marks the start of the widespread use by the mercantile class of companies for business purposes, for creative enterprises, and for the control and distribution of wealth. *Salomon's case* revolutionised the use of the corporate form, which became a mainstay method of running a small business. The form, crucially, was as applicable to a small family-run concern as it was to a large public company.

We examine *Salomon's case* in Section 1.3 below, and in Chapter 1 of the Workbook.

### DID YOU KNOW?

How does trouble at the top of a corporation affect its performance? Google the US company Amazon. This is a trillion-dollar company by share valuation. Its founder, CEO and Chair, Jeff Bezos, is the wealthiest individual in the world. He and his former wife, MacKenzie, together held 16 per cent of the stock in the company, worth approximately US$150 billion. In late 2018 the couple announced their pending divorce. Will personal issues at the top of the corporation affect its plans and results? It also conflates company law and family law.

LINK TO WB ACTIVITY

Refer to the diagrams in Section 1.2 of the Workbook and answer Activity 1.1.

# 1.3 A BRIEF HISTORY OF COMPANIES

The history of company law, from a modern Australian perspective, covers four developmental phases.

- The first in time is the long run of history ending with the liquidation of the East India Company in 1850.
- The second comprises those events that formed the basis of development up to the end of the 19th century.
- The third is the era of modern corporate law beginning in 1897 and continuing up to 2001 with the operation of a national, legally valid scheme as outlined in the CA2001. This marks the slow ascendance of federal law in Australia, given the problems with the Australian Constitution and its lack of a specific corporate law power.
- The fourth is the modern, current phase.

## Concepts: legal and commercial history and foundations

How companies and company law came about falls into four phases.

### First phase: incremental history to the epic corporation as government overseer

The long development of the company, from the basic conception of the corporate form by the Romans to the great historical sweep of the East India Company, forms the first phase. The East India Company:

- was complex, from a trading perspective
- provided the start of international mercantile freight
- became a quasi-governmental entity
- was also complex in the scale of its operations, and
- was vast in its geographical reach.

It operated from 1600 until its eventual demise in 1850.

### Second phase: the great democratising impulse for the creation of Pty Ltd companies

The 19th century saw the UK *Limited Liability Act* in 1855 and *Salomon's case* in 1897, providing huge impetus to the growth of small business and the mercantile class in the high streets of the UK and (by extension) in the main streets of Australia—in suburbia and beyond. The UK became known in the 1980s as a nation of shopkeepers, and the legacy of Mr Salomon was complete.

### Third phase: the growth of the Pty Ltd and conglomerates

The beginning of the 20th century coincided with the creation of Australia's federal system of government and the enactment of the Constitution in 1901. Embedded within the Constitution was, however, the problem of the lack of an oversight power for new corporations: s 51(xx) (the so-called 'corporations power') created a constitutional lacuna. It did not allow the new Federal Government to oversee and regulate newly formed corporations; that is, those formed from the date of the Constitution onwards. This was a somewhat remarkable oversight, given that *Salomon's case* had only been decided some four years previously, and marked the advent of the corporate form as the basis of many new and small corporations, including the type of business in which Mr Salomon played a crucial role.

### Fourth phase: start-ups alongside trillion-dollar corporations

The fourth phase has seen the rise in trillion-dollar companies—as big as many countries (by reference to the size of their economies). Current key issues facing companies include privacy, artificial intelligence and robotics, human autonomy and sovereign or nation state risk.

## Case law

While the 19th century concluded with *Salomon's case*, several UK cases earlier in the century provided signposts to the development of the general law and its contiguity with statute. Some of these key cases will be looked at in *Corporations Law: Concepts, Cases and Culture*, given that they inform the modern, often statutory, principles of Australian corporate law. For present purposes, it is useful to examine the relevant foundation principles from *Salomon's case*. It does no less than establish the modern foundations of the start-up company, which lies at the heart of the modern market-based economy:

### Case: Salomon v A Salomon & Co Ltd [1897] AC 22

**Court:** House of Lords, UK

**Facts:** Mr Aron Salomon was a sole trader who carried on the business of leather merchant and wholesale boot maker. He sold the business to a company he set up, Salomon & Co Ltd. A total of 20,001 shares were issued to Aron Salomon in part consideration for the sale of the business. Just six other shares were issued, one to each of six family members. This gave a total of 20,007 issued shares in total. The company later went into liquidation.

**Issue:** The liquidator asserted that the company was in effect Mr Salomon in his personal capacity. The liquidator further asserted that Mr Salomon was not therefore a creditor of the company and that a purported debenture securing £1,000 should be set aside.

**Decision:** The House of Lords held that the company was a separate and distinct entity from Mr Salomon, and that there was no evidence of fraud or other wrongdoing to set aside this conclusion. Hence, Mr Salomon could be a creditor in relation to the failed company.

**Judgment extract:** Lord Halsbury wrote:

> I am simply here dealing with the provisions of the statute, and it seems to me to be essential to the artificial creation that the law should recognise only that artificial existence—quite apart from the motives or conduct of individual corporators. In saying this, I do not at all mean to suggest that if it could be established that this provision of the statute to which I am adverting had not been complied with, you could not go behind the certificate of incorporation to shew that a fraud had been committed upon the officer entrusted with the duty of giving the certificate, and that by some proceeding in the nature of *scire facias* you could not prove the fact that the company had no real legal existence. But short of such proof it seems to me impossible to dispute that once the company is legally incorporated it must be treated like any other independent person with its rights and liabilities appropriate to itself, and that the motives of those who took part in the promotion of the company are absolutely irrelevant in discussing what those rights and liabilities are.

## Content: the statutory outcome from *Salomon's case*

The CA2001 formalises the position set out in *Salomon's case*. The corporation is a separate legal entity with all the legal powers equivalent to an individual, as confirmed by CA2001 s 124(1).

### CORPORATIONS ACT 2001 (CTH) s 124(1)

#### Legal capacity and powers of a company

(1) A company has the legal capacity and powers of an individual both in and outside this jurisdiction. A company also has all the powers of a body corporate, including the power to:

(a) issue and cancel shares in the company;

(b) issue debentures (despite any rule of law or equity to the contrary, this power includes a power to issue debentures that are irredeemable, redeemable only if a contingency, however remote, occurs, or redeemable only at the end of a period, however long);

(c) grant options over unissued shares in the company;

(d) distribute any of the company's property among the members, in kind or otherwise;

(e) grant a security interest in uncalled capital;

(f) grant a circulating security interest over the company's property;

(g) arrange for the company to be registered or recognised as a body corporate in any place outside this jurisdiction;

(h) do anything that it is authorised to do by any other law (including a law of a foreign country).

A company limited by guarantee does not have the power to issue shares.

As s 124(1) makes clear, the CA2001 equates the legal capacities of the corporation to 'an individual'; that is, an adult person with full legal capacity. This formalises the long-running simile in the common law that a company (and its participants) is somewhat like an adult human—with full legal capacity in terms of being a legal actor and business entity.

## Case law—20th century

There has been a continuation of major case law in terms of substantive corporate law topics. As Australian corporate law has matured and come of age, just like Australian law more generally, there has been less importance attached to UK case law. In its place, there has been more focus on Australian cases, and some concepts from US corporate law. An example of the latter is the business judgment rule, or the so-called 'safe harbour' provision for directors, which is located in s 180(2) of the CA2001 and is discussed in Chapter 8.

### LINK TO WB ACTIVITY

Refer to Section 1.3 of the Workbook and answer Activity 1.2.

# 1.4 CONSTITUTIONAL FOUNDATIONS OF AUSTRALIAN CORPORATE LAW

The concept of corporate law power in Australia begins with s 51(xx) of the Australian Constitution. This requires some conceptual background.

## Concepts: the Australian constitutional arrangement

The Commonwealth was created in 1901 by the consent of the UK Parliament. This was the result of a decade or more of debate, conventions and consultation in the colonies, and was enabled by the acquiescing role of the UK Parliament and the UK sovereign. The Commonwealth was a creature of statute, with enumerated powers in s 51 of the Constitution. The Constitution is the founding document of the Commonwealth. It creates a hybrid form of government, taking its key elements from the UK and the USA. From the UK it took parliamentary democracy and representative government. From the USA it took the federal arrangement combining a central and state governments—and did so largely because of the sheer size of the land mass of the continent.

In combining these disparate elements of federalism and parliamentary democracy, Australia rejected the so-called unitary system by which the UK is governed. That is, there are no states in the UK, just local councils and a central government based in London. New Zealand has a unitary system similar to the UK, with local governments and a central government based in Wellington. Australia, by contrast, has three levels of government—federal, state and local. Australia also rejected the presidential or republican model of the USA (or its progenitor, France), where the President sits alone as a co-equal branch of government. Under Australia's system, the Prime Minister comes from the party with a majority of votes in the House of Representatives. The Australian Parliament has, though, adopted the US terms 'House of Representatives' and 'Senate', as opposed to the UK terms 'House of Commons' and 'House of Lords'.

The Commonwealth was born 'fully formed' in 1901 with a wide range of powers. It was, however, subject to the limits of s 51. If there was no power enumerated in s 51—or elsewhere in the document—there was no power.

The High Court soon laid out its methodology for interpreting the Constitution. Four basic principles informed its view of how to do so:

- First, it held that each head of power in s 51 was to be read on its own terms, not in combination.
- Second, there was no reserve or 'all other matters'-type provision that the Commonwealth could use. The power had to be clear on the basis of the words in s 51 as a matter of interpretation.
- Third, the Constitution was, in essence, a statute and the usual rules of statutory interpretation were to be applied to elicit its meaning.
- Fourth, the literal or plain meaning of the words was the core principle on which to proceed with the process of interpreting the Constitution.

The Constitution also set up the so-called separation of powers arrangement in Australia (again based broadly on the US and UK) where there are three interlinking elements:

- the parliament—to make laws
- the executive branch—to administer law
- the judicial branch—to hear and determine disputes.

This configuration provides the basic architecture of the constitutional arrangement, and it also reflects the physical geography of the relevant buildings in Canberra (just as it does in London for the UK, and in Washington for the USA). It is a model of governmental arrangement. While the theory is that each branch is strictly separate, however, we can see overlaps. For instance, the public service and the Cabinet are part of the executive branch. However, members of the Cabinet and the Prime Minister are also members of the parliament.

In terms of courts, the Constitution establishes the High Court as the judicial body overseeing federal law. It is hence not possible for a state court to determine federal law. If both state and federal law purport to deal with the same subject matter, the inconsistency is settled by the Constitution in favour of the Commonwealth, as set out in s 109 of the Constitution.

Under s 107 of the Constitution, the states retain all of the powers that were not vested in the Commonwealth. They are sovereign entities with power to make law for the 'peace, order, and good government' of the jurisdiction/land area they control.

Another particularity of the Australian Constitution is the fact that the UK sovereign is represented within the arrangement by reference to the Governor-General. While this may appear like a legacy issue, and somewhat anachronistic, the potential power of the role was central to the political events of 1975, involving the Whitlam government.[5]

Changing the Australian Constitution is theoretically possible, but has proven to be difficult in practice. The process of amendment is dealt with under s 128 of the Constitution. The process set out by s 128 requires that for the proposal to succeed and become law, it needs to be approved by:

- a majority of the national vote (more than 50 per cent), and
- a majority of the states (at least four out of the six states).

This 'double hurdle' requirement has proven difficult to achieve. As a result, most proposals to amend the Constitution have failed. Since its inception in 1901, there have been 44 proposals put to referendum under s 128. Of these, only eight have succeeded.[6] The success rate is, therefore, less than 20 per cent.

## Context and culture

The context of Australian corporate law remains the federal constitutional arrangement. As we shall examine, the Commonwealth has its law making, oversight and regulatory role in relation to corporations only at the continuing gift of the states and territories. Corporate law has developed alongside the economic and social forces at play.

Given that corporations are creatures of statute, the role of statue is both critical and central to corporations.

## Content: legislation

In Australia, there is an extra layer of statutory analysis provided by the Australian Commonwealth Constitution. Remarkably, and surely by oversight, the framers did not give the Commonwealth power over new corporations.

### AUSTRALIAN CONSTITUTION s 51(XX)

#### Legislative powers of the Parliament

The Parliament shall, subject to this Constitution, have power to make laws for the peace, order, and good government of the Commonwealth with respect to:

…

(xx) foreign corporations, and trading or financial corporations formed within the limits of the Commonwealth;

5 For a fuller discussion of the legal and constitutional issues, refer to constitutional law texts.

6 See https://www.humanrights.gov.au/our-work/constitutional-reform-fact-sheet-historical-lessons-successful-referendum/.

This single sentence, with its comma and its reference to the past tense in the word 'formed', has proven to be the foundation issue of statutory interpretation; its resolution took a century of debate, litigation and political manoeuvring.

As a result, there is—in addition to the usual type of case law about what it is that companies do—a series of constitution-related cases that provide the narrative to the Australian Commonwealth's fundamental lack of power as regards corporations.

## Case law

### Case: Huddart, Parker & Co Pty Ltd v Moorehead [1909] HCA 36; (1909) 8 CLR 330

**Court:** High Court of Australia

**Facts:** These appeals were brought following convictions for breaches of the *Australian Industries Preservation Act 1906* (Cth), where the appellants had refused to answer certain questions put to them by the Comptroller-General of Customs.

**Issue:** Was the following section of the above Act a valid law of the Commonwealth under s 51(xx) of the Constitution?

> 5(1) Any foreign corporation, or trading or financial corporation formed within the Commonwealth, which, either as principal or agent, makes or enters into any contract, or engages or continues in any combination—
>
> (a) with intent to restrain trade or commerce within the Commonwealth to the detriment of the public, or
>
> (b) with intent to destroy or injure by means of unfair competition any Australian industry the preservation of which is advantageous to the Commonwealth, having due regard to the interests of producers, workers, and consumers,
>
> is guilty of an offence.
>
> Penalty: Five hundred pounds.

**Decision:** The Act was in breach of s 51(xx) of the Constitution. The Commonwealth did not have the power to make such a provision.

**Judgment extract:** Griffiths CJ wrote:

> In my judgment the words of [sec] 51(xx) are not clear and unequivocal, but are open to two constructions, and, applying the principles which I have stated, I think that they ought not to be construed as authorizing the Commonwealth to invade the field of State law as to domestic trade, the carrying on of which is within the capacity of trading and financial corporations formed under the laws of the State. In other words, I think that [sec] 51(xx) empowers the Commonwealth to prohibit a trading or financial corporation formed within the Commonwealth from entering into any field of operation, but does not empower the Commonwealth to control the operations of a corporation which lawfully enters upon a field of operation, the control of which is exclusively reserved to the States. For these reasons I think that secs 5 and 8 are beyond the constitutional power of the Commonwealth, and that the appeal of Huddart, Parker & Co should be allowed.

Barton J wrote:

> I am of opinion, therefore, that secs 5(1)(a) and 8(1) of these Acts, in so far as they deal with the domestic trade of the States, are in no wise incidental or ancillary to the execution of sec 51 (XX) of the Constitution, and that the invasion of that sphere is prohibited by the Constitution. Hence, I am bound to hold that these provisions are invalid, and that the company is entitled to succeed.

The next case is famous for its dicta about how statutes and the Constitution should be construed.

## Case: Amalgamated Society of Engineers v Adelaide Steamship Co Ltd ('Engineers' case') [1920] HCA 54; (1920) 28 CLR 129

**Court:** High Court of Australia

**Facts:** This case involved an industrial dispute arising as a result of a summons under s 21AA of the *Commonwealth Conciliation and Arbitration Act 1904* (Cth).

**Issue:** Did the Commonwealth have power under the Constitution to legislate in relation to industrial disputes?

**Decision:** No, the Commonwealth did not. The Court held that the Constitution needed to be strictly construed. The judgment reflects Australia's then narrow focus as part of the British Empire, and the High Court of Australia was guided by the two most senior courts of the UK: the Privy Council, and the House of Lords.

**Judgment extract:** Knox CJ, Isaacs, Rich and Starke JJ held as follows:

> For the proper construction of the Australian Constitution it is essential to bear in mind two cardinal features of our political system which are interwoven in its texture and, notwithstanding considerable similarity of structural design, including the depositary of the residual powers, radically distinguish it from the American Constitution. Pervading the instrument, they must be taken into account in determining the meaning of its language. One is the common sovereignty of all parts of the British Empire; the other is the principle of responsible government. The combined effect of these features is that the expression 'State' and the expression 'Commonwealth' comprehend both the strictly legal conception of the King in right of a designated territory, and the people of that territory considered as a political organism. The indivisibility of the Crown will be presently considered in its bearing on the specific argument in this case. The general influence of the principle of responsible government in the Constitution may be more appropriately referred to now.
>
> The settled rules of construction which we have to apply have been very distinctly enunciated by the highest tribunals of the Empire. To those we must conform ourselves: for, whatever finality the law gives to our decisions on questions like the present, it is as incumbent upon this Court in arriving at its conclusions to adhere to principles so established as it is admittedly incumbent upon the House of Lords or Privy Council in cases arising before those ultimately final tribunals.
>
> With respect to the interpretation of a written Constitution, the Privy Council has in several cases laid down principles which should be observed by Courts of law, and these principles have been stated in the clearest terms. In *R v Burah* Lord Selborne, in speaking of the case where a question arises as to whether any given legislation exceeds the power granted, says:—'The established Courts of Justice, when a question arises whether the prescribed limits have been exceeded, must of necessity determine that question; and the only way in which they can properly do so, is by looking to the terms of the instrument by which, affirmatively, the legislative powers were created, and by which, negatively, they are restricted. If what has been done is legislation, within the general scope of the affirmative words which

give the power, and if it violates no express condition or restriction by which that power is limited (in which category would, of course, be included any Act of the Imperial Parliament at variance with it), it is not for any Court of Justice to inquire further, or to enlarge constructively those conditions and restrictions.' In *Attorney-General for Ontario v Attorney-General for Canada* Lord Loreburn LC, for the Judicial Committee, said:—'In the interpretation of a completely selfgoverning Constitution founded upon a written organic instrument, such as the British North America Act, if the text is explicit the text is conclusive, alike in what it directs and what it forbids. When the text is ambiguous, as, for example, when the words establishing two mutually exclusive jurisdictions are wide enough to bring a particular power within either, recourse must be had to the context and scheme of the Act.'

In two decisions the Judicial Committee has applied these principles to the interpretation of this Constitution, namely, *Webb v Outrim* and the *Colonial Sugar Refining Co's Case*. In the first mentioned case, quite independently of any observations as to the meaning of the word 'unconstitutional,' it is clear that their Lordships proceeded on the ordinary lines of statutory construction. In the second case the Judicial Committee considered the nature of the instrument itself in order to determine the more satisfactorily the depository of residual powers, and having arrived at the conclusion, as to which this Court has never faltered, that the Commonwealth is a government of enumerated or selected legislative powers, their Lordships examined the language of sec 51 to ascertain from its words whether the suggested power could be deduced. The method of arriving at the conclusion is all that is relevant here. We therefore are bound to follow the course of judicial investigation which those two august tribunals of the Empire have marked out as required by law.

**Comment:** This case gave rise to the notion of strict legalism, which largely dominated the High Court methodology up to the High Court under Mason CJ, 1987–95. The literal approach sought to treat the Constitution in much the same way as an ordinary statute.

## Concepts: the development of corporate law in Australia

The development of corporate law and its oversight have been through several phases.

### Phase 1: 1901–60—'piecemeal' development

Corporate law within the new Commonwealth was off to an uncertain start, given that the Commonwealth lacked the necessary power within s 51(xx) of the Constitution to regulate companies. As a result, the Australian states each developed their own piecemeal version of corporate law oversight. This approach was in place until the 1950s. After the Second World War, however, economic activity was increasingly national, and so a form of national company law was needed.

### Phase 2: 1960–80—'uniformity'

The solution eventually arrived at was based on Victoria's *Companies Act 1958*. Each state used this Act as a starting point, or template, and modified it according to their own particular state needs. These were the Uniform Companies Acts variously passed by New South Wales, Queensland, Victoria, Western Australia, Tasmania and South Australia in 1961 and 1962.

The schemes, however, grew unwieldy over the next two decades, and did so for several reasons:

- Each of the states amended their Acts, so that any notion of national 'uniformity' and consistency became diluted.

- There were episodes of corporate fraud with the growth of the stock market, for instance, requiring a national approach.
- The financial markets were becoming more complex and international, again making it clear that a national approach was required.

By the late 1970s, it was again recognised that a political and legal solution with a nationally harmonious approach was a necessity if the Australian economy was to prosper in an increasingly connected world.

## Phase 3: 1980–2000—'co-operation'

Two decades of so-called uniformity were followed by a decade of the new model known as 'co-operation'. The co-operative scheme involved a complex grid of legislative arrangements by the states and territories underpinned by the *Companies Act 1981* (Cth).

New problems emerged in the 1980s. These included that:

- any state could at any stage withdraw from the agreement
- the resulting law was weak and lacked rigour
- there were different bureaucratic arrangements in each state, as well as national regulation
- the decade (infamous now for its 'greed is good' mantra) had another series of corporate excess and fraud, including the stock market crash of 1987 and its aftermath.

As a result, the Hawke-led Labor government passed the *Corporations Act 1989* (Cth). Before it came into law, New South Wales challenged its constitutional validity. It was clear that the Constitution was not able to provide an appropriate platform—or legally robust supporting mechanism—for 'co-operative federalism' with regard to corporate law.

It would not be until the year 2001 that the referral by the states to the Commonwealth provided a comprehensive political, legal and commercial solution, in the form of the CA2001.

The two High Court cases discussed below, starting with the *Incorporation case*, dealt further crucial blows to the Commonwealth's attempts to control the area of company law.

### Case: New South Wales v Commonwealth ('Incorporation case') [1990] HCA 2; (1990) 169 CLR 482

**Court**: High Court of Australia

**Facts:** The *Corporations Act 1989* (Cth) was an attempt by the Commonwealth to take over the regulatory function regarding companies. The Act was not to be proclaimed if the High Court decided that the Commonwealth Parliament did not have that power.

**Issue:** Was the proposed *Corporations Act 1989* (Cth) valid under s 51(xx) of the Constitution?

**Decision:** Six members of the seven-justice court held:

> There is thus no ground for thinking that s 51(xx) was framed with the intention of conferring upon the Commonwealth the power to provide for the incorporation of companies. Indeed, the history of the paragraph plainly indicates that the draftsmen of the provision did not contemplate that it should confer any power otherwise than in respect of corporations already formed.

The court essentially confirmed the approach in *Huddart Parker*.

**Judgment extract:** The joint judgment of Mason CJ, Brennan, Dawson, Toohey, Gaudron and McHugh JJ held as follows:

> 6. Section 51 of the Constitution provides that the Commonwealth Parliament shall have power to make laws with respect to:
>
> (xx) Foreign corporations, and trading or financial corporations formed within the limits of the Commonwealth.
>
> …
>
> 9. Both precedent and history support this construction of the text of s 51(xx). In *Huddart, Parker & Co Pty Ltd v Moorehead* (1909) 8 CLR 330 the five members of the Court were unanimously of the opinion that the subject matter of s 51(xx) is confined to corporations already in existence and does not extend to the creation of corporations. That, they said, is the plain meaning of the words 'formed within the limits of the Commonwealth'.
>
> …
>
> 11. *Huddart Parker* was concerned with the validity of ss 5 and 8 of the *Australian Industries Preservation Act 1906* (Cth). Those sections prohibited certain restrictive or monopolistic practices on the part of foreign, trading or financial corporations. In concluding that the relevant provisions were beyond power, a majority (Griffith CJ, Barton and O'Connor JJ) placed reliance upon the doctrine of reserved powers. But the question of the power to legislate for the creation of corporations was determined by all the members of the Court by reference to purely textual considerations, quite apart from the now discarded doctrine. Indeed, it was the view of the remaining members of the Court, Isaacs and Higgins JJ, concerning the doctrine of reserved powers which was to prevail in the *Engineers' Case*. However, in *Huddart Parker* they reached the same conclusion upon the meaning of the words 'formed within the limits of the Commonwealth' as the other members of the Court. Isaacs J was alone in dissent concerning the validity of ss 5 and 8 of the *Australian Industries Preservation Act*, but upon the question of the power of the Commonwealth Parliament to provide for the creation of corporations, he was unequivocal. He said, at p 394:
>
> The creation of corporations and their consequent investiture with powers and capacities was left entirely to the States. With these matters, as in the case of foreign corporations, the Commonwealth Parliament has nothing to do. It finds the artificial being in possession of its powers, just as it finds natural beings subject to its jurisdiction, and it has no more to do with the creation of the one class than with that of the other.

**Comment:** The constitutional impasse first confirmed in *Huddart Parker* (1909) was reconfirmed in the *Incorporation case* in 1990—the restrictions set out in s 51(xx) were essentially the same 80 years later. The stalemate continued, and would do so for another decade. *Re Wakim* in 1999 simply exacerbated the need for a comprehensive solution.

## Case: Re Wakim; ex parte McNally [1999] HCA 27; (1999) 198 CLR 511

**Court:** High Court of Australia

**Facts:** The case involved litigation that called into question legislation that provided for cost-vesting powers between the states and the Commonwealth.

**Issue:** Was legislation in which the states purported to give power to federal courts to hear state company law matters constitutionally valid? (This is what is referred to as cross-vesting legislation.)

**Decision:** The High Court held that the legislation was invalid as it was not within the scope of the Constitution.

**Judgment extract:** Gleeson CJ held as follows:

> Conferring, or agreeing to the conferment, upon a federal court, established under the Constitution to exercise the judicial power of the Commonwealth with respect to a limited class of matters, of jurisdiction to exercise the judicial power of the States is not in aid of the execution of the principal power. It is both a substantial addition to the power, and an attempt to circumvent the limitations imposed upon the power by the Constitution.

Another significant case followed soon afterwards

## Case: R v Hughes [2000] HCA 22

**Court:** High Court of Australia

**Facts:** The Commonwealth Director of Public Prosecutions (DPP) sought to prosecute offences under state-based corporate law.

**Issue:** Could the DPP do so?

**Decision:** The High Court held that the DPP could prosecute the offences under powers provided in s 51(i) and (xxix) of the Constitution. It reconfirmed that s 51(xx) provided no such power.

**Judgment extract:** The majority—Gleeson CJ, Gaudron, McHugh, Gummow, Hayne and Callinan JJ—held that the DPP could prosecute because:

> … the offences with which the accused is charged relate to the making of investments in the United States and thus to trade and commerce with other countries (s 51(i)). They also relate to matters territorially outside Australia, but touching and concerning Australia, and so would attract s 51(xxix).

Kirby J (in dissent) was scathing of the intricacies to which the Commonwealth and state governments had gone to solve the intractable problem posed by s 51(xx) of the Constitution:

> 58. In the *Incorporation Case 1990* this Court, by majority held that the corporations power did not entitle the Federal Parliament to legislate for the incorporation of trading and financial corporations. A key assumption of the *Corporations Act*, as enacted, was thus invalidated. This narrow decision of the Court will, in my opinion, one day need to be revisited. A factual consequence has been the grotesque complications that exist in the regulation of corporations under Australian law illustrated in *Byrnes*, *Bond* and now this case.
>
> 59. The precise reasons for adopting the scheme that now comes under scrutiny, in response to the *Incorporation Case*, are not disclosed. The rejection of a formal amendment of the Constitution to allow ample legislative powers to the Federal Parliament can doubtless be explained by the discouraging history of referendum proposals under s 128 of the Constitution. The disinclination to refer powers to, or to request and concur in the exercise of State powers by the Federal Parliament is said to arise out of a concern that such powers, once surrendered, might not be capable of retrieval by the States. But only political considerations, disputes over revenue and possibly a feeling of discouragement following the *Incorporation Case* can explain the nearly incomprehensible scheme of legislation eventually adopted.
>
> 60. Courts, including this Court, regularly speak in terms of the 'intention' of the legislature when interpreting particular legislation. This polite but unacceptable fiction has never been shown in starker relief than in the present case. So complex is the interlocking legislation, with fiction piled upon fiction, that it must be doubted whether any of those presenting and enacting it were truly aware of precisely what they were doing. It may be hoped that this and other recent decisions, together with the great national importance of the subject matter of the legislation, will encourage its early reconsideration and the adoption of a simpler constitutional foundation to reduce the perils that are otherwise bound to recur, possibly with serious results.

**Comment:** *Re Wakim* and *R v Hughes* marked the beginning of the end of the constitutional impasse; the cases proved the point (again) that the constitutional imbroglio concerning the corporations law power needed to be definitively settled at the governmental level—that is, between the states and territories on the one hand, and the Commonwealth on the other. Section 51(xx) did not allow the Commonwealth to pass company laws, to regulate companies, or to determine company law matters. Each of these were matters for the states. If the Commonwealth wanted to have a uniform approach to any or all of these issues, it needed the specific permission of the states, which retained sovereignty over them. This gave rise to the Alice Springs Agreement of 2000, which led to referral legislation by the states that then enabled the Commonwealth to pass two key pieces of legislation in the same year: the CA2001 and the *Australian Securities and Investments Commission Act 2001* (Cth).



## Constitutional arrangements leading to the CA2001

The issue of the Commonwealth Government's lack of ability to regulate and oversee corporations needed a political solution, where the states and territories ceded power to the Commonwealth.

Just as there has been a series of complex cases dealing with constitutional issues related to corporations since Federation, so too has there been a series of statutes, cooperative agreements, schemes, and the like dealing with the development of Australian corporate law, and the economic and social necessity that there be one nationally consistent system, rather than eight different systems (comprising the six states and two territories).

# Concepts: the Explanatory Memorandum to the Corporations Bill 2001 (Cth)

The Explanatory Memorandum is a 39-page document released in 2001 by the then Attorney-General and the Minister for Finance. It provides the background and context to the CA2001.

The Explanatory Memorandum pulled together the various strands of the previous decade. It explained that a 'clean start' was required to resolve the uncertainties relating to the system of corporate law that had been in place since 1990. Those uncertainties were underwritten by the High Court cases of *Re Wakim* (1999) and *R v Hughes* (2000).

An extract from the Explanatory Memorandum provides a summary of the main issues:

## EXPLANATORY MEMORANDUM TO THE CORPORATIONS BILL 2001 (CTH)

### Outline

2.1 The Bill is one of a package of bills responding to the High Court's decisions in *Wakim* and *Hughes*.

2.2 The other bills are:

- Australian Securities and Investments Commission Bill 2001;
- Corporations (Fees) Bill 2001;
- Corporations (Securities Exchanges Levies) Bill 2001;
- Corporations (Futures Organisations Levies) Bill 2001;
- Corporations (National Guarantee Fund Levies) Bill 2001; and
- Corporations (Consequential Provisions) Bill 2001.

2.3 The Bill is designed to replace the *Corporations Act 1989* and the Corporations Law of the Capital Territory, and the corresponding legislation of the Northern Territory and those States which make suitable references to the Commonwealth Parliament in accordance with section 51(xxxvii) of the Constitution, as the statutory basis for the formation of companies, corporate regulation and the regulation of the securities and futures industries.

2.4 The Bill will, in effect, re-enact the Corporations Law as a Commonwealth Act capable of operating throughout Australia. The principal objective of this explanatory memorandum is therefore to explain the differences between the Bill and the Corporations Law. Explanatory material for the provisions of the Corporations Law on which the Bill is based may be found in the explanatory memoranda for the legislation that enacted or amended those provisions.

The Explanatory Memorandum provided the following background.

## EXPLANATORY MEMORANDUM TO THE CORPORATIONS BILL 2001 (CTH)

### Background to the Bill

4.1 The current Corporations Law scheme commenced on 1 January 1991. Under that scheme, the Corporations Law is contained in an Act of the Commonwealth Parliament (the *Corporations Act 1989*) and is enacted for the Australian Capital Territory. Laws of each State and the Northern Territory apply the Corporations Law of the Australian Capital Territory as a law of the State or the Northern Territory. The scheme was designed to operate as a single national scheme even though it actually applies in each State and the Northern Territory as a law of the State or Territory.

4.2 The current Corporations Law is administered generally by a Commonwealth body, ASIC, established under the *Australian Securities and Investments Commission Act 1989*. Each State and the Northern Territory has passed legislation applying relevant provisions of that Act, and also conferring functions relating to the administration and enforcement of the Corporations Law on, among others, the Commonwealth Director of Public Prosecutions and the Australian Federal Police.

4.3 The 'cross-vesting' provisions of Commonwealth, State and Territory legislation comprising the current Corporations Law scheme were intended to establish a seamless and efficient system of adjudication by, among other things, allowing federal courts to exercise relevant State jurisdiction and State courts to exercise relevant federal jurisdiction.

4.4 The current scheme is also supported by the Corporations Agreement, an inter-governmental agreement to which the Commonwealth, the States and the Northern Territory are parties. The Agreement requires consultation and, in some cases, voting on amendments of the Corporations Law and related scheme legislation.

4.5 Recent decisions of the High Court have cast doubt on the constitutional foundations of important elements of the Corporations Law scheme.

4.6 The decision in *Wakim* rendered the cross-vesting arrangements invalid to the extent that they purported to confer State jurisdiction on federal courts.

4.7 In *Hughes*, the Court decided that the Commonwealth cannot authorise its authorities or officers to undertake a function under State law involving the performance of a duty (particularly a function having the potential to adversely affect the rights of individuals) unless the function has a sufficient nexus with a Commonwealth legislative power. As the limits of Commonwealth legislative power are uncertain, the decision has cast doubt on the ability of Commonwealth authorities or officers to exercise certain powers and functions under the Corporations Law. This has resulted in much uncertainty and inefficiency in relation to Australia's system of national corporate regulation.

4.8 These problems can be avoided by re-enacting the Corporations Law as a single federal law of national application. Under the section 51(xxxvii) of the Commonwealth Constitution, the Commonwealth Parliament may legislate with respect to matters referred to it by the State parliaments. Suitable State references can put beyond doubt the Commonwealth Parliament's power to enact the Corporations Law as a federal law of national application.

…

[The Explanatory Memorandum then explained the duration and renewal of the legislation.]

4.11 The Bill is introduced on the further assumption that:

- the amendment reference will not restrict the capacity of the Commonwealth Parliament to amend the Bill or the ASIC Bill once enacted (and as in force from time to time) in reliance on the legislative powers that it has apart from the references;
- the State reference legislation will include a general purpose or object provision to the effect that nothing in that legislation is intended to enable the making of a law under the amendment reference with the sole or main underlying purpose or object of regulating industrial relations matters even if, but for the provision, the law would be a law with respect to a matter referred to the Commonwealth Parliament by the amendment reference;
- the State reference legislation will include a 'sunset' provision terminating the references after five years (with provision for extension by proclamation);
- the Corporations Agreement will provide that if four States vote to terminate the amendment reference all referring States will terminate that reference (the Bill itself will provide that if any State individually terminates the amendment reference it will cease to be part of the scheme);

…

Given the constitutional problems with the schemes before this one, the focus was understandably on ensuring that the underlying constitutional framework was robust, and beyond a legal challenge for lack of power. This was achieved by a new approach. Rather than s 51(xx) of the Constitution, the founding of the CA2001 primarily relied upon the referral power of the states: s 51(xxxvii).

This referral power is referenced in the provisions of cl 4.11, which include two control mechanisms in the gift of the states:

- the scheme needs to be renewed every five years, and
- if four of the six states (a numerical majority) so decide, the scheme can be terminated.

## Statute in the context of corporate law

Statutes have expanded over time. The post-Second World War nation state has seen the relentless rise of statute and delegated legislation in both Australia and the UK.

The two decades since the CA2001 have arguably been the most economically efficient, in so far as the oversight and regulation of corporations are concerned.

### DID YOU KNOW?

There are two global US-based companies, Apple and Amazon, with one-trillion stock market values. A trillion dollars is one thousand billion dollars.

The average age of even the biggest corporations is just 37 years. This is less than half the life expectancy of the modern adult.

## Statutes and statutory interpretation

As the CA2001 is central to the study and understanding of all aspects of contemporary corporations law, it is worth recalling the basic textual analysis relevant to the reading of statutes.

We begin with the plain or literal meaning approach; that is, each word has its usual meaning, and the courts attribute those meanings. If only life and statute were so simple, though. Words often take on a new meaning given their context and the words surrounding them. Hence, we need a set of back-up principles to elucidate meaning beyond the literal approach. This include rules such as:

- the golden or 'mischief' rule, and
- the purposive rule.

We look at these issues in more detail in Chapter 4.[7]

### LINK TO WB ACTIVITY

Refer to Section 1.4 of the Workbook and answer Activity 1.3.

# 1.5 THE CONTEXT AND CULTURE OF THE CORPORATION

The context of corporate law can be viewed in several ways; first, as a set of specialised laws dealing with the subject matter of corporations, and operating within the law more broadly; second, as it relates to social economic and other forces at play; and third, in terms of the future: how should corporate law function in better and more useful ways?

John Parkinson, a founding legal academic specialising in theories about corporate social responsibility (CSR),[8] notes that large companies—especially valuable companies that are publicly listed on the stock exchange and that employ many people—are different from other interest groups in society because they have real 'social decision-making power', or influence, in two ways:

- directly, through interest groups (such as the Business Council of Australia) to make representations to government in order to influence government policy, and
- structurally, because of the crucial role boards and managers play in production, investment and employment decisions, which in turn shape the economic and political environment within which governments make policy.[9]

These factors give large corporations enhanced bargaining power and particular special influence.[10] The question then is, how should large corporations act within this framework?

Parkinson notes that 'corporate freedom of action is bounded by law (the rights of employees, environmental controls, and so on) and constrained by markets, but within these limitations there is a core of real business discretion'.[11] CSR looks at the legitimate use of this discretion and the form that corporate law *should* take in order to control it in the public interest. CSR focuses on the area of corporate discretion, and the project of seeking to improve and reform the corporate law in order to better provide for the public interest.



7 In terms of contextualising statutory interpretation relevant to corporations law, reading the following text is useful: DC Pearce and RS Geddes, *Statutory Interpretation in Australia*, 7th ed, LexisNexis, 2011.

8 CSR is examined more fully in Chapter 16.

9 John Parkinson, *Corporate Power and Responsibility: Issues in the Theory of Company Law*, Oxford University Press, Oxford, 1993, 19.

10 Ibid, 20.

11 Ibid, 19.

Set out below are three linked foundation ideas that are worth looking at.

## 1 The ongoing role of government in corporations

Legal corporate history shows that the first corporations were essentially extensions of nascent governments; they were given Royal Charters or permissions to trade for and on behalf of the government. The East India Company is a good example. Given a Royal Charter in 1600 by Queen Elizabeth I, it went on to essentially govern India as a colonial outpost of Britain. The company existed for 250 years. So historically, companies have long been connected to government. Hence, governments have a legitimate stake in overseeing them. ASIC is the Australian Government-funded corporate regulator.

## 2 From private profit making to public utility and the public good

Consider some of the biggest companies in the world, including Facebook and Google. They are very wealthy public companies designed to make a profit. They now control much of the online world.

Very powerful companies may, at some point, oversee things that are not simply goods and services, but public utilities. From the time of Thomas Edison and the invention of electricity, there has been tension between private power and public benefit. Governments have a legitimate stake as the regulator in ensuring competition around price and provision of service. In the USA, this has resulted in anti-trust laws to break up monopolistic arrangements where one company simply garners too much control. This occurred with Microsoft in the 1990s. In Australia, the ACCC looks at these issues.

So the issue is, how should governments regulate services such as online search (Google) and social connectivity (Facebook) when these services—which have rapidly gone from niche to normal—have become parts of everyday life that are necessary for participation in the 21st-century community? They are akin to emerging personal and community rights in a country like Australia. How should these services be regulated? Facebook, for example, has said that it is not a publisher of content, but a curator. Is this right? How is Facebook different from a traditional-style newspaper, which carries liability as a publisher?

## 3 Stakeholders and shareholders—profit maximisation?

Corporations have been subject to much theorising about what their role is—whether it is purely private (to make lots of profit for shareholders) or whether it is broader, and takes into account stakeholders such as customers and employees. The Banking Royal Commission[12] highlighted the problems that result when bank, insurance and financial services customers are not considered to be vital; when, instead, profit maximisation takes over.

How does CSR deal with this conundrum? Enlightened shareholder interest takes the narrative that what is good for customers should also be good for shareholders. There is a virtuous circle, or connection, between satisfied customers who stay, and who give good word-of-mouth recommendations so that the number of customers grow. This drives business and revenue, which in turn drives share price and share returns (via dividend income or capital value appreciation of the shares). These matters are elucidated further in Chapter 16.



12 Royal Commission into Misconduct in the Banking, Superannuation and Financial Services Industry, *Final Report*, 1 February 2019, https://financialservices.royalcommission.gov.au/Pages/default.aspx.

## KEY TRENDS

### Industry

- *'Red tape' vs effective regulation:* this is a debate about whether Australian business generally, and corporations specifically, are overregulated, and the role that is—and should be—played by the regulators, principally ASIC.
- *Market conduct and misconduct:* the Banking Royal Commission addressed these issues.

### Legal profession

- *Technology and the law:* the rise of 'AI' (artificial intelligence), and its likely impacts on the legal profession, is a widely discussed topic.

### LINK TO WB ACTIVITY

Refer to Section 1.5 of the Workbook and answer Activity 1.4.

### LINK TO WB ACTIVITY

Refer to the end of Section 1.5 in the Workbook and answer Activity 1.5.

# TEXTBOOK CHAPTER 1 REVIEW

## SUMMARY OF THE KEY POINTS FROM THIS CHAPTER

In this Chapter, we have examined the basic aspects or pillars of companies as business entities, and the historical and constitutional foundations behind the modern-day CA2001. The topics included:

- *legal studies and skills development*—the study of corporate law, and an overview of written and oral legal skills; the focus in this Chapter is on developing written skills
- *overview*—an overview of the corporation as a business entity and the basic architecture and relevant roles played by people within corporations
- *history*—a brief history of companies/corporations; this can be a major topic in its own right, depending on where the history is commenced, and from whose perspective it is narrated
- *legislation*—examining the legislative foundations of Australian corporate law and the fact that Australia, given its system of federal government, has needed to develop essentially a bifurcated legislative narrative in relation to corporations law; that is, there have been major constitutional issues and impediments to resolve, alongside and in addition to setting out the legislation relevant to corporations, as per the CA2001
- *context*—the modern context for the operation of corporations; this increasingly revolves, particularly for big corporations, around broader issues of corporate citizenship, and the developing concept of the responsible contemporary corporation.