BUSINESS ORGANISATIONS - AGENCY

There are 3 main methods of business organisation that agents use:

- **Sole trader**
- **Partnership**
- **Company.**

The best method is a function of the scale or size of your business, income factors, exposure to risk, how much control you require over the business and the type of business.

SOLE TRADER
A popular method is sole trader where the agent uses his/her name and is the one and only owner of the business.
ADVANTAGES:

- **Complete control**
- **Free and easy to set up**
- **Goodwill potential in the use of one's name**
- **May attract clients who wish to deal with a person rather than a corporation.**

DISADVANTAGES:

- **The sole trader is completely liable for debts and liabilities incurred**
- **Attracts the highest income tax rate**
- **May hamper growth - a sole trader is only possible for a small business.**

PARTNERSHIP
The partnership system is more popular amongst professionals than the sole trader. A partnership is defined as:

> **"The relationship that exists between persons carrying on a business in common with a view to profit."**

It is a contract between two or more parties to enter into a legally binding relationship. There are 3 essential elements of a partnership are:

1. **The carrying on of a business**
2. **In common**
3. **With a view to profit.**

All three are necessary for a partnership to be established. The Partnership Act allows a partner to bind the firm and the other partners when two elements are satisfied:

- **When the partners acts are within the type of business carried on by the firm.**
- **When the partners' actions are carried out in the usual way.**

If the partner does not however have any authority and the third party knows this, the partnership is not bound. Partners in a partnership are subject to several and joint liability
SEVERAL LIABILITY: *Several liability* is separate liability.
EXAMPLE
Under sole trader arrangements agent A borrows $1 000 from B and

agent C borrows $ 10 000 from B. Each party has a separate or several liability. If A fails to repay $1 000 to B, that is of no concern to C. C has no liability for A's debt. Similarly, if agent C fails to repay $10 000 to B, that is of no concern to A. A has no liability for C's debt.

JOINT LIABILITY: *Joint liability* means that all the parties have a joint obligation to repay irrespective of any personal arrangements between them.

EXAMPLE

Agents A and C jointly borrow $10 000 from B on the understanding between A and C that A will be responsible for repayment of $6 000 and C be responsible for repayment of $4 000. This is of no concern to B who only looks to the joint promise of A and C to repay the debt. If A goes bankrupt and cannot repay any part of the debt, B can look to C for repayment of the full amount. However, B, once obtaining judgment against one party, cannot then sue the. other party, even if the judgment has not been satisfied.

JOINT AND SEVERAL LIABILITY: Agents as partners are jointly and severally liable for a debt to a third party.

EXAMPLE

Agents A and C are jointly and severally liable to pay $10 000 to B. This means that B can sue A for the whole of the debt, or B can sue C for the whole of the debt, or B can sue them both. As between themselves, A and C are responsible for the debt in the proportions that they agreed.

DISSOLUTION OF PARTNERSHIP

An agency partnership is dissolved:

- **By the expiration of a fixed term**
- **If entered into for a single undertaking, by the termination of such undertaking.**
- **If entered into for an undefined time, by any partner giving notice**
- **Death of a partner**
- **Bankruptcy of a partner**
- **If it becomes unlawful.**

DISSOLUTION BY THE COURT: The court may dissolve the partnership on any of the following grounds:

- **Where a partner has been declared to be of unsound mind**
- **Permanent incapacity of a partner**
- **Where a partner is guilty of conduct which, in the opinion of the court, is calculated to prejudicially affect the business.**
- **Willful or persistent breach of the partnership agreement**
- **When the business can only be carried on at a loss**
- **Whenever circumstances have arisen that render it just and equitable that the partnership be dissolved.**

The author has carried out a survey on a number of small businesses and the reasons advanced why they formed a partnership. Overwhelmingly, the main reason was the reduction in tax liability as the rate is split between the two partners. This was a particularly, strong reason for husband/wife partnerships.

DRAFTING A PARTNERSHIP AGREEMENT

When drafting a partnership agreement, the following matters will need to be considered. These are, of course, only the barest essentials, and depend very much on circumstances. Partnership agreements will also contain provisions covering other matters that are not covered in these general comments. Therefore, this guide should not be used as a substitute for legal advice.

Legal QUESTIONS TO BE ANSWERED

- **Is a formal partnership agreement necessary?**
- **When will the partnership commence? What will be the duration of the partnership? This data should be included in the agreement, particularly if the partnership is for a set period only.**
- **How will partnership land be held? If the land is already owned by one of the partners, will the land be transferred to all the partners or held in trust for the partnership? Or will a lease be granted to the partnership? Normally an agreement would be drawn up to allow the partnership to lease the land and buildings from the partner owner.**
- **If the place where the partnership business will be carried on is already leased by one of the partners, will the lease be assigned to all partners? Usually the lease is rewritten or assigned to the new partnership as lessee.**
- **Will a firm of accountants be appointed to draw up the partnership accounts? It is advisable to engage an accountant to attend to the affairs of the partnership who is NOT the accountant used by any partner for their private affairs.**
- **Will there be any prohibition on partners assigning or changing their interest in the partnership? It is essential to have these points clearly defined in the partnership agreement.**

Financial QUESTIONS TO BE ANSWERED

- **In what proportions will profits and losses (including capital and losses) be shared? Will any partner be entitled to draw sums on account of profits? The usual practice is for all partners to work equal hours and profits and losses to be distributed equally. Partners would normally take equal drawings per month Against profits.**
- **Who will be the firm's bankers? What will be the cheque signing arrangements? Partnership cheques are normally signed by any two partners.**
- **If one partner decides to sell his/her interest, how is the business valued? Do other partners get the *right of first refusal*? Partnership agreements should detail the method of valuing the business and whether right of first refusal to other partners either singularly or collectively will be applicable.**

Personal QUESTIONS TO BE ANSWERED

- **In what proportions will capital be contributed and belong to the partners? Will capital carry interest? In the great majority of partnerships, all members contribute an equal amount of capital which does not carry interest.**
- **If a loan from a partner is contemplated, what will be the terms of the loan? This could be covered in the partnership agreement, usually stated as at current bank lending rate for business loans.**
- **Is it understood that all partners are jointly and severally liable to the full extent of their private assets for debts of the partnership? In this regard, a partner who has more private assets than the other partner(s) has more at risk. All partners should check their individual liability in relation to the partnership agreement.**
- **Will majority decisions of partners govern all matters? This could apply, however in large partnerships, to maintain harmony, a consensus of all partners may be appropriate for major decisions.**
- **What happens if there are two partners and they disagree? Generally in this situation the *status quo* would remain.**
- **Are partners required to insure each other for the protection of the remaining partner(s) in the event of the death of a partner? Worth considering. This is one method used to finance the purchase of a**

deceased partner's equity.

THE AGENCY AS A CORPORATION - CORPORATIONS LAW
The third method of operation is as a corporation. Advantages of incorporation include:

- **Limited liability**
- **Flexibility**
- **Perpetual succession**
- **The company's shares can be transferred**
- **Imputation of taxation**
- **The company has power to acquire, hold and dispose of property**
- **The company is capable of suing and being sued**
- **Separate legal entity: upon incorporation the company**
- **Becomes a new and independent legal entity.**

Disadvantages of incorporation include:

- **Procedural difficulties for shareholders to bring a court action on their own behalf and on behalf of their company.**
- **Limited role that shareholders have in management (that is, loss of control)**
- **The ever-increasing penalty provisions applying to the defaulting officer and director.**
- **Fees associated with complying with the Corporations Law. For example, filling of the Annual Return, annual accounts.**
- **The paperwork associated with special resolutions and Annual General Meetings.**
- **The need for auditors - or at least, accountants.**

The duties of the directors of an agency company are more onerous than the other two forms of ownership. However, most agents will be a Small Proprietary Company only (see later) and under the new company law, the duties and responsibilites are not as nearly as onerous as for large and public companies. To give you an idea of the extra cost and responsibilities that a corporatised agent incurs and has, the following is a brief description of the duties and responsibilites under the Act:

DIRECTORS DUTIES
Common law:

- **To act in good faith**
- **To act honestly in the company's best interest**
- **To exercise care, diligence and skill**
- **To avoid conflicts of interest**
- **Not to make secret profits and make full disclosure**
- **To act in the interest of creditors**
- **To act in the interest of beneficiaries when the company is a trustee.**

THE AUSTRALIAN SECURITIES COMMISSION (ASC)
The Australian Securities Commission (ASC) is an independent government body that ensures fair play in business, reduces corporate crime, helps to protect investors and Australia's business reputation abroad. Further, it aims to protect the interests of companies and investors by providing information about companies. The Corporations Law (the Law) and the Corporations Regulations impose various obligations on companies and their officers. Failure to

comply may render the company or its officers liable to certain penalties or prosecution.
This modules covers the routine requirements of the Law and Regulations that a corporatised agency must follow but it is not an exhaustive statement.
REGISTERED OFFICE
Every company must have a registered office within Australia to which all communications and notices may be addressed. Where the company has given the ASC notice of office hours under s218(2), the office must be open to the public for at least three hours between 9am and 5pm on each business day. If no s218(2) notice is lodged with the ASC, the office must be open for at least five hours between 10am and 4pm on each business day [s2I7, s218, s240(5)].
If the agent changes the place of his/her registered office, he/she must notify the ASC within seven days on Form 203 'Notification of change of office hours or address of one or more corporations' [s2I8]. No fee will be payable if the agent lodges the new details within this time. If the corporatised agent does not occupy the address specified as the registered office, the actual occupant of the premises must give consent in writing to the agent to use of the address as the address of the registered office.
COMPANY NAME
The corporatised agent must display the company name on the outside of every office or place in which he/she carries on the agency business. If it is the 'registered office' those words must also appear [s2I9(8)].
AUSTRALIAN COMPANY NUMBER
When it is registered, every Australian company receives a unique nine digit identifying number known as the Australian Company Number (ACN). The corporatised agent's name, in legible characters, followed by the words 'Australian Company Number' (or a permitted abbreviation) and the number itself must appear on:
The common seal and every other seal of the company

- **Every public document issued, signed or published by, or on behalf of, the company.**
- **Every eligible negotiable instrument issued or signed by, or on behalf of, the company.**
- **All documents intended or required to be lodged with the ASC under the Law [s219].**

LODGMENT OF DOCUMENTS
When the corporatised agent lodges a document, he/she must clearly identify:
- **The name of the company to which the document relates and its Australian Company Number.**
- **The title of the document**
- **The name, address and telephone number of the lodging party.**

If the document is an ASC printed form, space for these details are provided on the form. Requirements relating to annexures are listed on most ASC printed forms and in regulation 1.06 of the Corporations Regulations.
WHERE TO LODGE DOCUMENTS
Urgent documents, such as applications for incorporation applications

for change of company name charge documents notices of registered office notices of external administrators should be lodged over the counter at any ASC Business Centre or with a Local ASC Representative.
Documents such as:

- **Prospectuses**
- **Takeover documents trust deeds**
- **Applications for securities industry licences**

- should be lodged in person at an ASC Regional Office or by mail to Australian Securities Commission GPO Box 9827 in the capital city of your State or Territory.

FEES TO BE PAID
The corporatised agent may be required to pay a prescribed fee to lodge and register his/her documents. If the agent does not pay the fee at the time you lodge the document, processing will be delayed until the fee is received.
PREPARATION OF ACCOUNTS
Unless exempted by an ASC class order, public companies and large proprietary companies must prepare a profit and loss account and a balance sheet for each financial year that gives a true and fair view of the company's profit and loss and state of affairs at the end of the relevant accounting period [s292, s293].
These accounts must be prepared within the prescribed deadline (see definition of 'deadline' in section 9 of the Corporations Law), must comply with prescribed requirements and must be prepared in accordance with applicable accounting standards.
SMALL PROPRIETARY COMPANIES
The agent will most likely be a *small proprietary company*. A *small proprietary company* will not have to prepare financial statements unless:

- **Required to do so by the ASC**
- **Required to do so by members holding 5% of the company's shares**
- **It is controlled by foreign companies and is not covered by consolidated accounts lodged with the ASC [s283C(2) and s283B].**

Most agencies will come under the definition of a *small proprietary company*. Such a company is subject to much less rigorous rules and regulations compared to that for a large proprietary company.
A *small proprietary company* is one that has satisfied at least two of the following tests:

- **Gross operating revenue for the financial year of the company and the entities it controls (if any) is less than $10 million;**
- **Gross assets at the end of the financial year of the company and the entities it controls (if any) are less than $5 million;**
- **The company and the entities it controls (if any) have fewer than 50 employees at the end of the financial year [45A(2)].**

A company that cannot satisfy at least two of the above criteria is classified as a *large proprietary company* [s45A(3)].

APPOINTMENT OF AN AUDITOR
Unless the company is a *small proprietary company,* it must appoint an auditor within one month after the date of incorporation [s325, s3270)]. The initial appointment of an auditor can be made by the directors or by resolution at a general meeting of the company [s327]. This auditor will hold office until the first Annual General Meeting

when the company will make an appointment. The auditor then appointed will hold that office until death or removal or resignation or until the person is no longer deemed by the Law to be qualified to hold office [s327(4), s324].

A *small proprietary company* will not have to appoint an auditor unless:

- **Required to do so by the ASC**
- **Required to do so by members holding 5% of the company's shares;**
- **It is controlled by foreign companies and is not covered by consolidated accounts lodged with the ASC [s3251.**

ANNUAL GENERAL MEETING (AGM)

A *proprietary company* is not required to hold an Annual General Meeting. A *public company* must hold an Annual General Meeting at least once in every calendar year, and within five months of the end of the financial year [s245(l)]. A public company is required to hold its first Annual General Meeting within 18 months after its incorporation or within five months after the end of its first financial year, whichever comes first [s245(2)].

Annual Return

A company must lodge an annual return for each year. This annual return must be in the prescribed Form 316 'Annual Return of a company'. Form 316 and an instruction Guide on how to complete the annual return are sent by the ASC to every registered company each year in due time for the company to complete the form and lodge it. Details already supplied to the ASC by the company will be shown on the form. A proprietary company must lodge with the ASC an annual return for each calendar year before 31 January in the next calendar year [s335(1A)].

Lodgment of Annual Accounts

The Corporations Law requires all companies to keep records that would enable annual accounts to be prepared and audited if required.

Proprietary Companies

Some companies that were non exempt proprietary companies prior to the commencement of the First Corporate Law Simplification Act must attach accounts to the annual return they are required to lodge by 31 January 1996. That is the last annual return to which proprietary companies will be required to attach accounts. Thereafter, if a proprietary company is required to lodge accounts (for example, because it is large), those accounts will be lodged separately.

***Small proprietary companies*, that are foreign controlled and not covered by consolidated accounts lodged with the ASC by their parent company, are required to lodge company accounts and reports with the ASC. These proprietary companies must prepare and lodge audited accounts with the ASC within four months after the end of the financial year [s317(2), s283D(4)].**

***Large proprietary companies*, except disclosing entities, must lodge accounts within four months after the end of the financial year [s317B(2), s283D(3)].**

Special resolutions

Certain changes relating to a company need to be authorised by way of a *special resolution.* The term *special resolution* is defined in s253. The company must detail any such resolution on Form 205 'Notification of resolution' and lodge it with the ASC within the prescribed time.

Books and Registers

A company is required to keep the following Books and Registers.

- **Register of members [s216B]**
- **Register of option holders, if any [s216C]**
- **Minutes of all proceedings of general meetings and of meetings of its directors. [s258]**
- **Register of charges [s271]**
- **Such accounting and other records as will correctly explain the transactions and financial position of the company and enable true and fair accounts to be prepared. [s2891**
- **Register of debenture holders, if any [s2I6D]**
- **Register of holders of prescribed interests, if any [s1070]**

DUTIES OF COMPANY DIRECTORS

Every company must have directors. At least one is needed for a proprietary company and three for a public company. The company must supply the names and other personal details of directors to the ASC for inclusion on the public database, at the time the company is first registered and when there are changes of directors.

Directors are needed to ensure that specific individuals take responsibility for the management and direction of companies, and for such matters as seeing that books of account are properly maintained. It is common for the Articles of Association of a company (that is the company's rules) to give control of many aspects of the company's business to its directors. The tasks of directors are usually very different in the case of a smaller (usually proprietary) company than in the case of a larger (usually public) company.

In a proprietary company, directors are often involved in all aspects of the running of the company's business, including:

- **Buying or leasing trading premises**
- **Arranging for bank or other finance to enable the company's business to be carried on.**
- **Ordering goods and services**
- **Operating retail outlets**
- **Making sure the company's accounts are prepared property**
- **Paying suppliers.**
- **Seeing to the preparation of tax returns.**

In a larger company, expert employees carry out many of the tasks which the directors of a proprietary company may handle. Directors of larger companies, some of whom may be appointed from outside the company, are more involved with matters such as:

- **The appointment of executives**
- **Maintaining good industrial relations with the company's workers long-term business and financial planning.**
- **Looking at the overall performance of the company and its different divisions.**
- **Deciding whether the company should be moving into different types of business undertakings.**
- **Determining what part of the company's profits should be distributed to shareholders in the form of dividends.**
-

WHO CAN BECOME A COMPANY DIRECTOR?

Only persons 18 years of age or older can be appointed company

directors. In a public company, unless certain steps are taken by the company, a person cannot act as a director after reaching the age of 72. The following people must not manage a company (which includes acting as a director) unless they have the consent of the Federal Court or the Supreme Court of a State or Territory:

- **Insolvents under administration (those who have either been declared bankrupt or have entered into an arrangement under Part X of the *Bankruptcy Act*).**
- **Those who have been convicted of an offence against any law in connection with the promotion, formation or management of a company or other body corporate serious fraud (punishable by imprisonment for at least three months).**
- **An offence against certain provisions of the Law, including breaches of duties of directors and other officers [s232] and insolvent trading [s588G].**

Those convicted must not manage a corporation within 5 years of conviction or, if imprisoned for one of these offences, within 5 years after release from prison. The Court can also order a person not to manage any company, for such period as the Court thinks fit, if the person:

- **Has repeatedly breached taws relating to the running of companies**
- **Was a director or other officer of a company that repeatedly breached these laws and the person failed to take reasonable steps to prevent the company breaching these laws.**

A COMPANY IS A SEPARATE LEGAL PERSON TO WHICH DUTIES ARE OWED

A very important rule of company law, too often overlooked, is that a company is a separate legal "person" to which duties are owed by its directors and other officers, regardless of the personal taxation or business reasons for its establishment. In relation to some matters, such as the use of money and other property of a company, the law takes a very strict approach. The duties owed by directors and other officers are viewed as virtually the same as the duties owed by a trustee of the estate of a deceased person.

While the test applied by the Law in other situations, for instance in deciding the correctness of the day to day business decisions of a company, may not appear to be as strict, it must be remembered that in every situation directors and other officers are expected to have regard to the best interests of their company rather than to their own personal interest or advancement.

THE DUTIES OF DIRECTORS TO THEIR COMPANY

The general duties of company directors, and other company officers, are to act honestly, exercise care and diligence, not use inside information and not make improper use of information or their positions [s232]. A director shall at all times act honestly in the exercise of their powers and the discharge of the duties of their office [s232(2)]. The duty to act honestly is an aspect of the principle that directors, as *fiduciaries*, must act with the utmost good faith towards the companies with which they are associated.

The clearest cases of breach of the duty of honesty are those involving theft or other misuse of a company's property, actions that are viewed very seriously by the Law. The reason for this strict view of directors' duties arises from the privilege of *limited liability* that is given to company shareholders. If a company fails, leaving debts

owing to outsiders, the only property available to meet those debts in most circumstances are the company's assets plus any money that remains unpaid on the company's shares. Usually, this is the limit on the liability of the company's shareholders.

The amount of any company property wrongfully taken or used by directors reduces the property available to meet the claims of creditors if the company fails. Therefore, the Law protects creditors by requiring company directors to observe strict standards of behaviour. Breach of duty to act honestly covers more than outright dishonesty, such as theft of property belonging to a company or fraud. Directors who, without any intent to defraud, take a decision knowing that it cannot be in the overall best interests of a company would not act honestly.

In the exercise of their powers and the discharge of their duties, a director or other officer of a company must exercise the degree of care and diligence that a *reasonable person* in a similar position in a company would exercise in similar circumstances [s232(4)].

It is difficult to lay down a precise test as to what sort of care and diligence is expected from every director, as much will depend on the size of the company, the nature of its business operations, the types of persons who make up the board of directors, etc. However, in one recent case the Court said directors had to take reasonable steps to be in a position to monitor the company's management, to gain at least a general understanding of the business of the company, and how this might be affected by changing economic circumstances.

IN EVERY CASE A DIRECTOR SHOULD

- **Obtain ongoing information about their**
- **company's operations.**
- **Take an active part in Board meetings**
- **Question the impact on their company's business performance of any proposal (particularly one involving a substantial financial commitment).**
- **Seek outside professional advice when they do not have sufficient information to properly allow them to make an informed decision about any matter that comes before the board of directors for decision.**

Directors cannot simply agree to proposals put forward by other directors without obtaining some information about the effect of these proposals on the company's business. Nor can they allow themselves to remain uninformed about the state of their company's business. They cannot satisfy themselves that any decision is truly in the overall best interests of their company if they are just "rubber-stamps" for various proposals - *Morley's* case. The Courts can look at the special skills or education of a particular director when deciding whether that director has met the required level of care and diligence.

DUTIES RELATING TO THE USE OF INFORMATION OR POSITION

A director must not make improper use of information gained through their position to gain, directly or indirectly, an advantage for

themselves or for any other person, or to cause detriment to the company [s232(5)]. The Courts have held that this information need not be confidential. It is a question of how the information is used. A director must not make improper use of his or her position to gain, directly or indirectly, an advantage for themselves or for any other person, or to cause detriment to the company [s232(6)].
Where directors have personal interests that might give rise to conflicts of interest with their duties as directors, the nature of these interests must be disclosed at a directors' meeting [s231].

KEEPING PROPER BOOKS AND RECORDS
The Law sets out many requirements for the setting up and maintenance of registers and other company records. One obligation [s289] important for directors is the requirement that a company "keep such accounting records as correctly record and explain its transactions (including any transactions as trustee) and financial position". These records must be kept so that

- **"True and fair" accounts of the company can be prepared from time to time (at least annually).**
- **The accounts can be conveniently and properly audited in accordance with the provisions of the Law.**

FALSE OR MISLEADING STATEMENTS OR INFORMATION
Any person who makes or authorizes a statement which to their knowledge is false or materially misleading in a document required to be lodged with the ASC, is guilty of an offence. The offence includes making a document materially misleading by leaving something out [s1308]. It is also an offence not to take reasonable steps to ensure that the contents of a document lodged with the ASC are not in fact misleading [s1308]. A director or officer of a company who knowingly provides false or misleading information about the company's affairs to a director, auditor or shareholder of the company, is guilty of an offence [s1309].
The Company will also be liable under the Trade Practices Act (Part IV) and the local Fair Trade Act for any misleading or false advertising.

THINGS TO DO
About 500 words
Following on from the previous “works to be forwarded”; considering the agency you intend to establish how would you answer the following questions?

1. **Determine the relevant body in your state or territory that registers business names. Fill out the appropriate form for the name you intend to use.**
2. **Determine the relevant licensing body in your state or territory. What rules and regulations apply to registration of the business name and its display?**