

Foundation Studies

Business Environments

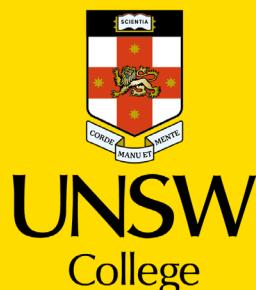
Part 2: The Legal Environment of Business

Unit 3

Choice of Business Structure

Lecturer:

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Overview

- Business law
- Unincorporated business organisations
 - Sole trader
 - Partnership
- Incorporated business structures
 - Company
 - Concept of separate legal entity
 - Concept of corporate veil
 - Lifting of the corporate veil

Cases in this unit

Salomon v Salomon & Co Ltd

Gilford Motor Co Ltd v Horne

Business Law

- Selected rules of law that are of particular relevance to business activities
- A set of rules to determine the rights, duties and obligations of people who are engaged in commercial activities

Choosing the Right Business Structure

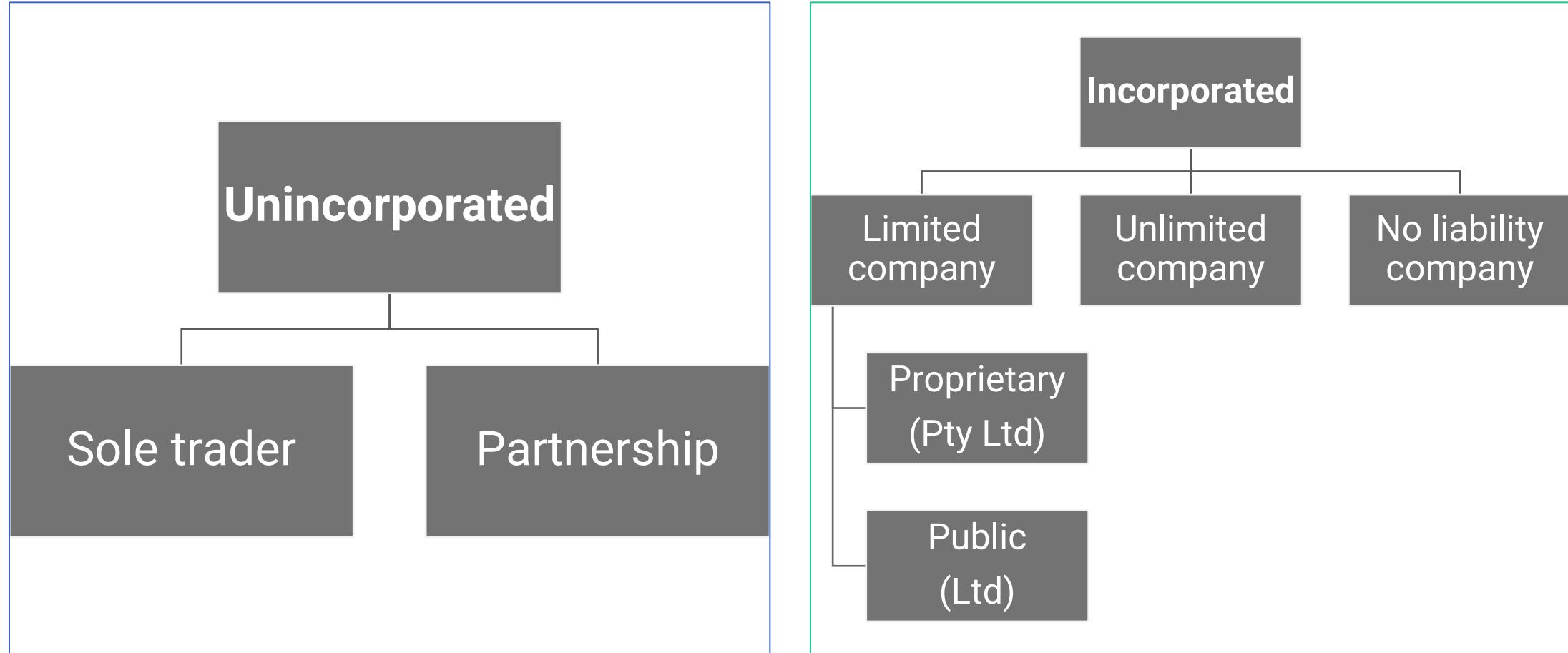
- When starting a business, selecting the appropriate structure is crucial for success.
- Each structure offers unique advantages and challenges that impact taxes, liability, and management.
- Key considerations for selecting a business structure:
 - Extent of liability
 - Taxation
 - Control and management
 - Regulatory requirements
 - Capital investment
 - Flexibility and future needs
 - Continuity
 - Decision-making
 - Compliance and record-keeping
- Considering these factors can help in making an informed decision about the most suitable business structure for specific needs and goals.

Forms of Business Structures

Numerous forms of structures available, including:

- Sole trader
- Partnership
- Company

Choice of Business Structures



Unincorporated Business Structures



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Sole Trader

- A person carrying on a business as an independent individual
- Easy to establish and run (lack of formalities)
- Owns and has full control of the business
- No disclosure requirements
- Access to limited resources/finance
- Risk of personal liability (unlimited liability)
- Liable for payment of tax (progressive tax rates)
- Business ends with the death of the sole trader

Partnership

- Exists between persons carrying on a business in common with a view to profit.
- Governed by *Partnership Act*
- Maximum of 20 partners
- Easy to establish (contractual arrangement between partners)
 - Partners may provide an ongoing source of funds
- Control is divided between partners
- Not a separate legal entity (See Slide 16)
- Risk of personal/joint liability
- Income splitting (progressive tax rates)
- No disclosure requirements
- Partnership ends with the introduction/exit of a partner

Incorporated Business Structures



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Company

- An association of persons who satisfy *Corporations Act 2001* (Cth) for registration
- Formalities: Created through the process of **registration (incorporation)**
 - Incorporation: Legal process of registering your structure to form a company under the *Corporation Act* with ASIC
- Separate legal entity (See Slide 15)
- Members of a limited company have limited liability
- Management is separated from ownership
- Taxed at a flat rate
- Perpetual succession

201 Application for registration as an Australian company



Form 201

Description Application for registration as an Australian company

Note: From October 2019, Australian company registrations must be completed online. The paper Form 201 is no longer available.

You can register a company online using the Business Registration Service (BRS) or a Private service provider (PSP).

A small number of customers may experience issues when trying to register certain company types online. Visit our [web page](#) for more information.

Purpose Register a new Australian company

Applicable Fees 201A ~ Public company - with share capital \$597

201B ~ Public company limited by guarantee \$491

201C ~ Proprietary company \$597

[Picture Source](#)

Proprietary and Public Companies

Proprietary company

- Maximum 50 shareholders
- Most suitable for use by a small business
- Restricted fundraising ability
- Less regulatory burdens than public companies
- Financial secrecy for small proprietary companies

Public company

- May be listed on ASX
- Raise funds from the public
- Subject to financial disclosure and more regulation

Legal Effects of Incorporation

- Upon the incorporation of a company, it becomes a separate legal entity, separate from its members and controllers
 - Company is a legal person

Legal Effects of Incorporation

- Legal consequences flowing from the separate legal entity principle:
- The company:
 - can confer limited liability on its members
 - can enter into contract with their members, directors and outsiders in its own corporate name
 - can acquire, hold and dispose of property in its own corporate name
 - may sue or be sued in its own corporate name
 - has perpetual succession (it may exist forever in its own right, even as the members of the association change)

Company as a Separate Legal Entity

Salomon v Salomon & Co Ltd [1897] AC 22

Facts

- Mr Salomon:
 - major shareholder, director and creditor
- Company's business failed; value of assets were insufficient to pay both Mr Salomon and company's other creditors

Company as a Separate Legal Entity

Salomon v Salomon & Co Ltd [1897] AC 22

Issue

- Was Mr Salomon personally liable for debt owed to Broderip?

Held

- No. Upon the incorporation of a company, it becomes a separate legal entity from its founders, directors, members and controllers

Corporation Veil

- The artificial screen that separates legal identity of company from its members/directors
 - Protects directors and owners from the company debts/liabilities
 - founded on the separate legal entity principle

The Corporate Veil



Source: Anil Hargovan, et al. *Australian Corporate Law*. LexisNexis, 2023.

Lifting the Corporate Veil

- Courts are prepared to lift/pierce (disregard) the corporate veil in special and limited circumstances
- Courts may look behind the corporate veil to determine why the company was formed

Lifting the Corporate Veil

Avoidance of legal obligation

- Attempts by the owner to deliberately use the company to [avoid legal/contractual obligations](#) undertaken by them
- Corporate veil lifted to enforce legal/contractual obligations

Lifting the Corporate Veil

Gilford Motor Co Ltd v Horne [1933] 1 Ch 935

Facts

- Horne signed an employment contract with GMC promising not to take its customers when he leaves GMC
- Horne resigned and set up a company which targeted GMC's customers

Lifting the Corporate Veil

Gilford Motor Co Ltd v Horne [1933] 1 Ch 935

Held

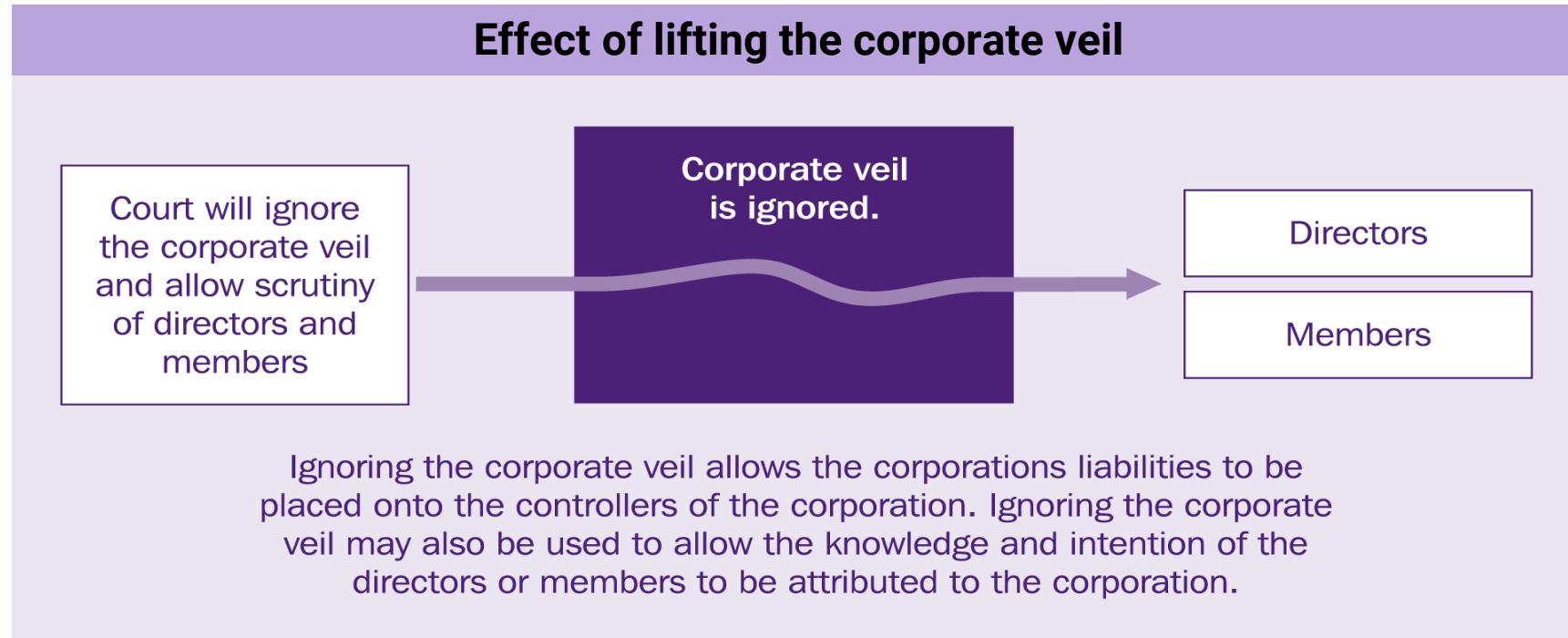
- Horne misused the corporate personality to avoid obligations under his employment contract when he left GMC
- Corporate veil lifted

Lifting the Corporate Veil

Effects of lifting the corporate veil

- No distinction between identity of company and identities of owners/directors
- Forces personal liability for debts of company onto owners/directors

Lifting the Corporate Veil



Source: Anil Hargovan, et al. *Australian Corporate Law*. LexisNexis, 2023.

End of Lecture

Next week:
The Legal Environment of Business: Contract Law (I)



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