

LEGAL PROFESSION ADMISSION BOARD

MARCH 2014

LAW OF ASSOCIATIONS

Time: Three Hours This paper consists of **six** questions.

Candidates are required to attempt any **four** questions.

No question is compulsory.

All questions are of equal value.

If a candidate answers more than the specified number of questions, only the first **four** questions attempted will be marked.

All questions may be answered in one examination booklet.

Each page of each answer must be numbered with the appropriate question number.

Candidates must indicate which questions they have answered on the front cover of the first examination booklet.

Candidates must write their answers clearly. Lack of legibility may lead to a delay in the candidate's results being given and could, in some circumstances, result in the candidate receiving a fail grade.

This examination is worth 80% of the total marks in this subject.

Permitted Materials: This is an open book examination. Candidates may refer to any books and any printed or handwritten material they have brought into the examination room.

As some instances of cheating, plagiarism and of bringing unauthorised material into the examination room have come to the attention of the Admission Board, candidates are warned that such conduct will result in instant expulsion from the examination and may result in exclusion from all further examinations.

This examination should not be relied on as a guide to the form or content of future examinations in this subject.

Question 1

The Eastern Suburbs Cyclists Association was established in early 2012 as an unincorporated association (“**Association**”). At the time of its establishment the members of the Association elected a committee of three persons, namely Angela, Tom and David. Under the Association’s constitution committee members are elected every two years.

After being elected as committee members, Angela, Tom and David executed a lease, as committee members of the Association, for a hall owned by Quentin Properties Pty Limited (“**Quentin**”). The term of the lease was for four years. The hall was used by the Association for all of its administrative activities as well as for social functions conducted by the Association.

Two years after commencement of the lease Ben, Sue and Mario were elected as committee members to the Association replacing Angela, Tom and David. After his election Mario convinced Ben and Sue that the Association ought to move from the existing leased premises from Quentin and move to another hall owned by Mario’s uncle. Ben and Sue agreed. Shortly thereafter Ben, Sue and Mario execute a new lease, as committee members of the Association, over the hall owned by Mario’s uncle and gave notice to Quentin purporting to terminate the lease with Quentin. There was two years left on the existing lease with Quentin.

Quentin wants to commence proceedings for breach of lease against the Association and/or against Angela, Tom and David as the committee members who executed the lease with Quentin and/or against Ben, Sue and Mario as the committee members who terminated the lease with Quentin.

Advise Quentin. Would your answer be different if the Association was incorporated under the *Associations Incorporation Act 2009 (NSW)*? Give reasons.

(20 marks)

Question 2

Paul is the holder of the Governing Director’s share in a family manufacturing company which was incorporated in 2005 (“**Company**”). At the time of incorporation the other shareholders in the Company were Paul’s wife, Mavis who held three “B” class shares and Paul and Mavis’ sons, Peter, Clive and Don, who each held one “B” class share each in the Company. Peter, Clive and Don worked in the Company on a full time basis.

Pursuant to the constitution of the Company Paul, as holder of the Governing Director’s share in the Company, had vested in him “all powers and authorities and discretion vested in the board of directors”. Paul, therefore, had complete control of the Company. Upon Paul’s death his Governing Director’s share would convert to a “B” class share.

Pursuant to the constitution, whilst Paul remained the Governing Director, Mavis and Peter, Clive and Don as holders of “B” class shares had no voting rights. However the constitution provided that after the death of Paul the “B” class shares would carry voting rights.

(Question 2 continues)

(Question 2 continued)

Mavis died in 2012, leaving her three “B” shares in the Company to her three sons. Shortly thereafter Paul formed a friendship with Cleo. Eventually Paul and Cleo married and Cleo moved into the family home. Peter, Clive and Don did not get on with Cleo whom they regarded as an opportunist and this view was reinforced when Paul advised his sons that he proposed to issue a special category of shares to Cleo which would give her control over the Company upon Paul’s death. Cleo neither had experience nor qualifications in the manufacturing industry.

In January 2014 Paul as Governing Director issued the special category of shares to Cleo giving her control of the Company upon his death. The effect of the issue of the special category of shares to Cleo therefore was to dilute the voting power of the “B” class shares upon Paul’s death.

Advise Peter, Clive and Don on whether Paul, by issuing the special category of shares to Cleo, breached his duty to the Company pursuant to section 181 of the *Corporations Act*. Give reasons having regard to the relevant authorities.

(20 marks)

Question 3

Molly and Anthony are shareholders in Wall Furniture Pty Limited (“**Company**”), a furniture manufacturing company in North Sydney. The other shareholders in the Company are Sue, Julia and Oliver. Each shareholder holds one ordinary share in the Company. The directors of the Company are Sue, Julia and Oliver.

In June 2012 Sue, Julia and Oliver incorporated another company called Furniture On the Run Pty Limited (“**Furniture on the Run**”).

In the period July 2013 to January 2014 the Company received numerous furniture orders from customers. In many cases Sue, Julia and Oliver diverted those orders to Furniture on the Run rather than having the orders filled by the Company. This resulted in a loss of profit to the Company.

Molly and Anthony were previously unaware that Sue, Julia and Oliver were diverting orders from the Company to Furniture on the Run. Molly and Anthony approached Sue, Julia and Oliver for an account of profits owed to the Company for the diversion of Company orders to Furniture on the Run. Sue, Julia and Oliver refuse.

Molly and Anthony now seek your advice as to whether they can apply to the Court to bring proceedings on behalf of the Company against Furniture on the Run and against Sue, Julia and Oliver for an account of profits. In your answer you should refer to the procedure involved and to the criteria that needs to be satisfied pursuant to section 237 of the *Corporations Act*.

(20 marks)

(Question 4 follows)

Question 4

Computer Data Pty Limited (“**Company**”) carries on business as a computer data service provider. There are four shareholders in the Company who hold the following number of shares: Christine has 10 ordinary shares, Frank has 2 ordinary shares, Robert and Julian have 1 ordinary share each. At the time that each member acquired shares in the Company it was understood that they would each be equally involved in the management of the Company. Christine, Frank, Robert and Julian are also the Company’s only directors.

From the time that the Company commenced operation, Christine began conducting the business of the Company as if it were her own, effectively excluding Frank, Robert and Julian from the management of the Company. Christine refuses to conduct meetings when requested and when meetings are eventually held Christine refuses to consider any proposed resolution by the other directors/shareholders. Christine pays herself a very high remuneration for consulting work she says she does for the Company. The other directors/shareholders regard this remuneration as excessive and not commensurate with the work she does or the skill that she possesses. Christine takes the view that she is entitled to be paid as much as the Company can bear.

In addition, Christine refuses to approve the payment of dividends despite the Company making profits. This has had the effect that neither Frank, Robert or Julian have received any profit distribution from the Company.

Advise Frank, Robert and Julian on whether they can bring an action against Christine pursuant to section 232 of the *Corporations Act* and, if so, what orders would you advise them to seek. Give reasons.

(20 marks)

Question 5

Max and Lucy are the sole directors and shareholders of the family business conducted by Queensland Flights Pty Limited (“**Company**”). The Company conducts the business of providing an aerial courier service in Queensland. Max and Lucy are married and Lucy is the Managing Director of the Company and has de facto control of the Company.

The Company owns two very large aircraft valued at approximately \$1 million (“**Company aircraft**”). In October 2013 Lucy, purporting to act on behalf of the Company, met with Matthew, an officer of Moneybank Pty Limited (“**Bank**”) with a view to obtaining a loan for the Company of \$800,000 using the Company’s aircraft as security. Lucy tells Matthew that the funds were needed to make improvements in the Company business.

In order to facilitate the loan Matthew gave Lucy an application form to complete. Lucy completed the application form and signed it as a director of the Company. Lucy also forged the signature of Max as director on the application form. The application form was then posted back to Matthew. Max was unaware of the loan application and was unaware that his name had been forged on the application form.

(Question 5 continues)

(Question 5 continued)

After receiving the completed application form from Lucy, Matthew undertook ASIC searches of the Company. Those searches revealed that both Lucy and Max were the only directors and shareholders of the Company. With that information Matthew decided not to inquire any further as to the authority of Lucy to act on behalf of the Company or as to whether Max knew of the loan application. In addition, Matthew undertook finance related searches in relation to the Company's aircraft which revealed that they were owned by the Company.

In November 2013 Matthew telephoned Lucy and informed her that the loan application had been approved by the Bank and that all that remained to be done was for the Company to execute security documentation over the Company's aircraft. Upon receipt of the security documentation, Lucy immediately affixed her signature as a director of the Company and again forged the signature of Max describing him as "secretary" for the Company. Max was unaware of the security documentation or that his name had been forged on the security documentation. Max was not the secretary of the Company but only a director and that fact was revealed by the ASIC search that Matthew had previously undertaken.

When time for payment of the loan funds occurred, Lucy told Matthew that notwithstanding that the loan was in the Company's name, the loan funds should be made out to her personally and not to the Company. Upon receiving this request Matthew became suspicious and when he looked at the executed security documentation he noticed that the purported signature of Max on that document differed slightly from the purported signature of Max that was contained on the application form. Despite his suspicions Matthew made no further inquiries.

In November 2013 Lucy received a cheque made to her personally for \$800,000. After receiving the \$800,000 she ran off with one of the pilots never to be seen again. The loan moneys of \$800,000 have not been repaid. In January 2014 the Bank commenced proceedings to take possession of the Company's aircraft.

Advise Max whether he could succeed in having the loan and the security documentation over the Company's aircraft set aside. Give reasons for your answer. You should have regard to the *Corporations Act* and the relevant case law.

(20 marks)

(Question 6 follows)

Question 6

The Finished Timber Company Pty Limited (in liq) ("**Company**") was wound up in December 2013. Kevin and Robert were the Company's directors since incorporation. Mrs Thompson was the Company's financial officer, but she was not a director of the Company. Despite her title Mrs Thompson had no formal financial qualifications.

The liquidator of the Company now seeks to recover from Kevin and Robert the amount equivalent to the amount owing to the unsecured creditors of the Company on the basis that at the time the debts were incurred the Company was insolvent or became insolvent by reason of incurring the debts.

Both Kevin and Robert believe that at the time of incurring the debts to the unsecured creditors the Company was not insolvent but rather was experiencing a temporary illiquidity and that they expected on reasonable grounds that:

- (a) the Company would have been able to conclude negotiations with a very large building organisation for the purchase of the Company's timber products, which would have increased the Company's income substantially; and
- (b) the debts incurred and which would continue to be incurred by the Company could have been paid by recourse to the assets of the Company and both Kevin and Robert were reasonably certain that those assets could have been realised within a 90 day period.

Further, Kevin and Robert state that throughout the relevant period they were advised by Mrs Thompson that the Company was solvent and was able to meet its obligations because most of the creditors did not press for payment within their normal trading terms and because there was an understanding that the creditors would not take recovery action against the Company provided that the Company paid within a reasonable time after 30 days notice was given. Mrs Thompson says however that she was never asked to monitor solvency and that her job was more akin to being a bookkeeper and that she did what she was told by Kevin and Robert.

Advise Kevin and Robert of their prospects of resisting the liquidator's action. Your answer should include an analysis of the essential elements that are necessary to be shown for the liquidator to be successful and an analysis of any statutory defences that Kevin and Robert may have to any such application.

(20 marks)

END OF PAPER