Part 1

Registering a No Liability Company

A no liability company is a public company that is limited by shares.[1] As per s.112(2) of the Corporations Act, 2001, a company is eligible to be registered as a no liability company only if it fulfills the following essentials:

1. it has a share capital
2. the constitution states that its sole purpose is mining[2], and
3. it does not have a contractual right to recover calls made on its shares from defaulters.

A body corporate that has not yet been registered as a company also needs to fulfill the aforementioned criteria in order to register itself as a no liability company.[3] The rules pertaining to its registration are enshrined mainly under s. 117-123, 136(1), 148, 152, 156, 162, 254B, 601BA. Following are the steps that a company must undertake in order to register itself as a no liability company:

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1. Reserving a Company Name

Part 2B.6 of the Act pertains to the general rules of use of company names. As per s.148, a company may register itself under a company name, or operate under its ACN, i.e. its Australian Company Number, which is generated by the ASIC upon registration.[4] Even though it is not mandatory, a company name is generally preferred in order to confer an identity to it and to distinguish from other companies. The company name must also include the words "No Liability" or "NL" at the end of its name to notify the public the nature of its organization.

2. Members and Obtaining Consents

It is up to the incorporators to determine whether the company shall be following the replaceable rules as enlisted in the Corporations Act, or draft its own rules as constitution. As per s. 136(1), if the latter is decided to be done, all members of the company at the time of its registration are to agree to the constitution in writing and give their consent.

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[1] Section 112(1) of the Act
[2] For the purpose of section 112(2), 'Mining' and 'Minerals' have been defined under section 9, Corporations Act.
[3] Section 601BA of the Act
[4] Tomasic, R., Bottomley, S. & McQueen R. (2002) *Corporations Law in Australia*, Federation Press: Australia.

Since a no liability company, in essence, is a public company, it is required to have at least one secretary[5] and a minimum of three directors[6]. Consent forms are also required of the persons who are to act in their respective positions, i.e. a director will give consent to act in the capacity of a director, a member shall give consent to act in the capacity of a member, etc.[7]

Since a no liability company also has a share capital, its members are also required to consent to take up a specified number of shares at the time of registration and to pay the amount owed by them in respect of the shares.

3. *Application to ASIC*

In order to reserve a name for the no liability company, Form 201 is to be sent as an application to the ASIC.[8] The rules pertaining to the application have been enshrined under s.117, which requires the application to:

- State the company is a no-liability company
- Provide details of
  - company name
  - address of the company office that is proposed to be registered
  - names and addresses of its members, directors and company secretary
- Declare the share capital, including the number of shares being issued to members and the amount they have consented to pay.

The company would also be required to attach a copy of its constitution with the application.

4. *Registration by ASIC*

The ASIC will review the application made by the company and choose to register it under the name or an ACN if it deems that the company fulfills all the aforementioned requirements. It may then issue a certificate of registration to the no liability company,[9] which would bear all the

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[5] Section 204A
[6] Section 221
[7] Section 120
[8] Section 152
[9] Section 118

necessary details pertaining to the company. Once registered, the company name or the ACN will be borne on all its public documents and negotiable instruments.[10]

As per 1274(7A), the certificate acts as conclusive proof that it has fulfilled the necessary conditions and is a registered entity. However, the ASIC is not bound by this section as it may challenge the validity of the certificate issued to a no liability company upon reasonable grounds.[11]

Part 2

Doctrine of Capital Maintenance

The doctrine of capital maintenance propounds that a company should not repay its shareholders from its undistributed profits, as their position falls below that of the creditors.[12] The doctrine is based on the logic that creditors only provide credit to the company for ordinary commercial transactions, and thus, their position must supersede that of the shareholders. This doctrine is intended for the protection of creditors, proper application of share capital, prevention of fraud and selective distribution of dividends etc.[13]

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The doctrine was developed by means of precedents, wherein the English cases of *Flitcrofts* case[14] and *Trevor v Whitworth*[15] are the most crucial. While in *Flitcrofts,* it was considered to be the creditors' right to "see that the capital is not dissipated unlawfully" and the members were not returned the capital "surreptitiously", in the latter case, the buyback of shares by the company was held to be *ultra vires.* Further, in *Aveling Barford Ltd. V. Perion Ltd.*[16], shareholders were held to have the right upon the capital only after the creditors of the company were paid. The principles stated in these cases were subsequently included in the statutory provisions of various countries, including Australia, UK, US, New Zealand, Hong Kong, etc.

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[10] Section 153.
[11] *ASC v SIB Resources NL* (1991) 9 ACLC 1147
[12] Norton Rose Fulbright (September 2008) *Capital Maintenance - the Companies Act 2006, Retrieved from* http://www.nortonrosefulbright.com/knowledge/publications/17080/capital-maintenancethe-companies-act-2006
[13] Islam, M.D. (2013) *The Doctrine of Capital Maintenance and its Statutory Developments: An Analysis,* The Northern University Journal of Law, Vol. IV: Northern University: Bangaldesh.
[14] (1882) 21 Ch. D. 519
[15] (1887) 12 App. Cas. 409
[16] (1989) BCLC 626; Also see *Redweaver Investments Ltd v Lawrence Field Ltd,* (1991) 9 ACLC 1032.

Thus, subject to certain exceptions, the application of the doctrine provides:[17]

1. A company cannot buy back its own shares unless it follows strict procedures laid down by the Act.
2. A subsidiary company cannot be a member of its holding company.
3. A company is not permitted to provide financial assistance to persons who are acquiring its shares.
4. The shareholders can only receive dividends from its distributive profits.

As noble as its intent is, the doctrine is losing its relevance in the contemporary corporate world and has been a subject of a much generated debate. Rules pertaining to capital maintenance have been reformed, and a variety of tests (such as solvency, fairness and disclosure) are applied to ascertain the capital decisions. United States and New Zealand have scraped off the doctrine, and apply a general solvency test wherein the shareholders are entitled to distribution during the solvency of the company, and creditors do not get a first preference.[18] In India, companies are permitted to reduce their share capital after passing a resolution and by obtaining a court order.[19] In the UK itself, shares were permitted to be classified as 'redeemable' or capable of being bought back by the company in the year 1980.[20]

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These progressive reforms have now been adopted by Australia. The Corporations Act requires the directors of the company to fulfill the solvency, fairness and disclosure tests[21] before distributing dividends to shareholders, reducing the share capital, buying its own shares, or providing financial assistance to persons acquiring its shares during the solvency of the company[22]. The company needs to mandatorily be solvent to take such decisions, or else it will attract penalty under s588G pertaining to insolvent trading wherein the directors will be held personally liable.

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[17] Morse. G & Charlesworth J. (1991) *Charlesworth and Morse: Company Law*, ed. 14, ELBS.
[18] Islam, M.D. (2013) *The Doctrine of Capital Maintenance and its Statutory Developments: An Analysis,* The Northern University Journal of Law, Vol. IV: Northern University, Bangladesh.
[19] Sections 100-105, Companies Act, 1956
[20] Sections 684-723, Companies Act 2006
[21] Tomasic, R. (2015) *The Rise and Fall of the Capital Maintenance Doctrine in Australian Corporate Law,* International Company and Commercial Law Review, 26(5) 174-187, University of South Australia.
[22] Sections 257A-257J, Corporations Act 2001

The doctrine of capital maintenance had been struck down by Corporation Act. The doctrine has been argued to be of 'no use' to the creditors[23], is outdated and meritless, as the exceptions that it bears supersede it. Further, the logic provided is fallible as, in practice, creditors do not rely on the share capital to recover their debts and usually enter into contractual agreements with the company to protect their own rights. Thus, the doctrine is irrelevant in the Australian context.

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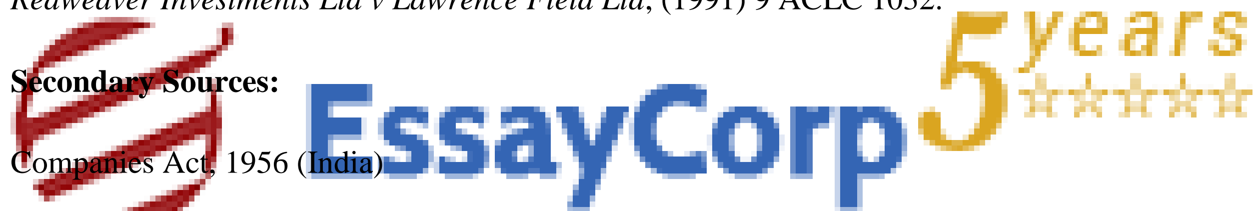

[23] Companies and Securities Law Review Committee (June 1986) *A Company's Purchase of its Own Shares,* Discussion Paper No. 5.

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