



## MEMO

To: Board of Directors  
From: Company Secretary  
Subject: **WHY FORM A COMPANY**

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As the proposed directors of “Zodiac Signs” you have asked me to explain, in simple terms, why you should form a company through which to operate the business.

The principal advantages/characteristics of using a company for your business – rather than just running it under a business name – include:

1. It is a separate legal entity, which is distinct from its shareholders, directors and other individuals connected to the company. It has its own rights and obligations.
2. It has perpetual succession – so it goes on ‘forever’.
3. It has shareholders who own the company – and their liability is protected; they have personal asset protection. Forming a company to undertake a business venture, own assets, or incur liabilities, is the principal way that a person can limit their personal liability – and protect their own assets – to the amount that they invest in the company’s shares (and/or are contracted to contribute if partly-paid shares).
4. It has a board of directors who manage the company (on behalf of the shareholders). A company is managed by directors who are appointed to represent the shareholders. Directors must remember to always act for the benefit of the company and not themselves. In fact, the Corporations Act lays down very strict guidelines in relation to directors’ actions, duties and powers and to try and minimize any conflict of interest.
5. Shareholders are not liable for the company’s debts, commitments and any other obligations. In contrast to shareholders, directors may become personally liable for a company’s debts if they continue to let it trade when they know it may be unable to pay those debts as and when they fall due (insolvent trading). A director may also be liable if the company suffers losses resulting from a breach of certain director’s duties.
6. Shareholders have little real say in running a company and making decisions. However, the law allows them to influence decisions for a company by meeting and voting on matters, subject of course to following the rules for calling and holding meetings and passing resolutions.
7. It has the power to acquire, hold, own and dispose of property and other assets in its own name.



8. It probably has better access to larger amounts of capital for running the business. It can also pledge or mortgage its assets as security in support of borrowings, etc.

8. It can enter into contracts in its own right – although people (the company's directors/officers) must sign on its behalf

9. It can sue, and be sued. It can initiate and take action against others to recover debts, damages, etc.

10. It has to keep its own accounting records, prepare financial statements, lodge tax returns, GST, PAYG, superannuation, etc – all separate from the affairs of its shareholders and/or directors. Another reason for using a company structure is because the company tax rate is a maximum 30%, whereas the personal tax rate of a shareholder may be much higher.

11. It is generally more expensive to run a company; there is more administration and a more strenuous reporting / regulatory regime to comply with and manage.

12. The name (used as the company's name) is largely protected throughout Australia (i.e., generally speaking, no-one else can have/use the same name – unless they already have some sort of 'rights' to the name and may take action if they believe you are infringing on their name/business) – whereas just registering a business name, for example, generally only provides protection within the state.

## **Corporations Act**

Chapter 2B of the Act sets out the basic features of a company, with Sections 124 ~ 127 detailing company powers and how they are exercised. Specifically, these cover:

- legal capacity
- constitutional restrictions
- agents and contracts
- execution of documents and deeds.

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### **DISCLAIMER**

*The comments in this memo reflect some commercial aspects and observations on the matter experienced or observed by the writer in practice as he understands them. The information is given as a guide only and does not represent a definitive or legal view of any of the issues raised, covered or referred to and the reader is urged to seek his own professional advice on all aspects of, or pertaining to, this and any related matter.*

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