Fall 23

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ESTABLISHING A BUSINESS ENTITY IN AUSTRALIA

ILN CORPORATE GROUP

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ESTABLISHING A BUSINESS ENTITY IN AUSTRALIA

"Establishing a Business Entity in Australia"
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TYPES OF BUSINESS ENTITIES

There are a number of business structures to choose from when starting a new business venture in Australia. Investors need to determine which form of business organisation is the most appropriate for their requirements.

The main types of business structures used by investors in Australia are:

- companies, including branch offices of foreign companies;
- partnerships;
- joint ventures; and
- trusts.

Each particular structure has advantages and disadvantages. Therefore, specific legal and accounting advice should be obtained before deciding upon the most appropriate investment vehicle.

Company

All Australian companies are regulated by the *Corporations Act 2001* (Cth) (**Corporations Act**).

A foreign investor can register an Australian company under the Corporations Act. The "limited liability" company is the most common business structure used by foreign investors in Australia.

A company is its own legal entity and has the same rights and obligations as an individual person. This means that a company can incur debt, can sue and be sued, is taxed as a separate legal entity and must file its own tax return.

A significant benefit in choosing a company structure is that the liability of the owners of the company (the shareholders) to third parties is generally limited to the amount (if any), which is unpaid on their shares.

The most common company types are public companies and proprietary (or private) companies. A proprietary company is generally simpler and less expensive to administer than a public company because it is subject to fewer administrative requirements imposed by the Corporations Act.

(a) Proprietary company limited by shares ("Pty Ltd")

This is the most common form of corporate business entity in Australia. The company is incorporated with share capital which is owned by the shareholders. The liability of the shareholders is limited to the amount which is unpaid on their shares.

Pty Ltd companies:

- must have at least one, but no more than 50, non- employee shareholders;
- must have at least one director residing in Australia;
- must have a registered office in Australia;
- must have a public officer, who is responsible for complying with the tax obligations of the company and dealing with the Australian tax authorities;
- may have a company secretary, but does not need to; and

- have fewer fundraising options available, compared to a public company.

Pty Ltd companies are further divided into "large proprietary" and "small proprietary" companies.

The Corporations Act sets out certain tests to determine whether a company is a "large proprietary" or a "small proprietary" company, including consolidated revenue thresholds and the number of employees of the company (and any other entity it controls).

There are less disclosure requirements imposed on a small proprietary company, including that its financial reports do not need to be audited.

(b) Public company (Limited)

Public companies involve ownership by the public and they are not restricted by the same limitations that apply to Pty Ltd companies. A public company is able to raise capital directly from the public by offering shares and other securities. Subject to certain requirements as set out in the 'ASX Listing Rules', public companies may also apply for listing on the Australian Securities Exchange in order to get access to capital markets.

Public companies:

- must have at least one shareholder with no upper limits on the number of shareholders;
- must have at least three directors (not including alternate directors), two of whom must ordinarily reside in Australia;
- must have at least one secretary, who ordinarily resides in Australia;
- must have an auditor, and such auditor must be appointed within 1 month after the day that the company was registered;
- must have a public officer for tax purposes;
- must have a registered office in Australia that is open each business day for at least 3 hours between 9am and 5pm; and
- may raise capital by issuing a disclosure document to offer shares and other securities to the public/potential investors.

Establishing a Pty Ltd company

The process for incorporating a Pty Ltd company in Australia is relatively straightforward and inexpensive. It is also a relatively quick process - subject to all relevant information being provided, a company can be registered in a matter of days.

(c) Choose a company name

Before registering a company, the owners must choose the name for the company. The appropriate searches should be conducted to ensure that the proposed company name is not identical or similar to another Australian company or business name, and that it does not infringe on the intellectual property rights of another entity.

If the company wishes to trade using a name that is different to the company's registered name, then it must register this name separately as a business name with ASIC. Appropriate searches should also be conducted to ensure the proposed business name is not similar to existing business names, company names or trade marks.

(d) Consider internal operations

Before registering the company, the owners will need to decide what the governance framework for the company will be. For example, how directors will be appointed and removed, the terms of issue for shares, the right of shareholders to receive dividends, and the process for transferring shares.

Usually, these governance issues are addressed in a document called a constitution. Sometimes, the constitution is also supplemented by an additional agreement entered into by the shareholders called a "shareholders agreement".

The constitution is usually adopted upon the registration of the company. If a constitution is not adopted upon the registration of the company, then the "replaceable rules" in the Corporations Act will apply. However, the "replaceable rules" do not cover all governance matters, so it is preferable for a company to adopt its own constitution upon registration.

(e) Registration

In Australia, a company is registered by using the Australian Government's Business Registration Service.

The application for registration must contain details of the following:

- the directors of the company (one of whom must reside in Australia);
- the "Director ID" number (also referred to as the DIN) for each director;
- the company secretary (if the company is to have one). has At least 1 secretary must reside in Australia;
- the shareholders of the company and the number of shares held by each shareholder;
- the address for the registered office of the company and its principal place of business;
- the amount paid by each shareholder for its shares;
- the proposed name of the company; and
- details of any ultimate holding company of the company.

Any constitution for the company must also be lodged.

Once registration is complete, the company will be issued an Australia Company Number (**ACN**). The company's name and ACN must be displayed on documents published by the company, and wherever the company conducts business.

Australian Branch

An overseas company wanting to carry on business in Australia must either incorporate a new company in Australia (refer above) or register itself as a foreign company with ASIC.

Registration of a branch office under the Corporations Act gives the overseas company the right to carry on business in Australia. The overseas company must comply with Australian law and is subject to certain reporting and disclosure requirements.

A foreign branch is not classified as a separate legal entity. Therefore, the overseas company will be liable for all of the debts and obligations of the Australian branch.

An Australian branch of a foreign company:

- is taxed as a separate entity in Australia, on all income sourced from Australia;
- must have a local agent who is responsible for the company's obligations in Australia and may be personally liable for breaches; and
- must have a registered office in Australia.

Choice of Australian Branch or Subsidiary

There are a number of factors to consider when deciding whether to establish an Australian branch or incorporate a new company in Australia as a subsidiary of a local parent company.

These factors include the following:

- a subsidiary is a separate legal entity from its parent company. It has limited liability, and the parent is not usually liable for the debts or obligations of the subsidiary. There are some exceptions to this, such as in the case of the insolvency of the subsidiary;
- an Australian branch of an overseas company is not a separate legal entity. Therefore, the overseas company will be liable for all debts and obligations of the Australian branch;
- the use of an Australian branch may cause practical difficulties when dealing with financiers. For example, if finance from an Australian financial institution is required, then that institution may require audited financial statements relating to the Australian operations of the applicant. This may not be readily available in an acceptable form in the case of an Australian branch;
- the use of a branch may also cause some difficulties when dealing with third parties. For example, they may need to be satisfied as to the nature of the foreign corporation's legal structure and the means by which it is able to bind itself to obligations in Australia; and
- the annual return of a branch office must include the worldwide financial accounts of the company of which it is a branch, unless exempted by ASIC. This document is available to the public.

Partnership

A partnership is an arrangement between two or more entities to carry on a business together with a view to a profit. Except for certain professional partnerships, business partnerships cannot have more than 20 partners.

A partnership is created by an agreement among the partners. Usually, this agreement is documented in a written partnership agreement. Partnerships are regulated by the terms of the partnership agreement (if there is one), the common law and the relevant Partnership Act which applies in the applicable state and territory.

A partnership is not a separate legal entity. Therefore, each partner is jointly and severally liable for the debts of the partnership. Partners also share in the profits of the partnership.

Limited partnerships can also be established in some states under specific state legislation. Limited partnerships allow some partners to limit their liability for debts. Limited partnerships are generally taxed as companies.

Joint Venture

A joint venture occurs when two or more parties come together in order to undertake a

specific project. The joint venture arrangement can be incorporated or unincorporated.

(f) Unincorporated Joint Venture

In an unincorporated joint venture, the parties usually enter into a joint venture agreement, which sets out the rights and obligations of each joint venture party.

Each party is treated individually or separately for tax purposes. This enables each party to use its own preferred tax structure.

The main disadvantage of a joint venture is there is often joint liability to third parties.

(g) Incorporated joint venture

In an incorporated joint venture, the joint venture is conducted by a company. The company is often established for the specific joint venture, and each party is a shareholder. The shareholders usually enter into a shareholders agreement, which sets out the rights and responsibilities of the shareholders. The parties must also comply with the Corporations Act.

Trust

An Australian business may be carried on by way of a trust.

Under a trust structure, the trustee (who may be an individual or more commonly a company) conducts the business and holds all income and capital on trust for the beneficiaries. The beneficiaries can be individuals, trusts or companies.

The trust is created by a document called a trust deed. The trust is governed by the terms of the trust deed, Australian state or territory legislation and the common law.

Trusts fall into two categories: discretionary trusts and unit trusts.

(h) Discretionary trusts

Under a discretionary trust, the trustee has discretion to distribute the income and capital of the trust to any of the beneficiaries. It is common for discretionary trusts to have specified (or named) beneficiaries, as well as classes of general beneficiaries (which may include the family members of a named beneficiary).

One of the benefits of a discretionary trust is the trustee has the ability to make distributions which consider the beneficiaries' individual tax circumstances. Discretionary trusts are most often used for family-owned businesses. Generally, discretionary trusts are not an appropriate investment vehicle.

(i) Unit trusts

Under a unit trust, the beneficiaries (referred to as unitholders) subscribe for units in the trust. Each unitholder has an interest in the capital and income of the trust that is relative to the number of units that they hold. Unit trusts have the benefit of conferring a clearly defined entitlement and are often considered more appropriate than a discretionary trust for non-family business ventures.

Sole Trader

This is the simplest form of business structure. A sole trader is an individual person who carries on business as an individual under their own name or under a registered business name. A sole trader is personally liable for all debts of the business.

Managed Investment Schemes

A managed investment scheme (**MIS**) enables a group of investors to contribute capital in consideration of acquiring a right in the benefits of the scheme. The contributions are pooled for investment (typically in a trust-based arrangement) or used in a common enterprise, in order to produce that benefit. Investors do not have day-to-day management of the MIS' operations. Instead, a MIS is managed by a 'responsible entity' with an Australian Financial Services Licence (**AFSL**), acting in accordance with the scheme's constitution and the Corporations Act.

Where a MIS has 20 or more retail clients, it must be registered with ASIC, and its 'responsible entity' must be a public company with at least three directors.

COMPARISON – PROS AND CONS OF EACH BUSINESS STRUCTURE

Structure	Advantages	Disadvantages
Sole Trader	• Simple and inexpensive to set up and operate • The owner retains control of the business and over its decision making. Therefore, the owner is able to exercise flexibility and speed in decision making. • Less regulatory requirements than there are for the other structures.	• No separate legal existence - the owner will be responsible for all debts and liabilities of the business. • Creditors have the right to claim against the personal assets of the owner. • Limited access to capital, if the business grows. • No continuity of existence – without a succession plan, the business will not survive if the initial owner dies.
Partnership	• Simple and relatively inexpensive to set up – a partnership can be set up informally by the parties carrying on business together with a view to a profit. However, a written partnership agreement is recommended. • Partners can combine their financial resources and expertise. • Tax is paid by the partners on their own tax returns and at their own marginal tax rates. • Tax losses of the partnership can be used to offset the partners' personal tax liabilities. • Partnerships are under no obligation to	• No separate legal entity - partners are jointly and severally liable for the debts and obligations of the partnership. • Statutory limits on the number of partners allowed. • Difficulties can arise when there is a change in the partnership structure (e.g.: when a partner leaves the partnership).

	make public disclosures of accounts and reports. • The partnership structure is often more flexible than other structures.	
Company (including incorporated joint ventures)	• Investment is easier - shares can be transferred. • Limited liability for shareholders – the personal liability of shareholders is limited to the amount (if any) unpaid on their shares. • Can be easier to raise finance. • It continues indefinitely, so no succession issues. • Suitable for businesses that want to expand. • Taxation benefits - the differential between the corporate rate and the top effective personal tax rate may give rise to tax planning opportunities in certain circumstances. • Profits may be accumulated and re-invested by the company without the need for distribution to shareholders.	• Ongoing costs (accounting and reporting) and compliance. • Loss of control – directors rather than shareholders make management decisions. • Directors can be personally liable in certain circumstances (refer to our comments in respect of director's liability below).
Trust	• Trusts may be more effective for tax purposes where assets are to be held for ultimate sale. • Trust structure can be more flexible than a company structure. For example, the legal restrictions that apply to reductions in the capital of a company do not apply to similar reductions in the capital of the trust. • Discretionary trusts have flexibility in the distribution of income.	• It can be expensive to set up a trust. • Trust structures are complex and are subject to numerous legal and regulatory requirements. • The trustee is subject to strict legal obligations.
Unincorporated Joint Ventures	• Each party is treated independently for tax purposes. • Flexibility in management/governance arrangements.	• There is usually joint liability to third parties.

CORPORATE GOVERNANCE AND REGULATION

Individuals, partnerships and corporate entities that operate businesses in Australia are subject to a broad range of regulatory and reporting requirements which vary depending on a range of factors, including the:

- structure, nature, and ownership of the entity which conducts the business;
- state or territory in which the business is being conducted; and
- nature of the business being conducted (such as the type of goods or services that are provided).

Australian Securities and Investments Commission (ASIC)

Australian corporate entities are primarily governed by the Corporations Act.

ASIC is the national body that is responsible for regulating the incorporation, operation and management of corporate entities in Australia. ASIC also hosts and maintains a public register of Australian corporate entities, which is accessible by the general public.

The Corporations Act places ongoing disclosure and reporting obligations on Australian companies, including requirements for certain information to be provided to ASIC for the purposes of public records. These reporting obligations include:

- reporting any changes to their company details and structure (such as changes to company officers, shareholders, registered addresses or issued share capital) to ASIC within a specified period after such change occurs;
- notifying ASIC before undertaking certain actions (such as providing financial assistance to a person who is seeking to acquire securities in that company); and
- lodging financial reports with ASIC each financial year (this obligation applies only to entities that are considered "disclosing entities", as defined in the Corporations Act).

Australian Securities Exchange

In addition to the obligations set out in the Corporations Act, public companies that are listed on the Australian Securities Exchange (**ASX**) must also comply with the ASX's listing rules and regulations. The key functions and responsibilities of the ASX are to:

- act as a market operator, clearing house and payments system facilitator for companies listed on Australia's public securities market exchange; and
- oversee the compliance with, and enforcement of, the ASX listing rules and other regulations.

Taxation Obligations

The Australian taxation system can be described as a self-assessment model, whereby taxpayers are responsible for lodging their own tax returns with the Australian Taxation Office (**ATO**) at the end of each relevant reporting period.

Tax File Numbers and Australia Business Numbers

Given that companies are considered as separate legal entities, Australian companies are required to obtain their own Tax File Number (commonly known as a TFN) for the purposes of complying with their taxation obligations.

Australian companies that conduct business activities are also required to apply for an Australian Business Number (commonly known as an ABN), which is used for the purposes of allocating and calculating any tax payable on the company's business income.

Income Tax Returns

Individuals and companies are generally required to lodge an annual income tax return at the end of each Australian financial year (which runs from 1 July to 30 June each year).

The income tax rate applicable to Australian business structures will depend on the type of entity that conducts the business. For example, the income tax rate for:

- Australian companies are generally fixed at 30%, except for those which qualify as "Small Business Entities"; and
- "Small Businesses Entities" (which are companies, unit trusts or public trading trusts which have an annual business turnover of less than AUD $50 million) has been reduced to 25% for the 2022-23 financial year.

Company Dividends and Tax Consolidation

Dividends paid by Australian companies to Australian resident shareholders are subject to a dividend imputation system, whereby shareholders are entitled to franking credits for the tax that the company has paid on its profits (from which dividends are paid). The effect of franking credits is that dividends are ultimately taxed at each shareholder's applicable income tax rate and are not taxed at the full rate at both the company and shareholder level.

Australian corporate groups consisting of a parent company and a series of wholly owned subsidiaries are able to form what is known as a "consolidated tax group". Consolidated tax groups are treated as a single entity for income tax purposes, and transactions within the group are often disregarded for the purposes of calculating income tax.

Goods and Services Tax (GST)

GST is a broad-based tax of 10% which applies to most goods, services and other items sold or consumed in Australia. GST is a multi-stage tax (similar to a Value-Added Tax) that is payable by suppliers at all levels of the supply chain. GST registered entities are entitled to claim refunds of the GST that they have incurred on their business inputs.

Businesses or individuals carrying on an enterprise that has (or is expected to have) an annual turnover of more than a specified amount are required to register for GST purposes. The GST component of a business' sales must be reported to the ATO on either a monthly, quarterly, or annual basis by lodging Business Activity Statements (also known as BAS statements).

Certain non-resident entities are eligible to access a simplified GST registration regime, whereby they may either be liable to the ATO or entitled to a refund at the end of each relevant reporting period. Whether an entity is required to make additional GST payments or is entitled to receive a GST refund will depend on the amount of GST collected through sales, when compared to any tax credits received from GST paid on goods and services purchased by the business in the course of carrying on their enterprise.

Other Taxation Liabilities

In addition to lodging annual income tax returns, companies and other corporate or business entities may also have taxation liabilities in respect of:

- **Capital Gains Tax (CGT)** - CGT is imposed on the capital gains realized from the sale of certain assets. Assets that are sold by individuals or corporate entities that are considered Australian residents for tax purposes may trigger a CGT liability, even if the relevant assets were not located in Australia.
- **Fringe Benefits Tax (FBT)** – Employers are required to pay FBT on the value of the non-cash benefits or allowances that they provide to their employees. The FBT rate for the year ending March 2024 is set at 47%.
- **Superannuation Guarantee Charge (SGC)** - If an employer fails to pay the statutory minimum level of superannuation to their employee's nominated superannuation fund, the employer will be liable to pay the Superannuation Guarantee Charge. The SGC is an amount equal to the value of the relevant shortfall in statutory superannuation payments, plus interest (currently at a rate of 10%) and administrative charges.
- **State and Territory specific taxes** - In additional to the federal taxes outlined above, each Australian State and Territory has their own taxation framework which may create additional tax liabilities for entities that conduct business in Australia. Examples of such state-based taxes include:

  Payroll Tax: Each State and Territory has a Payroll Tax system under which an employer is liable to pay tax on the value of the employer's monthly payroll expenses (including any relevant fringe benefits). Payroll Tax rates are generally between 4-7% but may differ significantly between each State and Territory. Each State and Territory also has a monthly wage threshold test to determine whether an employer is required to pay Payroll Tax.

  ***Stamp Duty*:** Individuals or entities that acquire land, certain interests in real property or interests in other entities that have significant land holdings may be required to pay an additional state-based tax known as Stamp Duty. Acquisitions to which Stamp Duty may apply, and the relevant rate of such Stamp Duty, varies significantly from State to State. Acquisitions of real property by foreign investors will often attract a higher rate of stamp duty.

  ***Land Tax*:** Individuals or entities that are the registered proprietor of Australian real property will also incur an annual Land Tax liability. Similar to Stamp Duty, the types of real property that will attract a Land Tax liability, and the relevant rate of such Land Tax, varies significantly between the States and Territories.

Capital Raising Regulation

The Corporations Act provides a framework for regulating fundraising activities (including capital raising) within Australia. The relevant provisions of the Corporations Act impose rules regarding offers or invitations to subscribe for new 'financial products', including shares, units in a trust, partnership interests and debentures in respect of both private and publicly listed entities.

The underlying principal of the fundraising rules under the Corporations Act is that, unless a specific exemption applies, a person must not make an offer in respect of a new financial product before providing potential investors

with a disclosure document. Depending on the circumstances of the offer and the characteristics of the target entity, the offering party may also be required to lodge a copy of the relevant disclosure documents with ASIC, prior to extending the offer to potential investors.

Generally speaking, a disclosure document must be in the form of a prospectus, which, depending on the nature of the financial product, can be either a long-form or short-form document. There are specific exemptions which allow for much simpler disclosure documents to be used in certain circumstances.

There are certain types of offers in respect of financial products which are exempt from the disclosure requirements set out in the Corporations Act. These include:

- offers to subscribe for new shares that are issued under an employee incentive scheme;
- offers to sell existing financial products (being financial products that are sold more than 12 months after the date that they were first issued);
- offers made to "sophisticated investors", being investors that hold net assets or have an annual income above a specified threshold;
- offers to "professional investors", such as stockbrokers or other persons who hold a financial services licence; and
- "small scale offerings", which are personal offerings made by an entity where no more than 20 investors will have acquired securities in the entity and no more than $2 million of capital is raised, within any 12-month period.

Importantly, companies (and in some circumstances, the company's directors) can be liable for civil and criminal penalties for failing to comply with the fundraising provisions of the Corporations Act, such as by:

- offering securities without a providing an appropriate disclosure document in the form required by the Corporations Act;
- making unsolicited offers of financial products and conducting advertising in respect of new financial products; and
- omitting required information from a disclosure document or producing a disclosure document that is misleading.

The regulatory framework around capital raising in Australia is robust and can be very complex. It is important that appropriate legal advice is sought before companies undertake capital raising activities.

Competition and Consumer Laws

Individuals and entities conducting business in Australia must also take note of Australia's Competition and Consumer protection laws, which are set out in the *Competition and Consumer Act 2010* (Cth) (**CCA**). At a high level, the CCA sets out the following prohibitions and consumer protections:

- **Prohibition on Anti-competitive Agreements** – Contracts, arrangements or understandings which have the purpose or likely effect of substantially lessening competition in the relevant market, are prohibited under the CCA.
- **Prohibition on Price fixing** – Competitors must not enter any contract, arrangement or understanding that has the purpose or effect of fixing a price for the provision of goods or services.

- **Prohibition on Exclusive Dealing** – Generally speaking, exclusive dealing occurs when an individual or entity, when trading with another party, imposes restrictions on the other party's freedom to choose how they trade with other businesses. Exclusive dealing will be in breach of the CCA where the conduct has the effect of substantially lessening competition in the relevant market. Examples of exclusive dealing include:

  Third Line Forcing: Where a business will only agree to supply goods or services to another party on the condition that the party who receives those goods or services also purchases goods or engages the services of a particular third party.

  Full Line Forcing: Where a supplier refuses to supply goods or services unless the receiving party agrees not to purchase certain other goods or services from the supplier's competitors.

- **Prohibition on Resale Price Maintenance -** Resale price maintenance occurs when a supplier prevents, or attempts to prevent, a business (such as an independent retailer or distributor) from advertising or selling products below a specified minimum price. Suppliers are permitted to specify a *recommended retail price* for their products, however the CCA prohibits suppliers from threatening not to supply goods if those goods are not sold at the recommended retail price, or from otherwise exerting pressure on retailers to sell the goods at a specified price.

- **Prohibition on Unconscionable Conduct** – Unconscionable conduct is a very broad concept that does not have a precise legal definition in the CCA. Broadly speaking, the CCA prohibition on unconscionable conducts seeks to prohibit business conduct that is harsh or oppressive, and that extends beyond the ambit of commercial bargaining or negotiation tactics.

- **Prohibition on Misleading and Deceptive Conduct** – The CCA prohibits persons from, during trade or commerce, engaging in conduct that is misleading or deceptive or that is likely to mislead or deceive. Australian Courts have historically taken a very broad approach in determining the types of conduct that may be misleading or deceptive, which can include activities such as advertising, oral representations, as well as representations in respect to contractual matters.

- **Product Liability** – Businesses that manufacture goods or import goods into Australia for the purposes of resale will be liable to consumers for any safety defects in respect of the goods. The CCA provides that consumers may seek compensation from a manufacturer in respect of goods which have safety defects, if it can be established that the defects have caused the consumer to suffer loss or damage.

<u>International Trading Considerations</u>

Individuals or entities that conduct businesses in Australia with the intention of trading internationally should also familiarise themselves with the following concepts:

- **Transfer pricing** – Australia's transfer pricing regime requires that international related-party transactions must be made on arms' length terms. The primary purposes of the transfer pricing rules are

to ensure that the consideration exchanged by the relevant related parties has been agreed on the basis of an acceptable pricing methodology, to ensure an appropriate level of tax is paid.

- **Customs duty -** Customs duty is imposed on goods imported into Australia. The rate of customs duty is generally around 5% of the value of goods (when converted to Australian dollars), depending on the type of goods being imported and the country of origin. GST may also be applied to goods at the time that they are imported.
- **Excise duty** - Excise duty is a commodity-based tax that applies to alcohol, tobacco, fuel, and petroleum products that are produced, stored or manufactured in Australia. In addition to paying the relevant excise duty, businesses that produce, store or manufacture alcohol, tobacco or petroleum products are required to obtain and maintain an excise licence.

Other Regulatory Bodies

In addition to the regulatory bodies and agencies described above, individuals and companies that carry on businesses in Australia may also need to interact with (and comply with the relevant regulations enforced, or administered by) the following regulatory bodies:

- **Australian Prudential Regulation Authority (APRA)** - APRA is an independent statutory authority that was formed to oversee the Australian financial services industry and enforce prudential financial standards. APRA's regulatory functions include the supervision of banks, insurance companies, building societies, credit unions, and superannuation funds.
- **Australian Transaction Reports and Analysis Centre (AUSTRAC) –** AUSTRAC is the federal financial intelligence agency that is primarily responsible for investigating and prosecuting money laundering and counter-terrorism financing.
- **Reserve Bank of Australia (RBA)** - The RBA is an independent statutory body that is primarily responsible for performing Australia's central banking functions. The RBA has a range of functions, including establishing monetary policy (such as setting Australia's cash rate) and ensuring the stability of Australia's financial system.
- **Foreign Investment Review Board (FIRB) -** The FIRB is a non-statutory advisory body within the federal Treasury department. One of the key functions of the FIRB is to assess (and if thought fit, consent to) proposals by foreign persons to acquire interests in Australian land, businesses, and companies. In 2021, significant changes to Australia's foreign investment framework were made in response to the COVID-19 pandemic. Some of those changes have now been reversed. However, it is extremely important that foreign investors seek advice in respect of these changes when deciding whether to invest in an existing Australian company or to establish a new business operation in Australia.
- **IP Australia -** IP Australia is the federal government agency responsible for processing applications for the registration of certain registrable intellectual property rights, such as patents, trademarks, and registered

designs. IP Australia has the authority to conduct hearings and determine whether to grant or refuse applications in respect of intellectual property rights.

REQUIREMENTS FOR LOCAL SHAREHOLDING/DIRECTORS

Director Requirements

Australian private companies must have at least one director who:

- is over 18 years of age;
- has not previously been disqualified from acting as a director (for example, because of acting as an officer of two or more companies that have gone into liquidation within the past 7 years); and
- ordinarily resides in Australia. Note the requirement for a director to "ordinarily reside" in Australia is not a question of citizenship, rather it is a question of where that person is usually domiciled.

Australian public companies must have at least three directors who satisfy the age and qualification requirements set out above, two of which must ordinarily reside in Australia. Public companies must also have at least one secretary who resides in Australia.

Australian branches of foreign companies do not require a local director but must appoint at least one local agent.

Directors of Australian companies are also required to obtain a Director Identification Number (**Director ID**) before their appointment.

Local Shareholding Requirements

There are no minimum start-up capital requirements for establishing a company in Australia. In fact, it is very common for many companies to start out as "$2 Companies", being a company with only AUD $2 in issued share capital.

Australian companies must have a minimum of one shareholder. There is no local shareholding requirement for establishing a private company in Australia, however it is worth noting that foreign persons or entities that wish to acquire shares in established Australian companies, or interests in Australian businesses, may be required to obtain the approval of the FIRB prior to such acquisition occurring.

Australian private companies must not have more than 50 shareholders (excluding any employee shareholders). Where this 50-shareholder limit is exceeded, the Corporations Act requires the company to convert to a public company.

Director's Duties

Director's duties in respect of Australian companies are largely set out in the Corporations Act, however there are some duties which derive from Australian common law. These duties include:

- **Duty of care and diligence** – Directors must act with a degree of care and diligence in performing their role as a director. The relevant level of care and diligence is measured against the expectation that a reasonable person would have of a person acting in the capacity of a company director. A director may not be liable for breach of their duty to exercise care and diligence, if it can be established that the director:
  - (a) made the relevant decision in good faith and for a proper purpose;
  - (b) reasonably believed the decision was in the best interests of the

company, after having made all reasonable inquiries necessary to inform themselves about the subject matter of the decision; and

(c) made the relevant decision while having had no personal interest in the matter.

- **Duty to act honestly in good faith** – Directors must act in the best interests of the company as a whole and for a proper purpose. Broadly speaking, this duty requires a director to exercise independent judgement when acting on behalf of a company, to ensure that the best interests of the company are (objectively) paramount at all times.
- **Duty not to improperly use inside information or position –** Directors must not use their position (or any information that they gain by virtue of their position) to gain an advantage for themselves or someone else, or to the detriment of the company.
- **Duty to avoid a conflict of interest and to disclose material personal interests** – Directors must make clear disclosures to the company where the affairs or business of the company relate to matters in which the director has a material personal interest. In this regard, it is also worth noting that directors of public companies are required to obtain shareholder approval for transactions which involve their related parties and make disclosures to the market in respect of the director's personal interests.
- **Duty to avoid insolvent trading –** Directors have a duty to ensure that a company does not trade while insolvent, or when the director suspects that the company might be insolvent.
- **Duty to keep proper accounts and records** – Further to the duty to ensure that a company does not trade whilst insolvent, directors must keep themselves informed of the accounting position of the company, as well as the company's mandatory financial reporting obligations (if applicable).

Director's Liability

In Australia - given that companies are separate legal entities - company directors are generally not personally liable for the debts of the company. However, there are some circumstances where a director may be personally liable for a company's debt, or where a director's conduct may subject them to civil and criminal penalties, as well as damages. Examples of such circumstances include:

- **Insolvent Trading –** Directors who allow a company to trade whilst insolvent will be in breach of the Corporations Act, and in some circumstances, may be personally liable for the debts incurred by the company during the period in which the company traded whilst insolvent.
- **Personal Guarantees –** It is common for directors of small private companies to provide a personal guarantee as security for debts incurred by a company. Given that personal guarantees are a separate and binding agreement between the director and the relevant financier, a director will be personally liable for the debt to which the guarantee relates.
- **Breach of Directors' Duties** – Where a director breaches their fiduciary or statutory duties to a company as set out in the Corporations Act (and as outlined

above), they may be liable for civil and criminal penalties, as well as damages in favour of the company.

- **Taxation Debts and Superannuation Contributions** – Directors can be personally liable for a company's failure to comply with their GST, Pay As You Go (PAYG) withholding tax and Superannuation Guarantee Charge (SGC) payment obligations.
- **Phoenix Activity –** "Phoenix Activity" occurs where the directors of a company place the company into liquidation or administration to avoid paying the company's debts, and then establish a new company for the purpose of continuing the previous company's business. Directors who engage in Phoenix Activity may be subject to civil and criminal penalties, and in extreme circumstances, may even face imprisonment.

SHAREHOLDERS' RIGHTS AND PROTECTION

Shareholders do not have the right to manage the affairs of the company. The constitution of the company usually vests the management of the company in the board of directors. Typically, the board will delegate the day-to-day operation of the company to the chief executive officer.

Shareholders have no right to demand access to information including the books of the company, under the Corporations Act. Shareholders may apply to the Court for an order to inspect the books of the company.

Shareholder Oppression under the Corporations Act

The Corporations Act provides Australian Courts with the authority to make a broad range of orders where it is established that a company has acted (or proposes to act) in a manner that:

- is contrary to the interests of the company's shareholders (as a whole); or
- is oppressive to, or unfairly prejudicial against, one or more of the company's shareholders.

Such orders can include orders that:

- require the company to be wound up;
- require the company's constitution to be modified or repealed; or
- compel or prevent a person from engaging in certain conduct.

The types of conduct which may give rise to a successful claim of shareholder oppression will be assessed by the Court on an objective basis and will involve an examination of whether the conduct would be seen as oppressive in the eyes of a reasonable person.

A common example of shareholder oppression is where a majority shareholder misuses their control and influence over the company in a way that is unfairly prejudicial to minority shareholders.

Shareholder's rights under the Corporation Act

The rights and protections that apply to shareholders under the Corporations Act will depend on the nature of the relevant company, as well as the provisions of the company's constitution and other constituent documents (such as a shareholders agreement).

Examples of shareholder rights which are contained in the Corporations Act (and will apply to private companies, despite any contrary provision within a company's constituent documents) are set out below:

- **Amending the Constitution:** A company may only amend its constitution by passing a special resolution of members. To pass a special resolution, at least 75 percent of the company's shareholders must vote in favour of the proposed resolution.
- **Capital Alterations:** Companies are required to obtain shareholder approval before undertaking alterations to the company's share capital. These alterations include capital reductions, selective buybacks, and share buy-backs. The percentage of shareholders who must approve a proposed capital alteration will depend on the nature of the proposed alteration, and in some circumstances, may require the passing of a special resolution.
- **Right to Call Meetings of Shareholders:** Shareholders who hold at least 5% of the shares with voting rights in a company may, by written notice to the directors, demand that the directors call a meeting of shareholders. Alternatively, shareholders who hold at least 5% of the shares with voting rights in a company may call a meeting of shareholders themselves by following the notice and timing requirements set out in the Corporations Act.
- **Right to Notice of Meetings of Shareholders:** Subject to any restrictions on the rights attaching to a shareholder's shares**,** shareholders generally have the right to receive written notice of, and attend and vote at, meetings of shareholders. The Corporations Act provides that, as a general rule, at least 21 days written notice of a shareholder's meeting must be provided for private companies.

FOREIGN INVESTMENT, THIN CAPITALIZATION, RESIDENCY AND MATERIAL VISA RESTRICTIONS

Australia's Foreign Investment Framework

Relevant Legislation

Australia's foreign investment framework is set out within the *Foreign Acquisitions and Takeovers Act 1975* (Cth) (**FATA**), the *Foreign Acquisitions and Takeovers Regulations 2015* (Cth) (**Regulations**), and the Australian Federal Government's specified Foreign Investment Policy from time to time.

The FATA requires "foreign persons" or foreign government investors who propose to acquire interests in Australian real property, or certain interests in Australian companies or businesses, to obtain FIRB approval prior to such acquisition taking place.

Who is considered a Foreign Person?

The concept of a "foreign person" as set out in the FATA is far reaching and includes not only individuals who are not ordinarily resident in Australia, but will also include:

- a corporation or the trustee of a trust in which an individual not ordinarily resident in Australia, a foreign corporation or a foreign government holds a substantial interest; and
- a corporation or the trustee of a trust in which 2 or more persons, who together hold an aggregate *substantial interest*, are:
  - (a) not ordinarily resident in Australia;
  - (b) a foreign corporation; or
  - (c) a foreign government entity.

A "substantial interest" for the purposes of the above means an interest of 20% or more in the relevant company or trust.

Acquisitions of Residential and Commercial Property

There are certain restrictions imposed on the purchase of residential and commercial property by foreign persons.

Acquisitions of interests in Australian Companies and Businesses

As a general rule, foreign persons are required to obtain FIRB approval prior to entering into an unconditional agreement to acquire substantial interests (i.e., interests of 20% or more) in Australian companies or businesses which have an annual turnover above a specified threshold.

Acquisitions of interests in Australian companies by foreign government entities or in respect of Australian companies that conduct "sensitive business", such as media, telecommunications, transport, military related industries and activities and securities technologies, are subject to a very strict foreign investment approval process.

The relevant monetary thresholds which trigger the requirement of foreign investors to notify the FIRB and/or seek FIRB approval vary significantly depending on the characteristics of the target entity or business, and generally apply to businesses or companies which are valued at more than $310 million AUD.

Importantly, there have been significant changes to Australia's foreign investment framework as a result of and since the COVID-19 pandemic. These include the introduction of a new 'Register of Foreign Ownership of Australian Assets' and related reporting obligations on foreign persons in respect of their Australian assets. Any person or entity seeking to invest in Australian land or companies should seek legal advice regarding the relevant FIRB approvals which must be obtained.

The overarching policy objective behind the FIRB's regulation of foreign investment into Australian companies and businesses is to ensure that any proposed foreign acquisitions are not contrary to Australia's national interest.

Capitalization Obligations

In Australia, "thin capitalization" rules apply to:

- **"Outward investing entities"** – being Australian entities with specified overseas investments; and
- **"Inward investing entities"** – which are foreign entities with certain investments in Australia, regardless of whether they hold the investments directly or through Australian entities.

One of the key objectives of the thin capitalization rules is to ensure that inward and outward investing entities fund their Australian operations with a sufficient amount of equity capital. This is achieved by limiting the debt deductions that inward and outward investing entities are able to claim in their annual tax returns, which would otherwise have the effect of minimizing their Australian taxation liabilities.

The thin capitalization rules can change from year to year and will only apply when an entity's debt-to-equity ratio exceeds the allowable limits. Foreign entities which conduct business operations in Australia should seek independent taxation advice in respect of the thin capitalization rules.

Business or Investment Visas

Migration to Australia is primarily governed by the *Migration Act 1958* (Cth) (**Migration Act**) and the *Migration Regulations 1958* (Cth) (**Migration Regulations**). Non-Australian persons generally have a right to travel to, enter, and remain in Australia provided that they obtain an appropriate class of visa and complete the immigration clearance process.

There are a broad range of visas that are available for foreign persons who wish to seek employment or commence business operations in Australia. These visa classes include:

- **Subclass 188 - Business Innovation and Investment (Provisional) visas**

  A Subclass 188 Visa allows foreign persons to own, manage and conduct businesses and to conduct investment or entrepreneurial activities in Australia. A Subclass 188 Visa is generally valid for up to 5 years, however provisional visa holders may be able to apply for a permanent visa once certain requirements are met.

- **Subclass 400 - Temporary Work (Short Stay Specialist) visa**

  A Subclass 400 Visa allows for foreign persons to enter and remain in Australia for the purposes of performing short-term, highly specialised work. In order to be eligible for a Subclass 400 Visa, the applicant will be required (among other things) to have specialised skills, knowledge or experience that is not commonly available in Australia. A Subclass 400 Visa can be granted for up to 6 months; however, applications for more than 3 months must be supported by a strong business case.

- **Subclass 482 - Temporary Skill Shortage visa**

  A Subclass 482 Visa allows Australian businesses to sponsor a suitably skilled foreign person to work in their business, if they are unable to source an appropriately skilled Australian worker. Subclass 482 Visas are generally valid for a period of 2 years; however, they may be granted for up to 4 years if an International Trade Obligation applies. Eligible Subclass 482 Visa holders can now apply for permanent residency through the Temporary Residence Transition visa stream.

Foreign persons who wish to enter Australia for the purpose of seeking employment or commencing business operations in Australia should seek the advice of a registered Migration Agent, who will be able to provide advice in respect of the appropriate class of visa and the associated application process.

Restrictions on Remitting Funds out of Australia

The general position is that there are no restrictions on the amount of funds (including cash and electronically transmitted funds) that may be transferred in or out of Australia. However, the *Anti-Money Laundering and Counter-Terrorism Financing Act 2006* (Cth) (**AML/CTF Act**) requires certain transactions to be reported to AUSTRAC within 10 business days of such transfer occurring, for the purpose of detecting tax evasion and money laundering.

The AML/CTF Act imposes additional regulatory requirements on businesses that are classified as "reporting entities". Reporting entities are entities which provide "designated services", including financial, gambling, bullion or digital currency exchange services.

At a high level, the AML/CFT Act requires reporting entities to:

- implement an AML/CTF compliance program, which includes verifying the identity of clients before a designated service is provided, and collecting and verifying information about beneficial owners of clients;
- report specific kinds of transactions and suspicious matters to AUSTRAC; and

- keep accurate records in respect of their customers.