



CIMA EXAM PRACTICE KIT

2005
EDITION

ONLY TEXT ENDORSED BY CIMA

CIMA

PUBLISHING

Paper C5

Business Law

Relevant for **2005** Computer Based Assessment



Brian Benton

CERTIFICATE | MANAGERIAL | STRATEGIC

CIMA Exam Practice Kit

Business Law

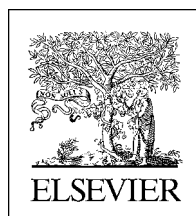
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CIMA Exam Practice Kit



Business Law

Brian Benton



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CIMA Publishing
An imprint of Elsevier
Linacre House, Jordan Hill, Oxford OX2 8DP
30 Corporate Drive, Burlington, MA 01803

First published 2005

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British Library Cataloguing in Publication Data

A catalogue record for this book is available from the British Library

Library of Congress Cataloguing in Publication Data

A catalogue record for this book is available from the Library of Congress

ISBN 0 7506 6585 8

For information on all CIMA Publishing Publications
visit our website at www.cimapublishing.com

Typeset by Integra Software Services Pvt. Ltd, Pondicherry, India
www.integra-india.com
Printed and bound in The Netherlands

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About the Author

Brian Benton is the Director of a Legal Tuition Company. He has been lecturing Law for over 20 years in both the public and private sectors. He has formerly been Head of Law at a large Birmingham College. He works with all the major accountancy tuition providers, lecturing all around the country. He has a Law degree from London University and Solicitors qualifying examinations. Brian is also a qualified Chairman at his local Magistrate's Court.

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Introduction

Welcome to the new CIMA Exam Practice Kit which has been launched to coincide with a major change in the syllabus where new examinations will take place from May 2005.

This Kit has been designed with the needs of home study and distance education candidates in mind, and it is also ideal for fully taught courses or for students resitting papers from the old syllabus.

These hints, questions and answers have been produced by some of the best-known freelance tutors in the United Kingdom who have specialised in their respective papers and the questions and topics selected are relevant for the May 2005 and November 2005 examinations.

The exam practice kits will complement CIMA's existing study manuals with the Q & A's from May 2005 published in the next edition of the CIMA study manual and the Q & A's from November 2005 examination published in the 2006 edition of the Exam Practice Kit.

Good luck with your studies.

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Syllabus Guidance, Learning Objectives and Verbs

A The syllabus

The syllabus for the CIMA Professional Chartered Management Accounting qualification 2005 comprises three learning pillars:

- 1 Management Accounting pillar
- 2 Business Management pillar
- 3 Financial Management pillar.

Within each learning pillar there are three syllabus subjects. Two of these subjects are set at the lower “Managerial” level, with the third subject positioned at the higher “Strategic” level. All subject examinations have a duration of three hours and the pass mark is 50 per cent.

Note: In addition to these nine examinations, students are required to gain three years relevant practical experience and successfully sit the Test of Professional Competence in Management Accounting (TOPCIMA).

B Aims of the syllabus

The aims of the syllabus are:

- To provide for the Institute, together with the practical experience requirements, an adequate basis for assuring society that those admitted to membership are competent to act as management accountants for entities, whether in manufacturing, commercial or service organisations, in the public or private sectors of the economy.
- To enable the Institute to examine whether prospective members have an adequate knowledge, understanding and mastery of the stated body of knowledge and skills.
- To complement the Institute’s practical experience and skills development requirements.

C Study weightings

A percentage weighting is shown against each topic in the syllabus. This is intended as a guide to the proportion of study time each topic requires.

All topics in the syllabus must be studied, since any single examination question may examine more than one topic, or carry a higher proportion of marks than the percentage study time suggested.

The weightings *do not* specify the number of marks that will be allocated to topics in the examination.

D Learning outcomes

Each topic within the syllabus contains a list of learning outcomes, which should be read in conjunction with the knowledge content for the syllabus. A learning outcome has two main purposes:

- 1 to define the skill or ability that a well-prepared candidate should be able to exhibit in the examination;
- 2 to demonstrate the approach likely to be taken by examiners in examination questions.

The learning outcomes are part of a hierarchy of learning objectives. The verbs used at the beginning of each learning outcome relate to a specific learning objective, e.g. evaluate alternative approaches to budgeting.

The verb “evaluate” indicates a high level learning objective. As learning objectives are hierarchical, it is expected that at this level, students will have knowledge of different budgeting systems and methodologies and be able to apply them.

A list of the learning objectives and the verbs that appear in the syllabus learning outcomes and examinations follows:

<i>Learning objectives</i>	<i>Verbs used</i>	<i>Definition</i>
1 Knowledge <i>What you are expected to know</i>	List State Define	Make a list of Express, fully or clearly, the details of/facts of Give the exact meaning of
2 Comprehension <i>What you are expected to understand</i>	Describe Distinguish Explain Identify Illustrate	Communicate the key features of Highlight the differences between Make clear or intelligible/ State the meaning of Recognise, establish or select after consideration Use an example to describe or explain something

3 Application*How you are expected to apply your knowledge*

Apply	To put to practical use
Calculate/compute	To ascertain or reckon mathematically
Demonstrate	To prove with certainty or to exhibit by practical means
Prepare	To make or get ready for use
Reconcile	To make or prove consistent/compatible
Solve	Find an answer to
Tabulate	Arrange in a table

4 Analysis*How you are expected to analyse the detail of what you have learned*

Analyse	Examine in detail the structure of
Categorise	Place into a defined class or division
Compare and contrast	Show the similarities and/or differences between
Construct	To build up or compile
Discuss	To examine in detail by argument
Interpret	To translate into intelligible or familiar terms
Produce	To create or bring into existence

5 Evaluation*How you are expected to use your learning to evaluate, make decisions or recommendations*

Advise	To counsel, inform or notify
Evaluate	To appraise or assess the value of
Recommend	To advise on a course of action

Business Law and computer-based assessment

The examination for Business Law is a 60-minute computer-based assessment comprising 40 compulsory questions, with one or more parts. Single part questions are generally worth 1–2 marks each, but two and three part questions may be worth 4 or 6 marks. There will be no choice and all questions should be attempted if time permits. CIMA are continuously developing the question styles within the CBA system and you are advised to try the on-line website demo at www.cimaglobal.com, to both gain familiarity with assessment software and examine the latest style of questions being used.

Computer-based assessment

CIMA has introduced computer-based assessment (CBA) for all subjects at Certificate level. The website says

Objective questions are used. The most common type is “multiple choice”, where you have to choose the correct answer from a list of possible answers, but there are a variety of other objective question types that can be used within the system. These include true/false questions, matching pairs of text and graphic, sequencing and ranking, labelling diagrams and single and multiple numeric entry.

xiv Syllabus Guidance, Learning Objectives and Verbs

Candidates answer the questions by either pointing and clicking the mouse, moving objects around the screen, typing numbers, or a combination of these responses. Try the online demo at <http://www.cimaglobal.com> to see how the technology works.

The CBA system can ensure that a wide range of the syllabus is assessed, as a pre-determined number of questions from each syllabus area (dependent upon the syllabus weighting for that particular area) are selected in each assessment.

In every chapter of this study system we have introduced these types of questions but obviously we have to label answers A, B, C and so on rather than using click boxes. For convenience we have retained quite a lot of questions where an initial scenario leads to a number of sub-questions. There will be questions of this type in the CBA but they will rarely have more than three sub-questions. In all such cases examiners will ensure that the answer to one part does not hinge upon a prior answer.

There are two types of questions which were previously involved in objective testing in paper-based exams and which are not at present possible in a CBA. The actual drawing of graphs and charts is not yet possible. Equally there will be no questions calling for comments to be written by students. Charts and interpretations remain on many syllabi and will be examined at Certificate level but using other methods.

For further CBA practice, CIMA Publishing has produced CIMA Inter@ctive CD-ROMs for all certificate level subjects. These products use the same software as found in the real Computer-based assessment and are available at www.cimapublishing.com.

The Business Law syllabus

Syllabus overview

The Business Law syllabus deals with those aspects of law which affect businesses and which contribute towards establishing the competence of the Chartered Management Accountant. By way of introduction, it covers fundamental elements of The English legal system, and uses professional negligence as the vehicle for demonstrating the system of judicial precedent. The syllabus then proceeds to look at the essentials of establishing and performing simple contracts and the remedies available in the event of a breach.

As an introduction to company law, the syllabus then proceeds to look at the essential characteristics of the various forms of business organisation. Following this introduction, the emphasis is placed upon the company limited by shares and the rules relating to company formation, finance and management. Students may be required to present their explanations in the form of a letter or memorandum.

Aims

This syllabus aims to test the student's ability to:

- explain fundamental aspects of the organisation and operation of the English legal system;
- explain the elements of the tort of negligence and the manner in which the tort impacts upon professional advisers;

- identify and explain the essential elements of a simple contract, what is regarded as adequate performance of the simple contract, and the remedies available to the innocent party in the event of a breach;
- explain the essential differences between sole traderships, partnerships and companies limited by shares;
- explain the ways in which companies are administered, financed and managed;
- apply legal knowledge to business problems and communicate the explanations in an appropriate form.

Assessment

This subject is assessed by a computer-based assessment. The assessment is 60 minutes and comprises 40 compulsory questions with one or more parts. A varied range of objective test questions are used.

Learning outcomes and syllabus content

3b(i) The English legal system – 10%

Learning outcomes

On completion of their studies students should be able to

- explain the manner in which behaviour within society is regulated by the civil and the criminal law;
- identify and explain the sources of English law;
- explain and illustrate the operation of the doctrine of precedent by reference to the essential elements of the tort of negligence, by which we mean duty, breach and damage/loss/injury;
- explain the application of the tort of negligence to professional advisers.

Syllabus content

- The sources of English law.
- The system of judicial precedent.
- The essential elements of the tort of negligence, including duty, breach and damage/loss/injury.
- The liability of professionals in respect of negligent advice.

3b(ii) Establishing contractual obligations – 10%

Learning outcomes

On completion of their studies students should be able to

- identify the essential elements of a valid simple contract and situations where the law requires the contract to be in a particular form;
- explain how the law determines whether negotiating parties have reached agreement;

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- explain what the law regards as consideration sufficient to make the agreement enforceable;
- explain when the parties will be regarded as intending the agreement to be legally binding;
- explain when an apparently valid agreement may be avoided because of misrepresentations.

Syllabus content

- The essential elements of a valid simple contract.
- The legal status of the various types of statements which may be made by negotiating parties. Enforceable offers and acceptances, and the application of the rules to standard form contracts and modern forms of communication.
- The meaning and importance of consideration.
- The principles for establishing that the parties intend their agreement to have contractual force.
- How a contract is affected by misrepresentation.

3b(iii) Performing the contract – 10%

Learning outcomes

On completion of their studies students should be able to

- explain how the contents of a contract are established;
- explain the status of contractual terms and the possible repercussions of non-performance;
- explain how the law controls the use of unfair terms in respect of both consumer and non-consumer business agreements;
- explain what the law regards as performance of the contract, and valid and invalid reasons for non-performance.

Syllabus content

- Incorporation of express and implied terms.
- Conditions and warranties and the nature and effect of both types of terms.
- The main provisions of sale of goods and supply of services legislation.
- The manner in which the law controls the use of exclusion clauses and unfair terms in consumer and non-consumer transactions.
- The level of performance sufficient to discharge contractual obligations.
- Valid reasons for non-performance by way of agreement, breach by the other party and frustration.

3b(iv) Contractual breakdown – 10%

Learning outcomes

On completion of their studies students should be able to

- explain the type of breach necessary to cause contractual breakdown;
- describe the remedies which are available for serious and minor breaches of contract.

Syllabus content

- The remedies of specific performance, injunction, rescission, and requiring a contract party to pay the agreed price.
- Causation and remoteness of damage.
- The quantification of damages.

3b(v) The law of employment – 10%*Learning outcomes*

On completion of their studies students should be able to

- distinguish between employees and independent contractors and explain the importance of the distinction;
- explain how the contents of a contract of employment are established;
- explain the distinction between unfair and wrongful dismissal;
- demonstrate an awareness of how employers and employees are affected by health and safety legislation, including the consequences of a failure to comply.

Syllabus content

- The tests used to distinguish an employee from an independent contractor.
- The express and implied terms of a contract of employment.
- Unfair and wrongful dismissal.
- An outline of the main rules relating to health and safety at work, sanctions on employers for non-compliance, and remedies for employees.

3b(vi) Company formation – 15%*Learning outcomes*

On completion of their studies students should be able to

- explain the essential characteristics of the different forms of business organisations;
- explain the concept and practical effect of corporate personality;
- explain the differences between public and private companies;
- explain the distinction between establishing a company by registration and purchasing “off the shelf”;
- explain the purpose and legal status of the memorandum and articles of association;
- explain the ability of a company to contract;
- explain the main advantages and disadvantages of carrying on business through the medium of a company limited by shares.

Syllabus content

- The essential characteristics of sole traderships/practitionerhips, partnerships and companies limited by shares.
- Corporate personality and its legal consequences.
- “Lifting the corporate veil” both at common law and by statute.
- The distinction between public and private companies.

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- The procedure for registering a company, the advantages of purchasing a company “off the shelf”, and the purpose and content of the memorandum and articles of association.
- Corporate capacity to contract.

3b(vii) Corporate administration – 10%

Learning outcomes

On completion of their studies students should be able to

- explain the use and procedure of board meetings and general meetings of shareholders;
- explain the voting rights of directors and shareholders;
- identify the various types of shareholder resolutions.

Syllabus content

- Board meetings: when used and the procedure at the meeting.
- Annual and Extraordinary General Meetings: when used and the procedure at the meeting.
- Company resolutions and the uses of each type of resolution.

3b(viii) Corporate finance – 10%

Learning outcomes

On completion of their studies students should be able to

- explain the nature of a share and the essential characteristics of the different types of share;
- explain the procedure for the issue of shares, and the acceptable forms of payment;
- explain the legal repercussions of issuing shares for an improper purpose;
- explain the maintenance of capital principle and the exceptions to the principle;
- explain the procedure to increase and reduce share capital;
- explain the ability of a company to take secured and unsecured loans, the different types of security and the registration procedure.

Syllabus content

- The rights attaching to the different types of shares issued by companies.
- The procedure for issuing shares.
- The purposes for which shares may be issued.
- The maintenance of capital principle and the ability of a company to redeem, purchase and provide financial assistance for the purchase of its own shares, and the situations in which such powers are useful.
- The rules for the reduction and increase of share capital.
- The ability of a company to borrow money and the procedure to be followed.
- Unsecured loans, and the nature and effect of fixed and floating charges.

3b(ix) Corporate management – 15%

Learning outcomes

On completion of their studies students should be able to

- explain the procedure for the appointment, retirement, disqualification and removal of directors;
- identify the powers and duties owed by directors to the company, shareholders, creditors and employees;
- explain the rules dealing with the possible imposition of personal liability upon the directors of insolvent companies;
- identify and contrast the rights of shareholders with the board of a company;
- explain the qualifications, powers and duties of the company secretary.

Syllabus content

- The appointment, retirement and removal of directors.
- Directors' powers and duties.
- Fraudulent and wrongful trading, preferences and transactions at an undervalue.
- The division of powers between the board and the shareholders.
- The rights of majority and minority shareholders.
- The qualifications, powers and duties of the company secretary.

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Examination Techniques

Computer-based examinations

10 Golden rules

- 1 Make sure you are familiar with the software before you start exam. You cannot speak to invigilator once you have started.
- 2 These exam practice kits give you plenty of exam style questions to practise.
- 3 Attempt all questions, there is no negative marking.
- 4 Double check your answer before you put in a final alternative.
- 5 On multiple choice questions, there is only one correct answer.
- 6 Not all questions will be MCQs – you may have to fill in missing words or figures.
- 7 Identify the easy questions first, get some points on the board to build up your confidence.
- 8 Try and allow five minutes at the end to check your answers and make any corrections.
- 9 If you don't know the answer try process of elimination. Sadly there is no phone a friend!
- 10 Take scrap paper, pen and calculator with you. Work out answers on paper first if it is easier for you.

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Examination Format

The examination is a computer-based assessment, made up of 40 objective test questions. Time allowed is one hour. Pass mark 50 per cent.

Questions are randomly selected from CIMA's own question bank.

The number of questions on each topic reflects the weighting in the syllabus.

Company law	20
Contract	12
Employment	4
English legal system and negligence	4

Such figures are only approximate.

Questions are multi-choice, consideration being required to choose the correct or incorrect statement(s).

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The English Legal System

1

Comparison of Criminal and Civil Law.

(a) Purpose	Criminal punishment of the wrongdoer Civil compensation of the victim
(b) Case brought by	Criminal – the state Civil – the victim
(c) Action	Criminal – prosecution Civil – suing
(d) Burden of proof	Criminal – beyond reasonable doubt Civil – on a balance of probabilities
(e) Court	Criminal – Magistrate’s Court, Crown Court Civil – County Court, High Court
(f) Outcome if defendant loses	Criminal – imprisonment, fine, community service, probation Civil – damages, specific performance, injunction

Judicial precedent

Sources of law

There are two main sources of law in the UK.

- 1 Acts of Parliament (sometimes called statutes).
- 2 Case Law developed by the courts.

The meaning of a judicial precedent

When a Judge decides a case before him, his judgment will have to be based on some legal principle or process of legal reasoning. It is desirable that in all the future cases of a similar kind the same process of legal reasoning should apply.

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Case Law is based on two fundamental principles.

- 1 The doctrine of binding precedent.
- 2 The hierarchy of the Courts.

A Judge is bound to apply the rules of law contained in earlier decisions of a higher Court and usually those of a Court of equal standing.

Not everything said is binding in later cases. We have to distinguish between *ratio decidendi* – the legal principle on which the Judge bases his decision – and *obiter dicta* – other remarks made in passing.

Ratio decidendi

The only thing that binds the Judge in a later case is the *ratio decidendi*, i.e. the legal reasoning for the decision. It is important to note that the *ratio* has nothing to do with the specific facts of the case; it is a general statement of law which is applicable to those material facts (and will be applicable to future cases where the facts are similar).

Obiter dicta

Not every statement of Law in a judgment is binding. Only statements based on facts found in that particular case and on which the decision is based form the *ratio* of the case. All other statements are merely comments of the Judge, which are called *obiter dicta* (things said by the way or in passing).

The hierarchy of the Courts

The *ratio* of a Court establishes a precedent and must be applied in any similar case unless and until it is overruled by a higher Court than the one which first formulated it or by Act of parliament.

The House of Lords

This is the highest Court in England and Wales and its decisions are binding on all lower Courts. Since 1966 the House is no longer bound by its own previous decisions and will depart from its previous *ratio* where the Lords consider it would lead to injustice or would restrict the development of Law.

The Court of Appeal

The Court of Appeal's decisions are binding on all Courts except the House of Lords, but it is bound by its own previous decisions.

The High Court of Justice

A single High Court Judge is bound by the decisions of higher Courts (i.e. the House of Lords and the Court of Appeal) but is not bound by the decisions of another High Court Judge.

Lower Courts

Lower Courts (i.e. Crown, County and Magistrate's Courts) are all bound by decisions of higher Courts.

Exceptions to the doctrine of judicial precedent

A Judge must follow the legal principles pronounced by his predecessors. There are exceptions to this rule.

- (a) The precedent may have been overruled subsequently, either by statute (i.e. a subsequent Act of Parliament) or by a higher Court (e.g. where the House of Lords overrules an earlier decision of the Court of Appeal).
- (b) The original decision may have been made through lack of care by a previous Judge. Later Judges are not bound to follow an earlier Judge who was clearly in error (*per incuriam*).
- (c) The later case may be distinguished on its facts, i.e. the facts of the case are different in a material respect from those of the previous case.
- (d) The *ratio* may be obscured and so cannot clearly be identified. This may occur when a conclusion in a case is reached by more than one Judge, each giving a different reason for his conclusion. (In the House of Lords five Judges will sit, each giving an individual judgment.)

Advantages of judicial precedent

Certainty – ensuring that people can assess their chances of success without wasting time or money.

Reform and flexibility – precedents can be modified and developed to meet the changing needs of society.

A great wealth of detailed rules – cases have been reported for centuries, therefore Judges are guided when making decisions.

Disadvantages of judicial precedent

The danger of illogical decisions – the system encourages a Judge to make artificial distinctions between the cases in order to avoid following precedent.

Rigidity – the binding force of precedent is a restraint on the discretion of the Judge which may lead to an unfair result.

Bulk and complexity of the system – the number of reported cases is so vast that Law can only be ascertained by searching through a large number of reports.

Judge-made law – decisions are made by Judges who are not democratically elected.

Retrospective character – it is retrospective in nature as it is only formulated as the need arises.

The common law

The common law has gradually developed since the Norman Conquest in 1066. By the 12th century, commissioners were being used for legal as well as fiscal and administrative purposes and were referred to as itinerant justices. The itinerants all came from a central source, the justice which they administered also became unified and developed into a law which was common throughout the country, the common law.

The writ system

The injured party in a case would issue a writ against the other party. When an itinerant justice next appeared, the writ would be heard in court and the matter decided.

Parliament, another newly emerging body, regarded the invention of new writs as a usurpation of its powers as the supreme lawgiver and, in 1258, the Provisions of Oxford forbade the practice of creating new writs.

The development of equity

There were a number of problems with the common law.

- (a) It was too rigid, owing to the inability to issue new writs and thereby recognise new problems. Cases had to be fitted into an existing definition.
- (b) It was entangled in procedure, making justice slow and expensive to obtain.
- (c) The only real remedy available was damages, which was not appropriate in every case.

As a result, people who felt they had an unsatisfactory outcome began to petition the King directly. The King delegated the task of hearing such appeals to the Lord Chancellor. In this way an additional branch of law, known as “equity” developed.

Under the new system of equity, cases were decided not exclusively on the basis of what had gone before but on the basis of fairness, justice and morality.

Equity initially concentrated on:

- (a) new rights and the solution to new problems originally not recognised by the common law and
- (b) on the development of remedies, the purpose of which was to counter the inefficiency of injustice of common law.

Its main features were as follows.

- (a) fairness
- (b) flexibility
- (c) additional remedies (injunctions and decrees of specific performance).

Equity did not replace the common law. The common law courts often produced a satisfactory conclusion and no recourse to equity was required. Equity was therefore “a gloss on the common law”, not a substitute for it.

In cases of conflict between the two, however, equity prevailed.

Equitable principles and remedies are discretionary. Common law is available as of right.

The Judicature Acts 1873–1875

Until the 19th century, common law and equity courts remained separate and the injured party had to bring his case in the appropriate court. The Judicature Acts 1873–1875 established what is now known as the Supreme Court, administering both common law and

equity. The plaintiff could now bring his action in the same court, whatever form of remedy he required.

Equitable maxims

- (a) Equity will not suffer a wrong to be without a remedy.
- (b) He who seeks equity must do equity.
- (c) He who comes to equity must come with clean hands.
- (d) Delay defeats equity (the doctrine of laches).
- (e) Equity acts in personam.

Interpretation of statutes

Legislation

In its widest sense the term legislation includes all methods of making law. To legislate is to make new law in any fashion.

In its narrow or strict sense, legislation is that source of law which consists of the declaration of legal rules by a competent authority. In the UK, legislation is made by Parliament.

Legislation may be used to develop law by:

- (a) enacting new law
- (b) repealing old law or altering it
- (c) consolidating existing statutes, e.g. Companies Act 1985
- (d) codifying existing law of all sources which means to bring together law from various sources including decisions of cases and put them into statute.

Law created by legislation is generally referred to as statute.

Forms of legislation

Supreme legislation proceeds from the supreme or sovereign power in the state and therefore cannot be repealed, annulled or controlled by any other legislative authority. In England, supreme legislative authority is vested in Parliament and is expressed in the form of Acts of Parliament.

Subordinate legislation. Parliament delegates some legislative powers to ministers, government departments and the like. Such delegated legislation must remain within the power conferred by Parliament and may be questioned in the courts on the grounds that it exceeds these limits (i.e. it is *ultra vires*).

The legislative process

A statute is law that has been passed by the House of Commons and the House of Lords and has received the Royal Assent.

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The procedure involved is as follows.

First reading

This is purely formal. The title of the bill and the name of the member introducing it is read-out by an official and the bill is then ordered to be printed.

Second reading

This involves a discussion of the general principles of the bill. If nobody opposes it or if a vote is taken on the bill and there is a majority in favour of it, the bill will pass on to the committee stage.

Committee stage

At this stage the bill is examined in detail by a committee made up in the same proportions as the House of Commons.

Report stage

At the report stage, the committee which has considered the bill will report back to the House on its discussion and proposed amendments.

Third reading

This constitutes the final debate on the general principles of the bill and a vote is taken. Assuming the bill passes its third reading, it then passes to the other House.

The House of Lords

The procedure followed in the Commons is repeated in the Lords.

The Royal Assent

After a bill has passed through both Houses of Parliament, it receives the Royal Assent and unless the bill provides anything to the contrary it will immediately become law.

Delegated legislation

This is the procedure whereby Parliament delegates the ability to legislate to ministers or government departments.

Forms of delegated legislation include the following.

- (a) *Orders in council*. These are enacted under powers delegated to the Privy Council (i.e. the Cabinet).
- (b) *Ministerial regulations*. These are known as statutory instruments which are made by individual ministers within some limited sphere relating to their departmental responsibilities, e.g. interest rates on late payment of tax.
- (c) *Bye-laws*. Local authorities are given powers by many Acts of Parliament to make bye-laws operative within their own geographical areas, e.g. on park opening hours and parking regulations.

Advantages of delegated legislation

- (a) It relieves pressure upon parliamentary time.
- (b) Delegated legislation enables rapid changes to be made in the law.

- (c) Subordinate legislation is more flexible than supreme legislation, which can only be changed by more legislation.
- (d) As regards legislation on technical topics, delegated legislation enables legislators to consult with experts and interests concerned.

The main disadvantage of delegated legislation is that it is made by a body which is arguably not truly representative of and accountable to the people.

Judicial approaches to interpretation

Although it is Parliament which produces an Act of Parliament, the real enforcement and application of the individual statute is a matter for the courts. Whenever there is a dispute as to what a particular section of an Act means, it is the Judges in the courts that will decide the meaning, using statutory interpretation rules evolved by the courts.

The literal rule

Words in the statute must be given their ordinary and natural meaning and if they have only one meaning that is deemed to be the intention of parliament, even if the result is considered to be ludicrous or unlikely.

The golden rule

Words are given their ordinary and natural meaning as far as it is possible, but only if that meaning does not produce absurdity. If there is ambiguity, then the court will try to modify the strict grammatical meaning so as to give the provision a rational meaning.

The mischief rule

This rule can only be applied where the words of the Act are ambiguous or uncertain. In such cases, the court can look outside the Act to ascertain:

- (a) What was the mischief which existed before the Act?
- (b) What cure (remedy) did Parliament intend for that mischief?
- (c) What interpretation best gives effect to the cure?

Aids to interpretation

Various guidelines have come into use for the interpretation of statutes.

The *eiusdem generis* rule ("things of the same kind") is that general words which follow two or more particular words in an Act must be confined to a meaning of the same kind (*eiusdem generis*) as the particular words.

The rule *expressio unius est exclusio alterius* means that express mention of one thing implies the exclusion of another.

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Using the rule *noscitur a sociis* (“a thing is known by its companions”), the meaning of a word must be deduced by taking the word in its context.

Presumptions

- (a) Presumption against the alteration of the law unless expressly provided.
- (b) Presumption against ousting the jurisdiction of the courts.
- (c) Presumption against the Act having retrospective effect.
- (d) Presumption that the Act applies to the whole of the UK but not elsewhere.
- (e) Presumption that the crown is not bound by statute.
- (f) Presumption against the imposition of criminal liability without fault.

Internal and external aids to the interpretation of statutes

Internal aids are aids found within the statute itself. They include the following.

- (a) The long title of the Act.
- (b) The preamble.
- (c) The interpretation section.

External aids are aids which are not found in the Act. They include the following.

- (a) Dictionaries.
- (b) Reports of Proceedings in Parliament (Hansard) (*Pepper v Hart* 1992).
- (c) The Interpretation Act 1978.
- (d) Reports of Committees.
- (e) Judicial precedents of interpretation.

European law

Efforts are made to remove differences between member states’ rules governing trade and commerce so that economic activity may be pursued just as easily in one member state as another.

The Single European Act, implemented from 1 January 1993, seeks to create a truly “common” market by allowing for free movement of goods, services, people and capital.

Sources of European law

The European Community is governed by its own law, the sources of which are as follows:

- (a) Treaties made between the member states. The most important is the Treaty Establishing the European Economic Community (known as the EEC Treaty) which was made in 1957.
- (b) Regulations made by the Commission.
- (c) The case law of the European Court of Justice, which is also known as the Court of Justice of the European Communities (CJEC).
- (d) Directives adopted by the Council.

The council consists of one member from the government of every member state and is commonly called the Council of Ministers. The Council makes decisions only by unanimous agreement so that in principle no member state should have a decision imposed on it by the opinion of a majority of members.

In each member state, Community law has effect as if it were part of the member's internal law. Parliament made Community law a part of UK law by enacting the European Communities Act 1972, s2(1).

Conflict between EC and national law

It is possible for Community law to be in conflict with the national law of a member state. For example, national law may require payment of a customs duty that has been prohibited by Community law. The CJEC has repeatedly said that Community law must be given precedence in such a case. In practice, the governments of member states have always acted to remove inconsistencies between national and Community law, though sometimes with reluctance.

The structure of the Courts

The criminal courts of England and Wales

The Magistrate's Court

Personnel

These courts are usually staffed by lay persons (also called Justices of the Peace) who are appointed by the Lord Chancellor. Each bench of magistrates is assisted by a salaried clerk who is legally qualified and advises them on law and procedure. Some magistrate's courts, especially those in larger cities are staffed by professional magistrates known as District Judges.

Jurisdiction

In criminal proceedings the magistrates deal with three main types of offences.

- 1 *Summary offences.* These are only triable by the Magistrate's Court – not assisted by a jury; the maximum penalty that can be imposed by magistrates is six months imprisonment and/or a fine of up to £5,000.
- 2 *Offences triable by either the Magistrate's Court or the Crown Court.* These offences are known as offences triable either way, depending on how serious these offences are. There is a preliminary hearing in the Magistrate's Court. If it is considered serious, the matter will be referred to the Crown Court. The accused has the right to demand for this type of offence to have a trial by jury in the Crown Court. If the offence is tried by the magistrates and the accused is found guilty the magistrates may still commit him for sentence to the Crown Court as their penalty is still limited.
- 3 *Indictable offences.* These are triable by the Crown Court. The most serious criminal offences (e.g. murder, rape) must be tried on indictment in the Crown Court. The magistrates hold a preliminary investigation known as committal proceedings to ensure that the prosecution have sufficient evidence.

Appeals procedure

Only the defendant may appeal from the Magistrate's Court to the Crown Court on the grounds of sentence and/or conviction on questions of law and fact.

The Crown Court

Personnel

There are three types of Judge who may sit in this court: a High Court Judge, a Circuit Judge and a part-time Judge known as a Recorder.

Jurisdiction

The Crown Court deals with the most serious criminal offences (e.g. murder, manslaughter, treason, robbery, etc.). It has an appellate jurisdiction, hearing appeals by the accused on law, fact and sentence from the Magistrate's Court.

Appeals procedure

An appeal would lie to the Court of Appeal Criminal Division by the accused on points of law, law and fact, or against sentence. There is also an appeal to the Divisional Court of the Queen's Bench on a point of law by either prosecution or defence by way of case stated.

The Court of Appeal Criminal Division

Personnel

The head of the court is the Lord Chief Justice and he is assisted by Lords Justices of Appeal. To hear a case usually three of these will sit.

Jurisdiction

The court hears appeals by the accused from the Crown Court on sentence, conviction, questions of law and fact. The court can quash a conviction, reduce a sentence or, in some cases, order a new trial.

Appeals

An appeal lies to the House of Lords. However a point of law of general public importance must be involved and either the Appeal Court itself or the House of Lords must grant permission for the point to be considered by the House.

The House of Lords

Personnel

The head of the court is the Lord Chancellor who is assisted by Lords of Appeal in Ordinary (the Law Lords). When an appeal is heard a minimum of three of these Judges will sit but if the case is of fundamental importance five judges will sit.

Jurisdiction

The House of Lords hears appeals from the Court of Appeal Criminal Division and the Divisional Court of the Queen's Bench. All appeals are on points of law by prosecution or defence.

The civil courts in England and Wales

The Magistrate's Court

Jurisdiction

The civil jurisdiction of magistrates is fairly small. However they do exercise authority in the following areas.

- (a) The Children's Act 1989.
- (b) Affiliation cases.
- (c) Guardianship and adoption proceedings.

- (d) Actions for unpaid council tax and business rates.
- (e) Licensing of betting offices and liquor licenses.

Appeals

Appeal from the decision of magistrates in family matters (items a–c) lies to the Divisional Court of the Family Division and under item e to the Crown Court.

County Courts

Personnel

A county court is staffed by Circuit Judges and District Judges.

Jurisdiction

Matters involving Contract and Tort (civil wrongs), Probate, Uncontested divorce, Landlord and Tenant disputes, Bankruptcy, etc. Within the County Court is also the Small Claims which deals with matters up to £5,000. The procedure is speedier and cheaper and the parties will be bound by the decision.

The High Court of Justice

This is divided into three divisions for administrative purposes: Queen's Bench Division, Family Division and Chancery Division.

Queen's Bench Division of the High Court

Personnel

This is the largest of the three divisions. It is headed by the Lord Chief Justice and is staffed by High Court Judges (puisne judges).

Jurisdiction

It has three types of jurisdiction.

- 1 *Original*. Matters involving contract and tort above the limits available in the County Court. It also has two specialist courts: Commercial and Admiralty.
- 2 *Appellate*. The Divisional Court of the Queen's Bench in its civil capacity hears appeals mainly from tribunals.
- 3 *Supervisory*. This jurisdiction is exercised by the issue of prerogative orders and the writ of *habeas corpus*.

The prerogative orders are as follows.

Mandamus which compels a court, tribunal or public body to carry out its duty.

Prohibition is used to prevent a court, tribunal or public body from exceeding its jurisdiction.

Certiorari may be used to quash a decision made by a court, tribunal or public body.

Family division of the High Court

Personnel

This division is headed by a President and is staffed by High Court Judges.

Jurisdiction

The division is concerned with matrimonial disputes.

The Chancery division of the High Court

Personnel

The effective head of this division is the Vice Chancellor and it is staffed by High Court Judges.

Jurisdiction

This division deals with company and partnership law, trusts, tax, probate, mortgages and certain revenue matters. Two specialist courts – Patents and Company.

The Court of Appeal (Civil division)

Personnel

The court comprises the Master of the Rolls and Lord Justices of Appeal. A hearing is usually in the presence of three such judges.

Jurisdiction

It hears appeals from the County Court and all divisions of the High Court.

Appeal

Appeal, with leave is to the House of Lords.

The House of Lords

Appeals to the House of Lords are with leave of the Court below or of the House itself, either:

On a point of law from the Court of Appeal, or
Directly from the High Court by the “leap frog” procedure.

Alternative dispute resolution

Some disputes can be resolved outside the court process but such bodies exercise important judicial functions.

Tribunals.

Administrative. Set up by statute dealing with disputes arising from matters such as rent, land, social security and employment.

Domestic. Set up generally by professional bodies, e.g. law society, CIMA and ICAEW.

All are expected to act fairly and are supervised by the Queen’s Bench Division by way of prerogative orders.

Arbitration. Some commercial agreements will have a provision that in the event of a dispute between the parties it should be resolved by arbitration. Arbitration is generally quicker and cheaper than the courts. Both parties are bound by the arbitrators’ decision. There is no appeal against the decision.

? Questions

- 1.1 A Parliamentary Bill becomes an Act of Parliament
- A When it passes through the committee stage
 - B On receiving its third reading
 - C When passed by both Houses of Parliament
 - D On receiving the Royal Assent
- 1.2 What is the normal burden of proof placed upon the prosecution in a criminal case?
- A Balance of probabilities
 - B Beyond every reasonable doubt
 - C Beyond any doubt
 - D Beyond reasonable doubt
- 1.3 Which European Community Law-making measure is applicable to members without any need for legislation?
- A An enactment
 - B A decision
 - C A regulation
 - D A directive
- 1.4 Which European Union institution has law making powers?
- A The Council of ministers
 - B The European commission
 - C The European Parliament
 - D The European Court of Justice
- 1.5 There is concern over the validity of certain statutory instruments issued by a minister. How can the courts control such delegated legislation?
- A By applying rules of natural justice
 - B By determining if it is against public policy
 - C By discretionary power to declare void a regulation that is inequitable
 - D By use of the doctrine of *ultra vires*
- 1.6 Statements made *obiter dicta* are:
- A Binding in certain courts hearing similar disputes
 - B Not binding unless made by the House of Lords
 - C Principles of law which relate to the facts of the dispute upon which the decision is based
 - D Not binding on any later court determining a similar dispute but may be regarded as judicial authority
- 1.7 Which of the following is not an example of indirect or delegated legislation?
- A An order in Council
 - B A statutory instrument
 - C A judicial precedent
 - D A bye-law

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1.8 Which of the following statements is *untrue*?

- A Decisions of the House of Lords override statute
- B Appeals can be made from the House of Lords to the European Court of Justice
- C The House of Lords is not bound by its own previous decisions
- D Decisions of the House of Lords bind all lower courts

1.9 What does the "Golden Rule" of statutory interpretation mean?

- A Words should be given their ordinary meaning
- B The meaning of the words can be gathered from their context
- C Words should be given the meaning which is likely to give effect to the purpose or reform which the statute intended
- D Words should be given their ordinary grammatical meaning unless the result is manifestly absurd

 **Answers**

1.1 D

1.2 D

1.3 C

1.4 A

1.5 D

1.6 D

1.7 C

1.8 A

1.9 D

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The Tort of Negligence

2

A tort is a civil wrong, e.g. negligence, nuisance, trespass or defamation.

A tort arises independently of a contract, the basic remedy for a breach being a claim for un-liquidated damages.

The person who commits the tort is known as the Tortfeasor and he will always be liable.

Negligence

For a plaintiff to be successful in his claim the following are the essential elements.

- (a) The defendant owed him a *duty* of care.
- (b) The defendant *breached* that duty.
- (c) As a result the plaintiff suffered *damage*.

Duty of care

People owe a duty to their neighbours to take reasonable care to avoid negligent acts or omissions. *Donaghue v Stevenson*.

The duty of care is owed not only to the primary victim but also to secondary victims for nervous shock.

Statute also imposes a duty of care to occupiers of premises under the Occupiers Liability Act 1957 (visitors) and the Occupiers Liabilities Act 1984 (trespassers).

Breach of duty

As a general rule the plaintiff must show that the defendant failed to take reasonable care. Professional person's standards are higher dependant on the standard and practices at the time. Amateurs undertaking skilled work will have to reach the standard of a competent worker.

Res Ipsa Loquitur

This means the “facts speak for themselves”. Generally the plaintiff must prove that he was owed a duty and it was breached. *Res Ipsa Loquitur* reverses the burden of proof to the defendant to rebut negligence. *Bryne v Boadle*.

Resultant damage

The defendant’s act must be the principal cause of the plaintiff’s loss, i.e. the “But for” test. If the plaintiff would have suffered damage regardless of the defendant’s actions, no liability will arise.

Novus actus interveniens

It is a new act intervening to break the chain of causation between the defendant’s wrongful act and the subsequent damage sustained by the plaintiff.

Remoteness of damage

The damage must be of reasonably foreseeable type. No liability is owed for damages which are too remote – *The Wagon Mound*.

The type of damage must be foreseeable not the precise sequence of events.

Exception being “the Egg Shell Skull rule”, you must take your victim as you find him. *Smith v Leech Brain*.

Negligent misstatement

Professional persons, e.g. solicitors and accountants can be sued for breach of contract should a contractual relationship exist. They can also be sued for negligent statements that are made to third parties.

The basic tests for negligence must be shown – Duty Breach Damage.

Liability is owed for the consequences of negligent statements causing pure financial loss where the parties have a special relationship.

A special relationship will exist where a person makes a statement in an expert or professional capacity and he knows that others may reasonably rely upon it without taking any further advice.

These principles were established in *Hedley Byrne v Heller and Partners* and developed in *Caparo Industries plc v Dickman*.

The current position regarding accountants and auditors is that liability will be owed to the recipient where advice has been:

- (a) Communicated directly or indirectly.
- (b) Used for the specific purpose given.
- (c) Relied upon by the plaintiff.

The Floodgate test applies here, i.e. the giver of the information will be liable only when it would be reasonable to do so in the public interest.

Consequently accountants and auditors owe a duty to the Company as a whole, i.e. the shareholders as a corporate body, not to individual shareholders unless specific assurances were given.

Other issues

Vicarious liability

The person who commits the tort, the tortfeasor, is always liable but another may be held vicariously liable having joint and several liability. This is the situation in an employer–employee relationship.

The employer will be liable where the employee commits a tort within the “course of his employment”.

The employer will not be liable where the employee is acting outside the course of employment.

The principle has no general application to Independent Contractors.

Contributory negligence

The Law Reform (contributory negligence) Act 1943 allows the courts to reduce damages proportionately to the extent a plaintiff has contributed to his own injuries. *Sayers v Harlow UDC*.

Volenti non fit injuria

Meaning – no injury can be done to a willing person.

Volenti equals consent. Consent may be express or implied knowledge of the possibility of harm, it does not amount to consent.

Employees rarely consent voluntarily to the risk of harm. Rescuers or persons acting in an emergency situation also do not consent to potential harm.

Exclusion clauses

The Unfair Contract Terms Act 1977 prohibits the use by business from excluding death or personal injury if caused by their negligence, by the use of disclaimers or notices, such a provision would be void.

Any other exclusion, i.e. for financial loss would be void unless shown to be reasonable.

? Questions

- 2.1 While taking driving lessons John drove negligently and injured his instructor. John's duty of care in this case will be
- A the same as that owed by every driver
 - B that of any unqualified driver
 - C assessed on the basis of John's specific experience and skill
 - D that which might reasonably be expected of a similarly inexperienced driver
- 2.2 In negligence, to prove that damage arose from a breach of duty it must be shown that the breach caused the damage and
- A the type of injury was reasonably foreseeable
 - B the extent of injury was reasonably foreseeable
 - C the particular injury was reasonably foreseeable
 - D both the extent and type of injury was reasonably foreseeable
- 2.3 What is the effect of the maximum *Res Ipsa Loquitur* (the thing speaks for itself) in connection with the tort of negligence.
- A There is no need to prove damage
 - B The plaintiff contributed to his own misfortunes
 - C The plaintiff impliedly assented to the act which caused the injury
 - D The burden of proof is placed on the defendant
- 2.4 Which of the following does not need to be shown in an action for the tort of negligence?
- A That a duty of care was owed to the plaintiff by the defendant
 - B That there was breach of that duty of care
 - C That the defendant intended to harm the plaintiff
 - D That injury or damage was caused by the failure to exercise reasonable care
- 2.5 Tudor Ltd has three employees, Henry, Edward and Mary. In an argument with a customer over Britain's continued membership of the European Union, Henry assaulted the customer. Whilst driving goods on behalf of the company, Edward drove the company's van negligently. Whilst driving a company car to go on her holidays, Mary picked up a hitch-hiker who was injured as a result of Mary's negligent driving. For which of these acts of its employees will Tudor Ltd be vicariously liable?
- A All of them
 - B Those of Edward and Mary
 - C That of Edward only
 - D Those of Edward and Mary
- 2.6 Which of the following statements reflects the position of an occupier of premises as regards his duty to give a warning of danger on the premises?
- A No warning can absolve the occupier for responsibility to lawful visitors to the premises
 - B A warning by the occupier may be adequate for adult visitors to the building but not for children
 - C A warning by the occupier may be adequate for expert visitors to the building but not for other adults
 - D A warning by the occupier will always absolve him from responsibility to lawful visitors to the premises

- 2.7 Edna drove her car negligently and mounted the car causing injury to Fred a pedestrian. Fred's injuries were not serious but unfortunately he suffered from a rare blood disease which resulted in his being off work for six months. Fred was a high flying executive and claims for loss of earnings of £60,000. Edna disputes this claim as excessive. What is the position?
- A Edna is only liable for normal damages. Fred's disease is a *novus actus interveniens* and could not be foreseen
 - B Edna is liable for full damage since she must take her victim as she finds him
 - C Edna will not be liable for full damage. Under the "thin skull" rule the presence of the serious blood disease could not have been foreseen
 - D Edna will be liable only for the damage which could have been foreseen, Fred's loss of earnings were special damages

 **Answers**

2.1 A

2.2 A

2.3 D

2.4 C

2.5 C

2.6 B

2.7 B

Contract

3

Offer and acceptance

Offer

A contract is based on agreement. Agreement = offer + acceptance.

An offer is a definite and unequivocal statement of willingness to be bound in contract without further negotiations.

An offer must be distinguished from an invitation to treat.

Invitation to treat

This is an invitation to another party to make an offer himself. An invitation to treat cannot be “accepted”, because it is not an offer.

Examples of invitations to treat are as follows.

- (a) The display of goods in shop windows: *Fisher v Bell* 1960.
- (b) The display of goods on supermarket shelves: *Pharmaceutical Society v Boots Cash Chemists* 1953.
- (c) Most advertisements: *Partridge v Crittenden*.

Communication of offer to offeree

An offer can only be accepted and hence a binding contract created if it has been communicated to the offeree.

Communication may be either *express* (i.e. oral or written) or *implied* (e.g. through conduct).

An offer can be made to a specific person, to a group of people or to the world at large: *Carlill v Carbolic Smoke Ball Company* 1893.

Termination of an offer

Once terminated an offer cannot be accepted.

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An offer may terminate as follows.

- (a) *Lapse*. Expiry of a time limit, failure to meet a condition and death of one of the parties, or by counteroffer – change in the terms of the original offer.
- (b) *Rejection*. Rejection of the offer by the offeree. A request for further information is not an implied rejection.
- (c) *Revocation*. An offer can be withdrawn (revoked) at any time prior to acceptance provided the offeree has not bought the offeror's promise to keep the offer open: *Routledge v Grant* 1828, but is only valid when received.

Acceptance

Acceptance is an absolute and unqualified consent to all the terms of the offer. Any attempt to vary the terms of the offer may amount to a counteroffer, destroying the original offer. If there is no stipulated method of acceptance, then the offeree can accept by any reasonable method, which can include conduct: *Brogden v Metropolitan Railway* 1877.

If there is a stipulated method (e.g. acceptance must be in writing) then normally the offeree must use this method. Exceptions: silence cannot be an acceptance and the offeree chooses an alternative effective method of acceptance.

Effective date of acceptance

The normal rule is that acceptance is only effective when it is actually received:

Entores v Miles Far East Corporation 1955.

An exception to this is the postal rule. Where acceptance is by post it may be effective from the moment the letter is posted even if it never reaches the offeror, provided:

- (a) the post must be stipulated or reasonable method of acceptance and
- (b) the letter must be properly addressed and properly posted: *Household Fire Insurance v Grant* 1879.

Intention to create legal relations

For a contract to exist and be enforceable the parties must intend to create legally binding relations between themselves.

Commercial agreements

The legal presumption is that the parties to a commercial agreement intend to be legally bound. This can be excluded in the following ways.

- (a) By statute (Trade Union and Labour Relations (Consolidation) Act 1992).
- (b) By express declaration (e.g. the use of words such as “a gentlemen's agreement”, “binding in honour only”).
- (c) By a “without prejudice” clause. This is often used in law to negate legal liability in settlement negotiations.

Domestic agreements

In an arrangement within a family or between friends there is a rebuttable presumption that legal relations were not intended.

Consideration

English law enforces bargains, not promises. A bare promise is unenforceable unless bought by some consideration provided by the other party. A simple definition of consideration might be "The price of the other person's promise".

Executory and executed consideration

Executory – means yet to be done. This means that the consideration has been promised but has yet to pass between the parties (i.e. an exchange of promises to do something in the future).

Executed – means that the consideration has passed at the time the contract is made i.e. present consideration i.e. a promise in return for an act.

The rules on consideration

Consideration must be valuable but it need not be adequate. For example, a person who (foolishly) agrees to sell his Rolls Royce for £1 can be forced to do so, even though £1 is clearly less than adequate consideration: *Chappel v Nestle & Company* 1960 and *White v Bluett* 1853.

Consideration must be sufficient. This means that the promisor must truly incur some form of loss and that the promisee must truly gain some form of benefit. Here are some examples which do not rank as consideration.

- (a) Performance of an existing obligation imposed by law: *Collins v Godefroy* 1831 and *Glasbrook Bros v Glamorgan County Council* 1925.
- (b) Performance of an existing contractual duty owed to the other party to the contract: *Stilk v Myrick* 1809 and *Hartley v Ponsonby* 1857. However, the recent decisions in *Williams v Roffey Brothers* and *Nelson Contractors* 1990 appear to contradict the earlier decision in *Stilk v Myrick*.

Past consideration – 'is no consideration'

The basic rule is that consideration must pass at the time the contract is made (executed consideration) or afterwards (executory consideration), never before: *Re McArdle* 1951.

Exception – Unless there is an implied promise to pay: *Lampleigh v Braithwaite*.

The part payment problem

The issue here is whether a creditor's promise to release his debtor from all or part of the debt can ever be legally enforceable. The rule in *Pinnel's case* 1602 states that payment of a

lesser sum in satisfaction of a greater sum cannot be any consideration for the whole sum, i.e. it could never be sufficient consideration to support a second contract to write-off the balance of the debt.

The principle was upheld in *Foakes v Beer* 1884.

There are several exceptions to the rule in *Pinnel's* case.

- (a) Accord and satisfaction – accord means that both the parties agree freely to the part payment. Satisfaction might be payment at an earlier date, payment at a different place, payment in a different currency, payment through the giving of a chattel, etc.
- (b) Agreement by deed.
- (c) Part payment by a third party.
- (d) Composition with creditors.
- (e) Promissory estoppel.

The doctrine of promissory estoppel as equity is based on the principles of fairness and justice. The doctrine may operate to prevent a person going back on his promise to accept a lesser amount for a period of time, provided the following conditions are satisfied.

- (a) There is an existing contract between the parties.
- (b) The claimant must voluntarily waive his right under the contract.
- (c) There must be an intention that the defendant should rely on the waiver.

The principle was propounded in *Central London Property Trust v High Trees House* 1947. However there are a number of limitations on the principle.

- (a) It is a shield not a sword, i.e. it is a defence not a cause of action: *Combe v Combe* 1951.
- (b) It may only have a suspensory effect as shown in the *High Trees Case*. (The claimant's rights were suspended during the particular circumstances of the Second World War, but might be revived later.)
- (c) The party seeking to use it as an equitable defence must also have acted fairly in his dealings with the claimant: *D and C Builders v Rees* 1966.

Privity of contract

The meaning and effect of privity

Privity of contract states that, as a general rule, a contract cannot confer rights or impose obligations on anyone except the parties to the contract. Third parties cannot sue for the carrying out of promises made by the parties to a contract.

Two cases illustrate the point: *Tweddle v Atkinson* and *Dunlop Pneumatic Tyre Company Ltd v Selfridge*.

Exception to the general rule

- (a) *Trusts*. The beneficiary of a trust can enforce a trust's terms against the trustee even if the beneficiary has provided no consideration.
- (b) *Collateral Contracts*.

- (c) *Operation of law*. If the rights of one party to the contract pass by operation of law to another person, that other person may enforce those rights (e.g. when a company goes into liquidation).
- (d) *Assignment*. It is possible for one party to a contract to assign his rights and liabilities under the contract to another person, provided the other party to the contract has consented.
- (e) *Property*. The law of property has developed rules whereby a vendor of land may, as part of a contract to sell the land, impose a restriction on its use which he can enforce despite subsequent changes in ownership of the land. For example, when a house is sold it might be a condition that it never be used for business purposes. The condition will be enforceable even against anyone who subsequently buys the house and is not a party to the contract with the original owner.
- (f) *Statutory exception*. Where a husband or wife insures his or her own life, his or her spouse and children may enforce the contract with the insurance company (Married Women's Property Act 1882).
- (g) *Contracts Rights of Third Parties Act 1999*.

Terms of a contract

Conditions and warranties

The terms of a contract define the obligations of the parties and the remedies available if either party is in breach of contract. It is usual to classify each term of a contract as being either a condition or a warranty.

Conditions are terms which are so vital to a contract that non-performance may be treated by the innocent party as a substantial failure to perform the contract (*Poussard v Spiers* 1876).

Breach of condition – the innocent party may:

- (a) Repudiate the contract and if relevant sue for damages, i.e. he may refuse to accept performance and treat the contract as discharged, suing for any loss he incurs as a result.
- (b) Affirm the contract and sue for damages, i.e. he may continue with the contract, accept performance and sue at the end for any resultant loss.

Warranties are terms which are subsidiary to the main purpose of the contract such that their non-performance does not represent a substantial failure of the contract: *Bettini v Gye* 1876.

Breach of warranty – the innocent party must affirm the contract (i.e. continue with the contract), suing at the end for any resultant loss.

Innominate terms

A third “intermediate” type of term has been created to make the law on terms more flexible: innominate terms. These are terms whose breach may or may not cause a contract to fail substantially. This will depend on the consequences of the breach (*The Hansa Nord* 1976).

Express terms and implied terms

Express terms are terms expressly inserted into the contract by the parties. Such terms may be written, oral or a combination of both.

Implied terms are terms which have not been expressed by the parties but which for various reasons are contained within the contract. Terms may be implied into a contract by custom, by the courts or by statute.

Terms implied by custom:

Any contract may be deemed to include any relevant custom of the market.

Terms implied by the courts:

- (a) *Lack of business efficacy*. Here the court considers that the parties must have intended to include the term, because otherwise the contract would not be workable (The *Moorcock* 1889).
- (b) *By custom or trade usage*.
- (c) *Imbalance of bargaining strength*. In such a case the court may imply a term where it is just and reasonable to do so rather than strictly necessary (Liverpool City Council *v* Irwin 1977).

Terms implied by statute:

Parliament has decided that in certain types of contract the imbalance of bargaining power is so wide that statute is needed to ensure that certain terms are always implied into contracts. An example is the Sale of Goods Act 1979 which primarily seeks to protect the consumer when otherwise the rule of *caveat emptor* would imply (let the buyer beware).

SGA 1979 implies the following conditions in contracts for the sale of goods:

- S12 Title (Ownership)
- S13 Description
- S14 Quality and Fitness
- S15 Sample

Exclusion clauses

Validity tests

An exclusion clause is one which seeks to exclude or restrict the obligations of one of the parties under the contract.

To counter the more unfair aspects of exclusion clauses the person seeking to rely on the clause must prove that it passes various tests arising from both common law and statute.

Common law requirements

In order to be valid a first requirement is that the clause must be properly incorporated into the contract (i.e. it must be a term of the contract).

A person who signs a contractual document is bound by its terms even if he has not read them: *L'Estrange v Graucob* 1939.

A clause contained in an unsigned document will only be incorporated into the contract if “reasonable steps” are taken before the contract is made to bring it to the attention of the party who will be prejudicially affected by it.

An exception to the above rule arises where there have been regular and consistent dealings between the parties.

If the parties have entered into a regular number of contracts over a period of time using a form with consistent terms, such terms, including an exclusion clause, might be incorporated into the agreement, even if, in an isolated case, some contractual term is missing: *Spurling v Bradshaw* 1956 (Regular number – *Hollier v Rambler Motors*. Consistent terms – *McCutcheon v David MacBrayne*).

The contra proferentem rule

In order to be valid the clause must be worded so as to exclude the loss in question.

If the wording of the clause is ambiguous the courts will interpret it *contra proferentem*, i.e. in the way least favourable to the party seeking to rely on it: *Houghton v Trafalgar Insurance* 1954.

Statutory requirements relating to exclusion clauses

The main source of statutory regulation in this area is the Unfair Contract Terms Act 1977 (UCTA 1977).

This severely limits the ability of a party to exclude liability, both in contracts, generally and more specifically in contracts for the sale of goods.

Provisions of the 1977 Act

Clauses excluding liability in negligence are only valid in limited circumstances.

- (a) Death or personal injury – liability for negligence resulting in death or personal injury can never be excluded. Such clauses are therefore void.
- (b) Other economic loss – liability for negligence resulting in damage to property or other economic loss can be excluded but only if such exclusion is reasonable.

The following criteria under UCTA 1977 are therefore relevant in determining reasonableness.

- (a) Bargaining strength of the parties.
- (b) Choice.
- (c) Inducement.
- (d) Knowledge of the existence of the clause.
- (e) Insurance cover.

This is illustrated in the case of *St Albans City Council v ICL Limited* 1994.

The UCTA 1977 also has relevance to the SGA 1979. S12 can never be excluded, S13, 14 and 15 can never be excluded in a consumer sale but can be excluded in a non-consumer sale but only if such exclusion is reasonable.

The unfair terms in Consumer Contract Regulations 1999 makes any term void if the contract was not individually negotiated and is detrimental to the consumer.

Misrepresentation

Definition of a misrepresentation

In negotiations leading to a contract many statements may be made. Those statements which are incorporated into the final contract become contractual terms; those not incorporated may be representations, which if untrue are called misrepresentations. A misrepresentation is a false statement of material fact made by one party (the misrepresenter) before or at the time of the making of the contract, which was intended to (and did) induce the other party (the misrepresentee) to enter into the contract. The effect of a misrepresentation on a contract is to render it voidable (but not void) i.e. valid unless and until avoided.

The definition of misrepresentation can be broken down into the following elements.

A statement

Silence does not amount to a misrepresentation. Therefore in general there is no duty to volunteer information.

To this rule there are exceptions: half truths; change in circumstances; contracts of utmost good faith (contracts *uberrimae fidei*) such as insurance contracts.

A statement of fact

The statement must be of fact, not of law, opinion or intention: *Bisset v Wilkinson*. A statement of opinion may amount to a misrepresentation if the opinion was not honestly held (*Smith v Land and House Property Corporation* 1884) or if the opinion was that of an expert (*Esso Petroleum v Mardon* 1975).

The statement must be one of existing fact, not future intention. However, a statement of intention may amount to a misrepresentation if the intention was not honestly held: *Edginton v Fitzmaurice* 1885.

A statement of fact which is false

A statement is false not only if it is untrue but where it is true but misleading in the context: *Nottingham Patent Brick Company v Butler* 1866.

A statement made by one contracting party

The statement must be made by one of the contracting parties or his agent.

A statement which induced the other party to enter into the contract

Induced means that the statement must be one of the reasons the misrepresentee entered into the contract – it need not be the only reason.

Types of misrepresentation and remedies

- (a) Fraudulent misrepresentation occurs where the misrepresenter knows that the statement is untrue or is reckless as to its truth or falsity. *Remedies* – the misrepresentee may either rescind the contract, or claim damages for deceit.

- (b) Negligent misrepresentation occurs where the misrepresenter believes the statement is true but does not take reasonable care to ascertain its truth or falsity. *Remedies* – the misrepresentee may claim damages either for negligence or under s2(1) Misrepresentation Act 1967.
- (c) Innocent misrepresentation occurs where the misrepresenter is neither fraudulent nor negligent, i.e. he genuinely believes his statement to be true. *Remedies* – rescission or damages. However, if rescission is unavailable damages in lieu of rescission will not be granted by the court. Therefore in some instances there is no remedy for an innocent misrepresentation.

Rescission is an equitable remedy (and therefore discretionary) which restores the parties to their exact pre-contractual position.

There are, however, certain limitations or bars to rescission:

- (a) affirmation
- (b) lapse of time
- (c) full restitution (*resitutio in integrum*) is impossible
- (d) third-party intervention.

Discharge of contract

Performance

Discharge of contract releases the parties from their mutual obligations. There are various ways in which this can happen.

- (a) By performance.
- (b) By breach.
- (c) By frustration.
- (d) By agreement (i.e. the parties mutually agree to terminate their contract).

The rule on performance

The general rule is that performance must be complete, exact and precise for the contract to be discharged. Exceptions:

- (a) *Severable of divisible contracts*. For example, 100 tons of coal to be delivered in 10 ton consignments.
- (b) *Performance prevented by one party*. If one party prevents the other's performance the party not at fault can recover a reasonable sum for what he has done – *quantum meruit* (*Planche v Colburn* 1831).
- (c) *Acceptance of partial performance*. If one party freely and voluntarily accepts part performance then the other party can claim a *quantum meruit* (*Sumpter v Hedges* 1898).
- (d) *Substantial performance*. This occurs where the party has done all that was agreed but with defects (*Hoenig v Isaacs* 1952).

Breach

Remedies for breach

Although every breach of contract entitles the innocent party to claim damages, not every breach has the effect of discharging the contract and thus releasing the innocent party from his obligations.

- (a) Breach of condition entitles the innocent party to repudiate his future obligations.
- (b) Breach of warranty only entitles the innocent party to claim damages not to repudiate.

Types of breach of condition

- (a) *Actual breach*. This is where one party refuses to perform his side of the bargain after the due date or performs incompletely. The cases of *Poussard v Spiers* and *Bettini v Gye* are examples.
- (b) *Anticipatory breach*. This is where one party announces in advance of the due date for performance, his intention not to perform his side of the bargain, either expressly or by implication. The innocent party may sue immediately for damages on the announcement of the breach.

Where the innocent party requires no further co-operation from the other party, he can elect to affirm the contract, complete his part of the agreement and claim damages: *White and Carter v McGregor* 1962.

Frustration

Circumstances where a contract is frustrated

This occurs where events occur after the contract has been made which make the agreement impossible to perform. These events must be brought about by external factors beyond the control of the contracting parties.

Frustration applies in the following circumstances.

- (a) Supervening illegality (*Re Shipton, Anderson & Company* 1915).
- (b) Destruction of the subject matter (*Taylor v Caldwell* 1863).
- (c) Non-occurrence of the event on which the contract is based (*Krell v Henry* 1903).
- (d) Death or serious illness in a contract for personal services (*Robinson v Davison* 1871, *Condor v The Barron Knights* 1966, *Hare v Murphy Bros* 1974).
- (e) An extensive interruption which alters performance (*Metropolitan Water Board v Dick Kerr & Company* 1918).

Frustration does not apply in the following situations (i.e. these are non-frustrating events).

- (a) Self-induced frustration – this means that one party by his own choice induces impossibility which could have been avoided (*Maritime National Fish v Ocean Trawlers Limited* 1935).
- (b) Performance becomes more difficult or expensive (*Tsakiroglou v Noble & Thorl* 1962).
- (c) Where one party finds he cannot achieve what he has contracted to do.

The effects of frustration

Where frustration is found to exist the provisions of the Law Reform (Frustrated Contracts) Act 1943 apply. The consequences are as follows:

- (a) All sums paid are recoverable.
- (b) All outstanding balances cease to be payable.
- (c) If one party has incurred any expenses prior to frustration a reasonable sum may be claimed for that expenditure.
- (d) If one party has received some benefit prior to frustration, he must pay for that benefit.

Discharge by express agreement

Discharge by agreement (accord and satisfaction)

The parties may decide before either of them has performed his side of the contract that they will not perform it or that they will both do something different instead.

Their agreement to discharge the contract will be valid without any formality. The consideration is their mutual release. This is known as bilateral discharge.

Sometimes, one party will agree to excuse or release the other party from performance, even though he himself has already performed his part of the contract. This is known as unilateral discharge.

New agreement

A new agreement may be entered into by the parties to the original contract, whereby the earlier contract is replaced by a later one. This is termed novation. However, this will be effective only if both parties still had to perform their obligations under the earlier contract.

Provision for discharge

A provision may be incorporated in a contract whereby the contract will automatically be discharged if:

- (a) A condition is not fulfilled, which is termed a condition precedent (*Head v Tattersall*).
- (b) A certain event occurs, which is termed a condition subsequent.
- (c) The contract contains a term that either party may terminate by notice (e.g. contracts of employment).

Form of agreement to discharge

An agreement to discharge does not normally require any particular format; indeed, a contract under seal may be discharged by an oral agreement.

However, a contract which must be evidenced in writing (e.g. a money lending contract can only be varied in writing).

Remedies for breach of contract

Damages

This is the basic remedy available for a breach. It is a common law remedy that can be claimed as of right by the innocent party.

The object of damages is usually to put the injured party into the same financial position he would have been in if the contract had been performed properly.

Liquidated damages and penalty clauses

The parties may agree a sum to be paid in the event of a breach. This sum may be either liquidated damages or a penalty. Only liquidated damages are enforceable.

- (a) A liquidated damages clause is a genuine attempt at estimating the loss prior to the breach and is enforceable by either party to the contract. It does not have to be an exact figure.
- (b) Penalty clauses are clauses inserted *in terrorem*, i.e. to force a party to perform his obligations. The amount will be penal and thus designed to punish a party for the breach. Such clauses will not be upheld by the courts.

A clause is likely to be construed as a penalty clause if it exhibits any of the following features:

- (a) The figure stipulated is “extravagant and unconscionable”.
- (b) The figure stipulated is the same for both major and minor breaches.
- (c) Where the breach is a monetary breach, the figure stipulated is greater than the breach.

Unliquidated damages

These are damages awarded by the court in the light of the criteria outlined below. The rules for assessment of such damages were laid down in the case of *Hadley v Baxendale*. They state that the defendant will not necessarily be responsible for all the consequences of his breach as some damages may be considered too remote. The remoteness rules are as follows.

- (a) Normal loss (i.e. general damages) arises naturally from the breach such that the parties should have had it in contemplation as likely to occur as a consequence of any breach.
- (b) Abnormal loss (i.e. special damages) does not arise naturally from the breach but may still reasonably be supposed to have been in the contemplation of the parties at the time of making the contract.

The measure of damages

This is the sum required to restore the innocent party to the position he would have been in but for the breach. Therefore if there is no actual loss (e.g. because the buyer can get alternative goods more cheaply), only nominal damages are available. *Lazenby Garages v Wright* 1976.

Under the doctrine of restitution, the plaintiff is entitled to damages measured by the value to him of the contract broken, and not by the cost of performance to the defendant. The

injured party should seek to minimise the loss suffered (*Brace v Calder*). Although the measure of damages in contract is usually for financial loss other types of loss may also be recovered (e.g. personal injury, damage to property and mental distress such as frustration, disappointment and vexation). However all these types of loss are subject to the rule that damages which are too remote cannot be recovered. The difficulty of accurately assessing damages is no reason for refusing to grant any compensation at all, even though the assessment of damages is almost a matter of guesswork: *Chaplin v Hicks* 1910.

Equitable remedies

As equity is based on equality, fairness and justice then such remedies are only available where the court in its discretion considers that such a remedy is appropriate in all the circumstances of the case and is fair in relation to both parties to the agreement. Therefore equity has the following maxims which it takes into account when deciding whether to grant an equitable remedy.

- (a) "He who comes to equity must come with clean hands" or "he who seeks equity must do equity".
- (b) "Equity will not suffer a wrong to be without a remedy".
- (c) "Delay defeats equity" also known as the "doctrine of laches".

Usually the common law remedy of damages is sought for breach of contract. There are other possible remedies however.

Specific performance

This is an equitable remedy, being an order requiring the defendant to perform the contract – only available where the goods are rare or unique.

Specific performance is not available in the following circumstances.

- (a) Damages provide an adequate remedy.
- (b) The court cannot supervise performance.
- (c) The contract is for personal services.
- (d) It would not be just and equitable.
- (e) Not mutually enforceable.

Injunction

This is an equitable remedy and like all remedies granted by equity it is discretionary and available only in equitable circumstances. It is an order restraining the defendant from breaching his contract: *Warner Bros v Nelson* 1937.

Quantum meruit

This means "as much as he has earned" and is an equitable claim to compensate a person for a breach: *Planche v Colburn* 1831.

Limitation of actions

A claim for damages which is commenced outside the statutory limitation period is barred under the Limitation Act 1980. Such a contract is unenforceable.

The time periods are as follows.

- (a) *Simple contracts* – six years.
- (b) *Specialty contracts* (i.e. contract made by deed) – twelve years.
- (c) *Personal injury or death* – three years.

The period commences on the date the contract was breached, subject to exceptions (e.g. disability or fraud).

? Questions

- 3.1 An advertisement to sell a car in a newspaper will amount to
- A an offer
 - B a mere statement of price
 - C an invitation to treat
 - D a declaration of intent
- 3.2 What is the consequence if a contract is void at law?
- A It is the destitute of legal effect
 - B Further performance is excused
 - C The innocent party may repudiate
 - D Either party may repudiate
- 3.3 An offer was made by letter posted in London and delivered in Birmingham. A reply was made by fax machine in Manchester and received by the offer's fax machine in Liverpool. Where is the contract made?
- A Where the offer was made in London
 - B Where the acceptance was put into the fax machine in Manchester
 - C Where the acceptance was received on the fax machine in Liverpool
 - D Where the letter making the offer was received in Birmingham
- 3.4 In relation to social and domestic agreements the court
- A assumes the parties did intend to create a legally binding contract
 - B presumes that the parties did not intend to create a legally binding contract
 - C does not consider the intention of the parties
 - D does not make any presumptions about the intention of the parties
- 3.5 The equitable remedy of Rescission will
- A order that the parties terminate their actions under the contract
 - B force the parties for any reasonable acts they have undertaken
 - C remunerate the parties for any reasonable acts they have undertaken
 - D order that the parties are places in their exact pre-contractual position
- 3.6 S offers to sell his car to B for £10,000 cash. At what point in time does the contract come into being?
- A When B accepts the offer
 - B When B pays S the £10,000
 - C When the agreement is written down
 - D When the agreement is signed
- 3.7 D owes £4,000 to C. Two weeks before the debt is due for payment C approaches D and promises to accept £3,500 in full and final settlement if D will pay that sum immediately. D agrees and immediately pays £3,500 to C. Which of the following statements is/are correct?
- (i) C is bound by his promise as per common law
 - (ii) C is estopped by equity from going back on his promise

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- A (i) only
- B (ii) only
- C Both (i) and (ii)
- D Neither (i) nor (ii)

3.8 A plc has been induced to enter into a contract by the fraudulent misrepresentation of B.

Which of the following is *incorrect*?

- A A plc may be able to rescind the contract
- B A plc may be able to claim damages and then rescind the contract
- C A plc is entitled either to rescind the contract or to claim the damages
- D A plc is entitled to refuse to perform the contract if it is still executory

3.9 In the event of a breach of contract, the difference between a condition and a warranty is important because it determines

- A the measure of damages available to the innocent party
- B the type of damages available to the innocent party
- C the remedy available to the innocent party
- D whether or not the court will exercise its discretion to grant specific performance

3.10 Builder Ltd increase the contracted price to erect an office block for Mega plc; the building is to be ready for occupation by the end of 2004. Due to Builder Ltd's lack of adherence to safety requirements, the Health and Safety Executive have issued a notice prohibiting further work on the site until safety measures as per its improvement notice are implemented by Builder Ltd.

Which one of the following gives the correct position?

- A Builder Ltd increase the contract price to cover the costs of implementing the safety measures
- B Builder Ltd will be in breach of contract if it fails to complete the office block by the due date
- C If Builder Ltd fail to complete the office block by the due date it will not be in breach of contract provided it shows that it has taken all reasonable steps to do so
- D The contract between Builder Ltd and Mega plc is frustrated by the HSE's actions

3.11 Which of the following statements relating to remedies for breach of contract is/are *correct*?

- (i) Damages will not be ordered where the claimant has acted unfairly
- (ii) Damages will not be ordered where specific performance is an adequate remedy

- A (i) only
- B (ii) only
- C Both (i) and (ii)
- D Neither (i) nor (ii)

3.12 Steve by letter offered to sell Mack 800 tonnes of iron at £40 per ton "open till Tuesday". On Monday Mack sent a telex to Steve inquiring if Steve "would accept £40 for delivery over two months". No reply was received so later that day Mack sent a letter accepting the offer of £40 per ton which was posted first class and arrived on Tuesday. Meanwhile Steve had sold the goods to Dave on Monday evening and informed Mack by letter posted on that day. Mack sues Steve for breach of contract. What is his position?

- A Mack will succeed. His telex was a mere inquiry and he had accepted Steve's offer by post and therefore the offer had not expired
- B Mack will not succeed, his telex was a counter-offer which causes Steve's offer to lapse
- C Mack will succeed, provided he can show that there was consideration for keeping the offer until Tuesday
- D Mack will not succeed. The offer was revoked by Steve by letter on Monday before Mack's acceptance was received on the Tuesday

3.13 Robert's wife Kate, expressed the wish that Robert, if he survived her, should have the use of her house. After Kate's death her executor agreed to allow Robert to occupy the house (i) because of Kate's wishes and (ii) on the payment by Robert of £24 per year.

Robert seeks to enforce this agreement and the executor wishes to avoid it in order to sell the house. What is the legal position?

- A Robert can enforce the agreement on the basis of his deceased wife's wishes
- B Robert cannot enforce the agreement because the promise to pay is not consideration
- C Robert can enforce the agreement because the promise of £24 per year provides consideration for it
- D Robert cannot enforce the agreement because £24 per year is not sufficient consideration

3.14 Frustration discharges a contract when

- A a contract is impossible to perform at the time it is made
- B an event occurs after the contract has been made rendering the performance more difficult and expensive to perform
- C an event occurs after the contract has been made rendering its performance impossible
- D a party expressly promises to do something which he later decided is not in his best interests

3.15 By deed Victoria contracted to buy a herd of cows from Albert. She has failed to pay for them. Within what period of time must Albert bring an action to recover the amount owed to him?

- A A reasonable period of time
- B Six years
- C Twelve years
- D No limit

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- 3.16 Which of the following contracts must be effected in the form of a deed to be enforceable?
- A A hire purchase contract
 - B An agreement to guarantee the debt of another person
 - C A contract to lend money
 - D A promise in return for no consideration
- 3.17 A offers to sell certain goods to B for £150. B responds by sending a cheque to A for £140 and giving instructions for delivery of the goods. What is the effect of B's response?
- A It constitutes an acceptance of A's offer
 - B It causes A's offer to lapse
 - C It frustrates A's offer
 - D It constitutes a counter-offer, thereby destroying A's offer
- 3.18 Rosemary offered by letter to sell Mary her motorbike for £5,000. Mary wrote back saying she accepted the offer and would pay in two instalments at the end of the two following months. Is there a contract?
- A No, because Mary is trying to amend the contractual terms, Rosemary can be assumed to revoke the offer
 - B Yes, there has been an offer and acceptance and a binding contract applies
 - C No, Mary's response constitutes a counter-offer and is effectively a rejection of Rosemary's offer
 - D Yes, Mary's response is merely a clarification of contractual terms
- 3.19 Which of the following rules regarding consideration is *incorrect*?
- A Every simple contract must be supported by consideration
 - B Consideration must move from the promisee
 - C Consideration must be adequate
 - D Consideration must be sufficient
- 3.20 A number of children, by their father's will, were entitled to a house after their mother's death. During the mother's life, one of the children and his wife lived with her in the house. The wife made various improvements to the house, and at a later date all the children signed a document addressed to her, stating that "in consideration of your carrying out certain alterations and improvements to the property, we hereby agree that the executors shall repay to you from the estate, when distributed, the sum of £488 in settlement of the amount spent on such improvements". The agreed sum was not paid. The wife's action to recover the sum will fail on the ground that?
- A There was no intention to create legal relations
 - B Past consideration is not consideration
 - C The document should have been registered
 - D The contract was illegal
- 3.21 The doctrine of privity of contract means
- A a contract is not legally binding if it is a private agreement
 - B only the parties to a contract can enforce it
 - C the terms of a contract are primarily the concern of the parties to it
 - D an ambiguity in the contract will be interpreted against the party trying to avoid liability

- 3.22 Karen wrote to Joe and offered to sell her Ford Capri to him for £2,000. Joe wrote back saying that he accepted but would not be able to pay until the end of the month. Karen did not reply so Joe went to her office with £2,000 in cash and demanded the car. Is there a contract between Karen and Joe?
- A Yes, as Karen has made a valid offer which Joe has accepted
 - B Yes, as Joe's response was a request for further information and his action in bringing the money to Karen's office constitutes valid acceptance
 - C No, as Joe's response constitutes a counter-offer which has the effect of destroying Karen's original offer
 - D Yes, as Karen's initial offer stays open until expressly revoked
- 3.23 Under the Sale of Goods Act, when is there an implied condition of satisfactory quality?
- A Only if the seller is selling in the ordinary course of business
 - B If the seller is selling in the course of business
 - C If the seller is selling in the course of a business to a person buying as a consumer
 - D In all contracts for the sale of goods
- 3.24 An agreement to carry out an act already required by law amounts to
- A inadequate consideration
 - B illegal consideration
 - C past consideration
 - D insufficient consideration

 **Answers**

3.1 C

3.2 A

3.3 C

3.4 B

3.5 D

3.6 A

3.7 A

3.8 C

3.9 C

3.10 B

3.11 D

3.12 A

3.13 C

3.14 C

3.15 C

3.16 D

3.17 D

3.18 C

3.19 C

3.20 **B**

3.21 **B**

3.22 **C**

3.23 **B**

3.24 **D**

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Employment Law

4

Employment and self-employment

There are two main types of employment.

- 1 An employee has a contract *of* service.
- 2 A self-employed person has a contract *for* services.

The distinction is important for the following reasons.

- (a) Only employees are given statutory protection against unfair dismissal, redundancy, etc.
- (b) Only employees have implied into their contract certain common law duties of employer and employee.
- (c) Only employees can make their employers vicariously liable for their torts (i.e. for any damage caused by their acts or omissions).
- (d) Only employees are entitled to certain state benefits.
- (e) Employees' tax is deducted through PAYE and assessed under Schedule E.
- (f) An employer must pay National Insurance contributions in respect of every employee.

As it is not always easy to determine the difference, the courts have developed a number of tests to distinguish between workers who are employed and workers who are self-employed.

The control test

The test was set out in *Yewens v Noakes* 1880: "a servant is a person subject to the command of his masters as to the manner in which he shall do his work".

The integration test

This test (also called the organisation test) applies if the person's work is integrated into the business of the employer. If so, he is an employee (*Cassidy v Ministry of Health* 1951).

The economic reality test

This test looks at a number of different factors to decide on the economic reality of the working relationship. The leading case on the matter is *Ready Mixed Concrete v Minister of Social Security* 1969.

In this case it was stated that there was no exhaustive test or strict rules laid down as to factors which identified a contract of service. However factors which will be considered include the following.

- (a) The degree of control by the employer.
- (b) The degree of risk taken by the worker.
- (c) Ownership of tools and equipment.
- (d) Regularity of payment methods.
- (e) Regularity of obligations.
- (f) Regularity of hours.
- (g) Ability to provide a substitute.

Formation of the employment contract

The contract will consist of express terms, implied terms and statutory terms.

- (a) *Express terms*. Under the Employment Rights Act 1996 a statement of particulars must be given by the employer to the employee within two months of the commencement of employment. This must cover details such as pay, holidays, job title, etc.
- (b) *Implied terms*. Certain terms are implied into the employment contract by the common law and the courts, even if they are not expressly stated.
- (c) *Statutory terms*. Terms relating to employment are laid down in the Equal Pay Act 1970, the Sex Discrimination Act 1975 and other legislation.

Duties of employee and employer

Duties of the employee

- (a) A duty to obey lawful reasonable orders (*Pepper v Webb* 1968).
- (b) A duty of mutual co-operation, i.e. to perform work in a reasonable manner (*Pepper v Webb* 1968).
- (c) A duty to exercise reasonable care and skill (*Harmer v Cornelius* 1858, the plaintiff was given a job as a scene painter. In fact he was incompetent).
- (d) A duty of good faith, i.e. a duty to give loyal and faithful service. This duty includes the following.
 - 1 Not to make a secret profit: *Boston Deep Sea Fishing and Ice Company v Ansell* 1888.
 - 2 Not to compete with his employer's business: *Hivac Limited v Park Royal Scientific Instruments Limited* 1946.
 - 3 Not to disclose trade secrets or misuse confidential information: *British Syphon v Homewood* 1956.
- (e) A duty to render personal service, i.e. not to delegate the performance of his work.

Duties of the employer

- (a) A duty to pay reasonable remuneration.
- (b) A duty to indemnify the employee for reasonably incurred expenses in the performance of his duties.
- (c) A duty to provide a safe system of work.
- (d) A duty to give reasonable notice of termination of employment.
- (e) A duty of mutual co-operation, trust, confidence and respect. In *Wares v Caithness Leather Products 1974* an employer abusively reprimanded a woman in foul language.

Termination of employment

Methods of terminating the contract

- (a) *Termination without notice by the employer*. This is called summary dismissal and may be justified if the conduct of the employee prevents the continuance of employment.
- (b) *Termination without notice by the employee*. This is often a breach of contract unless the behaviour of the employer justifies the act (e.g. constructive dismissal).
- (c) *Termination with notice*. A notice period may be agreed expressly or by implication but cannot be less than the statutory minimum. A fixed-term contract expires. No notice is required.
- (d) *Termination by agreement*.
- (e) *Termination by operation of law*. For example, through frustration, dissolution.

Breach of contract

In some cases termination of employment will constitute a breach of contract.

- (a) The employee will be in breach of contract if he terminates his employment without giving the agreed notice or breaches some other term of his contract. The employer may then dismiss the employee without notice if the breach is serious and can sue for damages.
- (b) The employer may be in breach in cases of summary dismissal or constructive dismissal.

Constructive dismissal refers to situations where an employer makes it practically impossible for an employee to continue in his job, without actually dismissing him (*Donovan v Invicta Airways 1970*).

The employee's remedies are as follows.

- (a) If he was dismissed correctly, with proper notice, he has no claim against the employer.
- (b) If he was dismissed rightfully, but without proper notice, he may sue for unpaid wages.
- (c) If he was dismissed wrongfully, and without proper notice, he can claim wages due plus damages for wrongful dismissal, or a *quantum meruit* payment, or an injunction against the employer.

Note that damages are compensatory and may be reduced if the employee fails to mitigate his loss: *Brace v Calder 1895*.

Unfair dismissal

Here the employer terminates the contract without justifiable reason. Only employees who qualify can claim, therefore the following criteria must be established.

- (a) The employee must not be over retirement age.
- (b) He must have been continuously employed for at least one year.
- (c) He must have made a claim to the Industrial Tribunal within three months.
- (d) He must prove he was dismissed.

The employer, to defend himself, must show the main reason for dismissal was one which is permitted under statute.

The five permitted reasons are as follows.

- 1 Lack of capabilities or qualifications to perform the kind of work he is required to do.
- 2 Conduct (*Stevenson v Golden Wonder 1977*).
- 3 Redundancy.
- 4 Where continued employment would contravene a statute.
- 5 Some other substantial reason – of a kind such as to justify the dismissal of an employee.

Reasonableness

Once the employee has shown he was dismissed and the employer has shown it was for one of the five reasons outlined above it is then for the tribunal to decide whether the dismissal was fair on reasonableness grounds.

Inadmissible reasons

The Employment Rights Act 1996 sets out a number of reasons on which the employer is not allowed to rely to justify the dismissal. This is very important because the following consequences ensue if the employer seeks to rely on one of the inadmissible reasons.

- (a) The dismissal is automatically unfair, and the reasonableness test is not relevant.
- (b) The qualifying conditions of age and continuous service do not have to be satisfied.
- (c) The monetary awards are higher than for other reasons.

The following are inadmissible reasons for dismissal.

- (a) Complaints by an employee on health and safety matter.
- (b) Pregnancy or childbirth.
- (c) Trade unionism or refusal to join a trade union, or take part in its activities.
- (d) Assertion of a statutory right (rights given under Employment Rights Act 1996).
- (e) Unfair selection for redundancy (e.g. selection in contravention of agreed procedures or if the reason for selection was inadmissible).

If the dismissal was unfair the tribunal may order a re-instatement, re-engagement or compensation.

- (a) Re-instatement means that the employee is given his job back.
- (b) Re-engagement means that the employee is given a different job under a new contract.

- (c) If either of the above is not awarded then the tribunal may order compensation to be paid. This is made up of three awards: the basic award, the compensatory award and the additional award.
- 1 *Basic award*. This depends on the age of the employee, his weekly pay and the length of his continuous service. See notes on redundancy.
 - 2 *Compensatory award*. This is a discretionary award and is based on the employee's losses and expenses (e.g. wages, pension rights, etc.).
 - 3 *Additional award*. This is a special award of a higher amount, and is given:
 - where the employee ignores an order for re-instatement or re-engagement
 - where the dismissal is unfair because of unlawful race or sex discrimination
 - where the reason cited for dismissal is an inadmissible one.

Redundancy

Redundancy occurs in any of the following circumstances.

- An employer ceases or intends to cease business.
- The requirement for work of a particular kind or in a particular place by employees has ceased or diminished or is expected to cease or diminish.

If the new contract of employment is offered the employee should accept unless the contract is unreasonable. Otherwise his refusal to accept will not count as redundancy. Any dispute shall be settled by the tribunal with the onus on the employer. *Taylor v Kent County Council* 1969.

A claim should be made to a tribunal within six months.

The calculation of redundancy payments is based on age, length of service and level of final remuneration.

<i>Age</i>	<i>Amount</i>
41–64	1.5 week's pay
22–40	1 week's pay
18–21	0.5 week's pay

Length of service. The above amounts apply for each complete year of continuous service, up to a maximum of 20 years.

Final remuneration. The maximum at present is £280 per week (currently).

Discrimination in employment

Sex Discrimination Acts 1975 and 1986

Prohibits discrimination on the grounds of sex or marital status at all stages of employment including

- (a) advertising a post
- (b) selection of post
- (c) promotion and training
- (d) dismissal.

The Acts apply equally to discrimination against men and women. Discrimination may be both direct and indirect.

Direct – a woman on the grounds of her sex is treated less favourably than a man. The motive behind the discrimination is irrelevant.

Indirect – where an employer imposes a condition or requirement for a job that a large proportion of women would be unable to comply with: *Price v Civil Service*.

It is not unlawful to discriminate where a person's sex is a genuine qualification for the job.

- (a) Characteristics – model.
- (b) Authenticity – actor.
- (c) Decency or Privacy.

Action: in a tribunal for discrimination or unfair dismissal.

Race Relations Act 1976

Prohibits discrimination whether direct or indirect on the grounds of colour, race, nationality or ethnic or national origins at all stages of employment.

It is not unlawful to discriminate where a person's race is a genuine occupational qualification. This will be for reasons of authenticity in artist's or photographer's models.

Action: in a tribunal for discrimination or unfair dismissal.

Disability Discrimination Act 1995

Prohibits direct discrimination on the grounds of disability at all stages of employment. The act applies where an employer employs 15 or more people.

It is not unlawful to discriminate where the employer believes that the nature of the disability substantially affects the disabled persons' ability to perform the job.

Equal Pay Act 1970

Prohibits pay differentials between male and female employees at the same workplace, i.e. they do – like work – work rated as equivalent and work of equal value: *Hayward v Cammell Laird*. An employer may justify differentials if he can show a "genuine material difference", e.g. experience, productivity or qualifications.

? Questions

4.1 Anne works for E plc under a 4-year fixed term contract of employment. At the end of the 4 years E plc fails to renew the contract because Anne is pregnant.

Which of the following statements is/are *correct*?

- (i) Anne will succeed in an action against E plc for wrongful dismissal.
- (ii) Anne will succeed in an action against E plc for unfair dismissal.

- A (i) only
- B (ii) only
- C Both (i) and (ii)
- D Neither (i) nor (ii)

4.2 Which of the following statements is/are *correct*?

- (i) An employer has an implied duty to behave reasonably and responsibly towards employees.
- (ii) An employer has an implied duty to provide a reference.

- A (i) only
- B (ii) only
- C Both (i) and (ii)
- D Neither (i) nor (ii)

4.3 An employee is entitled to the particulars of his employment:

- A immediately on commencing employment
- B after one month
- C after two months
- D after completing his trial period

4.4 Which one of the following statements is *incorrect*?

- A It is automatically unfair to dismiss an employee for trade union activity
- B It is automatically unfair to dismiss an employee who refuses to obey a reasonable instruction
- C It is automatically unfair to dismiss an employee who becomes pregnant
- D It is automatically unfair to dismiss an employee who complains on health and safety

4.5 Which of the following statements is *incorrect* about wrongful dismissal?

- A It is a breach of contract
- B It can be heard in both civil courts and employment tribunals
- C It is a statutory right
- D Liability is limited to the net pay for the maximum contractual-statutory notice period

 **Answers**

4.1 B

4.2 A

4.3 C

4.4 B

4.5 C

The nature of a company and incorporation

The consequences of incorporation

Types of business organisation. The principle legal forms of business organisation used in Great Britain are:

- (a) Sole trader
- (b) Partnership
- (c) Corporation.

Sole trader

A sole trader is so called because he alone bears the responsibility for running the business and he alone takes the profit.

Partnership

Partnership is defined by s1 of the Partnership Act 1890 as “the relation which subsists between persons carrying on a business in common with a view of profit”.

Partnership law, i.e. the law governing such associations and now largely codified by the Partnership Act 1890, is based on the law of agency, each partner being at one and the same time both the principal and agent of the other(s).

A partnership does not have a separate legal personality. Partnerships are not legal entities distinct and separate from the persons of which they consist: their business and personal affairs are not separate.

A partnership does not require any formality to set up, in the sense there is no legal obligation for a Partnership document. Consequently a partnership can be formed orally by conduct or in writing. Not being a separate legal entity, the liability of the partners is unlimited and is joint and several.

Limited Liability Partnership. The Limited Liability Partnership Act 2000 came into force on 1 April 2001 and allows for the creation of a new form of business entity.

An Incorporation document must be filed at the Companies House stating

- (a) The name of the firm which must end in LLP.
- (b) Location of the registered office, i.e. England, Scotland and Wales.

- (c) Address of the registered office.
- (d) Name of the members (Partners) on Incorporation.

A Limited Liability Partnership is a separate legal entity distinct from its members. The firms' liability is unlimited. The members have limited liability. It is a cross between a Company and a Partnership.

The registered company. A registered company is a form of body corporate and as such has a legal identity distinct from the persons of which it is composed. It acquires its corporate status by registration under the Companies Act 1985.

Corporation

A corporation is an artificial legal person. A legal person is any entity, human or otherwise, which is accepted by the law as having certain defined rights and duties; it is capable of being the subject and object of legal rights and duties.

Incorporation, the process conferring corporate status, results in the corporation being recognised by the law as having a legal personality separate and distinct from its human members. This factor was first fully recognised as regards registered companies in the famous case of *Salomon v Salomon and Co Limited* 1897.

There are two kinds of corporation – the corporation sole and the corporation aggregate.

- 1 A corporation sole is a perpetual office, such as the Crown, having one human member at any one time: the association is successive.
- 2 A corporation aggregate is composed of a number of persons associated together. Registered companies are one kind of corporation aggregate.

Although incorporation under the Companies Act is the most common form of incorporation, it is not the only way in which a company may be formed. Corporate status may be acquired in any of the following ways.

- (a) *By royal charter.* Bodies acquiring corporate status in this way are technically termed “chartered corporation”. Examples include the BBC, the Association of Chartered Certified Accountants and the Institute of Chartered Accountants in England and Wales.
- (b) *By statute.*
 - 1 By a private (or local) Act – this method is used for the incorporation of public utility companies.
 - 2 By a (special) public Act – nationalised industries formed in this way are known as public corporations.
- (c) *By registration in compliance with statutory requirements.*

Companies formed in this way under the Companies Act 1985 or one of the earlier Acts are called registered companies.

The veil of incorporation

A company is a legal person in its own right distinct from its members. This fundamental principle can be illustrated by the following cases.

- (a) *Salomon v Salomon & Company Limited* 1897.
- (b) *Macaura v Northern Assurance* 1925.
- (c) *Lee v Lee's Air Farming* 1960.

However the concept of a veil of incorporation is a legal fiction, and so in certain circumstances the veil has been lifted by Parliament and the courts. In other words, there are sometimes grounds for treating a company and its owners as being the same, usually to prevent the owners from making unfair use of a legal technicality.

S213 Insolvency Act 1986 – fraudulent trading

Where the company is in the course of being wound up, if it appears to the court that the company business has been carried on with the intent to defraud creditors the court may order the persons responsible (i.e. normally the owners) to make contributions to the company's debt.

S214 Insolvency Act 1986 – wrongful trading

Where a company has gone into insolvent liquidation and is in the course of being wound up and it appears to the court that the company's business has been carried on wrongfully, the court can order the directors to make contributions to the company's debt incurred after wrongful trading commenced.

S24 Companies Act 1985

Where the number of members of a public company falls to less than two for six months, the remaining member, if aware of it, becomes jointly and severally liable with the company for debts arising after that time.

S349 CA85 – wrongful use of the company name

If an officer signs a document where the company's name is incorrectly stated, he is personally liable if the company defaults.

In the above situations, the grounds for lifting the veil of incorporation come from statute. There are also situations where case law has the same effect.

- (a) Where the company is a sham (*Gilford Motor Company v Horne* 1933).
- (b) Where it is in the public interest (*Daimler Company Limited v Continental Tyre & Rubber Company Limited* 1916).
- (c) Where the company is a quasi-partnership (*Ebrahimi v Westbourne Galleries* 1973).

Advantages of separate legal personality

- (a) Limited liability – each member of a limited company is liable to contribute only the amount he has agreed to pay on his shares.
- (b) Perpetual succession.
- (c) Transferability of interest.
- (d) Company owns its own assets – the assets and liabilities attach to the company as a separate entity, not to its owners.
- (e) Company may sue and be sued.
- (f) Ease of borrowing (the floating charge).
- (g) No maximum number of members.

Disadvantages of separate legal personality

- (a) Formality – documents required.
- (b) Publicity – accounts, business details.
- (c) Expenses – Registrar's fees, auditors, etc.
- (d) Subject to technical rules – capital maintenance.

Types of registered company

- (a) *Public limited company*. Limited by shares only.
- (b) *Private limited company*. Limited by shares or guarantee.
- 1 By shares – The liability of members to contribute to the debts of the company is limited to any amount unpaid on their shares.
 - 2 By guarantee – The members undertake to pay a stipulated amount in the event of the company’s liquidation.
- (c) *Private unlimited company*. Unlimited companies are liable for their own debts but on a winding up the members are liable to contribute without limit to the assets of the company for settlement of creditors.

Comparison of public and private companies

<i>Public</i>	<i>Private</i>
Must be limited	May be limited
Must be limited by shares (see below)	May be limited by shares or guarantee (see below)
Able to offer its shares and debentures for sale to the public	Cannot offer its shares and debentures for sale to the public
Must have an issued share capital with a nominal value of at least £50,000	No minimum issued share capital
Memorandum must state it is a public company	Memorandum does not state it is private
Name must end with the words “public limited company”	Name must end with the word “limited”, unless it is an unlimited company
Minimum of two directors	Can have one director only, but must then have a different company secretary
Minimum of two members, no upper limit	Minimum of one member, no upper limit

Comparison between companies and partnerships

<i>Company</i>	<i>Partnership</i>
Created by registration with a written constitution	No special formality required
Separate legal person. Company owns its property, can sue and be sued in contract	Not a separate legal person, partners own property, and are liable on contracts
Shares transferable	Limits on the transfer of shares. Partnership may have to be dissolved
No maximum number of members	Normal maximum is 20
Can create fixed and floating charges	Fixed charges only
Management by directors	Management by partners
Company liable for debts	Partners personally liable for debts
Disclosure rules	Private affair
Formal dissolution procedure	May dissolve by agreement

Formation and promotion of companies

Anyone intending to form and register a new company must file the following documents with the Registrar of Companies.

- (a) A signed memorandum of association: this sets out the company's constitution.
- (b) Signed articles of association: this sets out the company's internal regulations.
- (c) Signed statement of first director(s) and secretary(ies): this includes their name, address, nationality, age, occupation and the address of the registered office.
- (d) Statutory declaration of compliance with CA85 by either a solicitor, a director or the secretary.
- (e) The registration fee.

Public companies have to obtain a s117 CA85 trading certificate. For this to be obtained the directors must file a statutory declaration with the Registrar stating:

- (a) that the nominal value of allotted share capital is not less than £50,000
- (b) that at least 25 per cent of the nominal value of each share has been paid up plus all of any premium on each share
- (c) the amount of preliminary expenses (i.e. the costs of forming the company)
- (d) the amount of benefit given to promoters.

If a public limited company commences trading without first obtaining a s117 certificate the consequences are as follows.

- (a) It is a criminal offence by the company and its officers.
- (b) Contracts with third parties are still binding on the company.
- (c) Directors are personally liable if the company fails to perform the contract.
- (d) If a certificate is not obtained for 12 months or more it is a ground for compulsory liquidation.

Re-registration of companies

A private company may re-register as a public company by following certain procedures.

- (a) Type of resolution – special resolution with consent of 75 per cent of members attending the meeting.
- (b) Required to alter – memorandum and articles of association.
- (c) Documents to be filed with the Registrar – application form, new memorandum and articles of association, copy of latest balance sheet dated not more than seven months before the application, auditors report, statement of auditors, declaration of compliance from directors.
- (d) Special requirements – the company must have a minimum issued share capital of £50,000 of which 25 per cent has been paid up plus the whole of any premium.

A public company may re-register as private. The procedures are as follows.

- (a) Resolution required – special resolution.
- (b) Required to alter – memorandum and articles of association.
- (c) Documents to be filed with the Registrar – application form, printed copy of the new memorandum and articles of association.
- (d) Right of objection – court proceedings can be brought by at least 50 members or holders of 5 per cent or more of the issued shares within 28 days of the special resolution.

Promoters

There is no statutory definition of a promoter. However in simple terms a promoter is a person who decides to form a company and takes the steps to set it going.

Duties of a promoter

A promoter stands in a fiduciary relationship with the company he is promoting. This means that he is in a position of trust and must act in good faith in the best interests of the company.

He has a general duty of care and skill.

He has a fiduciary duty not to make a secret profit.

Any profit made must be disclosed to and approved by:

- (a) an independent board of directors and/or
- (b) the members and
- (c) potential members via a prospectus.

Possible liabilities of promoters

Pre-incorporation contracts. A company cannot contract prior to incorporation as it does not exist and therefore has no contractual capacity. The contract is therefore between the promoter and the third party: *Kelner v Baxter* 1866 (S36C CA85 reinforces the existing law).

Solutions for the promoter

- (a) Adoption of contracts by the company after incorporation, leaving contracts as non-binding options in the meantime.
- (b) Assignment of contracts by promoters to the company after incorporation.
- (c) An agreement of novation – after incorporation the company makes a new contract on the same terms as the old with the agreement of the other party.
- (d) Setting up an off-the-shelf (i.e. ready-made) company.

Advantages of a ready-made company

- (a) Cheap and simple.
- (b) Can trade immediately.
- (c) No pre-incorporation contracts.

Disadvantages of a ready-made company

Needs to deal with administrative matters.

Memorandum and articles of association

The memorandum of association

General points

It governs the relationship between the company and outsiders, i.e. it contains the information that outsiders may need to know about the company. If there is a conflict between the memorandum and the articles of association, the memorandum will prevail.

Contents of the memorandum

- (a) Name clause.
- (b) Registered office clause.
- (c) Public clause. This must be included if the company is to be public.
- (d) Objects clause.
- (e) Liability clause.
- (f) Capital clause. This states the authorised share capital.
- (g) Association clause.

The name clause

Statute imposes restrictions on the choice of name for a company. If it is a private company then its name must end with the word Limited or its abbreviation Ltd. The name of a public company must end with the words “public limited company” or the abbreviation plc: s25 CA85.

A company shall not be registered with a name:

- (a) that is the same as the one appearing on the index maintained by the Registrar of Companies
- (b) if the use of the name would be a criminal offence or is offensive (e.g. words associated with charities or formed for illegal purposes)
- (c) which would be likely to give the impression that the company is in any way connected with the government
- (d) which involves trading under a name closely resembling that of an established business.

Change of name

Voluntary – this requires the passing of a special resolution and application to the Registrar.

Mandatory – this may be ordered by the Secretary of State if the name is the same or similar to an existing or registered name, or if it is misleading and therefore liable to cause harm to the public. It may also arise from a successful passing off action.

The Business Names Act 1985

A business can trade under a name other than its own (e.g. A Smith Limited can trade as Sunshine Tours). The Business Names Act 1985 requires any company trading under a business name to disclose the true corporate name (A Smith Limited) on all business documents and at every place of business.

The objects clause

This clause sets out the limits of the company's permissible activities. Acts outside these purposes are known as *ultra vires*, i.e. beyond the powers of the company.

Although a transaction may be *ultra vires* the transaction is valid as regards third parties (s35 CA85), enabling an outsider to enforce it against the company.

An *ultra vires* transaction can be ratified by special resolution.

Members may seek an injunction to prevent an *ultra vires* transaction, unless a company is under a contractual obligation to a third party.

A number of methods have been used to get around the problems of *ultra vires*.

- (a) Lengthy objects clauses.
- (b) Independent object clauses.
- (c) General object clauses.
- (d) Changing objects in advance by special resolution.

It is possible to register a company with a clause that merely states that the company's object is to "carry on business as a general trading company".

Alteration of the objects clause

S4 CA85 allows companies to alter their stated objects by special resolution. However the Act gives rights to minority members (not less than 15 per cent in nominal value of the company's issued share capital of any class of share may within 21 days apply to the courts for an alteration of objects to be cancelled).

The contractual effect of the memorandum and articles

The articles comprise the internal regulations of the company and deal with such matters as the rights of shareholders, procedure at meetings, appointment and removal of directors.

By s14 CA85 the memorandum and articles bind the company and the members to the same extent as if they had been signed and sealed by each member, i.e. they take effect as a contract.

The memorandum and articles can constitute a contract between each individual member and every other member: *Rayfield v Hands* 1960.

The memorandum or articles cannot constitute a contract between a company and a third party: *Eley v Positive Life Assurance* 1876.

Alteration of the articles

By s9 CA85 a company has a general power to alter its articles by passing a special resolution. There is no statutory provision for a dissenting minority to appeal against a change.

Restrictions on altering the articles

The general power as outlined above is subject to numerous overriding restrictions.

- (a) The alteration must not conflict with the memorandum, Companies Acts or other relevant laws.

- (b) The number of shares which a member is bound to subscribe for may not be increased without his consent.
- (c) The alteration must be *bona fide* for the benefit of the company as a whole.

The alteration must not amount to a fraud on the minority.

An alteration which causes a breach of contract with an outsider is valid, but the company will be liable to pay damages: *Southern Foundries v Shirlaw* 1940.

Officers of the company

Appointment of directors

The Companies Act 1985 defines a director as “any person occupying the position of director by whatever name called”. The test is really one of function: if someone takes part in making decisions by attending meetings of the board then he is a director.

A private company must have at least one director, for a public company the minimum is two directors.

First directors are appointed on incorporation, simply by being named on Form 10. Subsequently, directors are appointed in accordance with the articles, by an ordinary resolution of members in general meeting.

Eligibility for office

The following persons are not eligible to be appointed as directors.

- (a) Persons named in the articles.
- (b) Undischarged bankrupts.
- (c) Anyone over 70 (plc only) (unless permitted by the articles).
- (d) A person who does not meet the shareholding requirements (if any).
- (e) Persons disqualified by the Company Directors Disqualification Act 1986:
 - for fraudulent and wrongful trading
 - for persistent default in filing returns
 - for conviction of a serious indictable offence relating to a company
 - for unfitness.

Remuneration

Directors’ remuneration will be set out in the articles and/or separate contracts.

Payment can be challenged if it is not a genuine payment.

Payment of an unreasonable amount may be classed as a gift: *Re Halt Garage Limited* 1964.

Vacation of office

Retirement by rotation

Table A states that at the first AGM all directors shall retire, and at subsequent AGMs one-third of the board shall retire on a first-in-first-out basis. Retiring directors are eligible for re-election.

Resignation

A director may resign either by notice in writing given to the company or by not offering himself for re-election.

Removal (s303 CA85)

Removal of a director requires an ordinary resolution (i.e. a simple majority).

Special notice of the resolution must be given by a member to the company, 28 days before the meeting.

The director may make written representations.

The director has a right to speak at the meeting.

If a director is removed before the expiry of a fixed-term contract, he may sue the company for breach of contract: *Southern Foundries v Shirlaw* 1940.

Compensation for loss of office (s312 CA85)

Any payment made to a director in connection with his loss of office or retirement requires approval by the members to be lawful (e.g. golden handshakes) unless it is in respect of contractual obligations.

Power of directors

The company's powers are exercised by two bodies, the directors and the members. The extent of directors' powers is generally defined by the articles, the objects clause and the directors' service contracts.

If the directors exceed their powers, or exercise them improperly, their acts can nevertheless be ratified by an ordinary resolution provided the transaction was *intra vires* (i.e. within the company's powers): *Bamford v Bamford* 1970.

Board meeting

The powers delegated to directors are exercised collectively by voting at board meetings. In the event of equal voting the chairman has the casting vote.

Provided the directors act within their powers the members cannot overturn decisions of the board. But shareholders dissatisfied with directors' policies may seek to

- (a) remove the directors under s303 CA85
- (b) regulate their future conduct by altering articles.

Managing director

A managing director may be appointed by the other directors if the articles permit. His powers and duties depend on his service contract. Managing directors are not normally subject to retirement by rotation, but the appointment is automatically terminated if he ceases to be a director: *Southern Foundries v Shirlaw*.

Duties of directors

General duties

The primary duty is to act *bona fide* for the benefit of the company as a whole.

The directors must demonstrate the skill and care of a reasonable man looking after his own affairs. The issue of care and skill was considered in: *Re City Equitable Fire Insurance Company 1925*, where the court laid down three principles.

- 1 The required degree of skill is what can reasonably be expected from a person of his knowledge and experience.
- 2 The director does not have to give continuous attention to the affairs of the company but should attend meetings whenever he is reasonably able to do so.
- 3 A director is justified in trusting an official to perform delegated duties honestly provided there are no grounds for suspicion and such delegation is permitted by the articles.

Fiduciary duties

A director is in a position of trust, being in control of the company's assets. This gives rise to certain fiduciary duties.

- (a) To act in good faith.
- (b) To use his powers for a proper purpose.
- (c) Not to fetter his discretion. Directors cannot do deals with each other or with outsiders on the way in which they will vote at board meetings.
- (d) To avoid a conflict of interest: *Cook v Deeks 1916* (depriving the company of assets); *IDC v Cooley 1972* (resigning to take advantage of an opportunity arising as a result of their directorship).

Statutory duties

The following statutory duties have arisen to reduce the risk of a conflict of interest and because of past abuses by directors.

- (a) Duty towards employees (s309 CA85). The directors must have regard to the interests of the company's employees as well as the interests of members.
- (b) Disclosure of interest in contracts (s317 CA85).
- (c) Substantial property transactions (s320 CA85). Any transaction between the company and a director involving a substantial asset (worth more than the lower of £100,000 or 10 per cent of the company's net assets) requires prior approval in a general meeting.

Loans to directors (s330 CA85)

There is a general prohibition under s330 preventing a company from:

- (a) making a loan to a director
- (b) entering into a guarantee on behalf of a director
- (c) providing any security in connection with a loan to a director.

However there are numerous exceptions to s330.

- (a) Loans to directors for any purpose under £5,000 are valid.
- (b) Loans to directors to perform their duties, provided that prior approval is given by members.
- (c) Loans by money lending companies in the ordinary course of business on terms not more favourable than to others (£100,000 maximum).

Relief from liability

In some cases, directors may be relieved from liability for breach of fiduciary duty by resolution of the members in a general meeting.

The company secretary

Every company must have a company secretary. A sole director cannot act as a secretary.

The company secretary is the chief administrative officer of the company and can bind the company to the extent of his actual (express or implied) authority. This usually extends only to contracts of an administrative nature: *Panorama Developments Limited v Fidelis Furnishing Fabrics Limited* 1971.

Therefore the secretary's authority does not extend to:

- (a) making trading contracts
- (b) borrowing money on behalf of the company
- (c) taking or defending legal proceedings in the company's name.

A company secretary has the following duties.

- (a) Ensuring the company's documents are in order (e.g. returns made to the Registrar).
- (b) Taking minutes of meetings.
- (c) Sending notices to members.
- (d) Countersigning documents to which the company seal, if it has one, is affixed.

Share and loan capital

Share capital

A company may issue to its members or the public either share capital or loan capital (debentures) or both.

The terminology of share capital

- (a) Authorised share capital means the total amount of share capital which the company is authorised to issue.
- (b) Issued share capital is the nominal value of shares which have been issued to members.
- (c) Called up share capital is the aggregate amount which a member is required to pay for his shares. Full payment may not always be due at the time that the shares are issued.
- (d) Paid up share capital is the aggregate amount of money paid up on shares.
- (e) Reserve capital is capital which the company has resolved not to call except in the course of winding up (i.e. uncalled capital).

Allotment of shares

Procedures before allotment

The authorised share capital can be increased by ordinary resolution: s121 CA85. A copy of the memorandum plus the ordinary resolution must be sent to the Registrar within 15 days.

Directors' authority to allot shares (s80 CA85)

The director of a company may not generally allot shares unless they are authorised to do so by the articles or by ordinary resolution. The directors' authority may be general or specific to a particular issue.

- (a) It must state the maximum number of shares which may be allotted and the date on which the authority expires.
- (b) It must not generally be for a period of more than five years.
- (c) It may be revoked at any time or varied by the members in a general meeting by ordinary resolution.

Directors' duties

The purpose of issuing shares is to raise capital and an issue for any other reason can be challenged.

Shares issued for the following reasons are therefore for improper purposes.

- (a) To facilitate a takeover: *Howard Smith v Ampol Petroleum* 1974.
- (b) To defeat a takeover: *Hogg v Cramphorn* 1967. However, consent of the members can be obtained at a general meeting: *Bamford v Bamford*.
- (c) To dilute a member's voting power: *Clemens v Clemens* 1976.

Pre-emption rights (s89 CA85)

Where a company, public or private, issues equity shares wholly for cash it must first offer them to existing equity shareholders in proportion to the nominal value of their equity holding. The holders of registered shares must receive notice in writing, and they have 21 days to take up or reject the offer.

Disapplication of pre-emption rights (s95 CA85)

Directors need not first offer shares to existing members in the following circumstances.

- (a) If the shares are subscriber shares, or for an employee share scheme, or bonus shares.
- (b) If the shares are issued for non-cash consideration.
- (c) If pre-emption rights are excluded.

Procedures on allotment

The law regards the issued share capital of a company as a buffer for the creditors. Consequently many of the rules relating to consideration for shares are designed to ensure that shares are not issued for an inadequate capital contribution.

If a company issues shares for a consideration in excess of their nominal value, s130 CA85 requires the premium to be credited to a share premium account. This is a capital account and is not distributable to members. It is treated as part of the paid up capital and may not be depleted. However the share premium account can be used for certain purposes defined in statute.

- (a) To write-off expenses on the incorporation of the company (known as preliminary expenses).
- (b) To write-off the discount on the issue of debentures.
- (c) To write-off underwriting commission.
- (d) To write-off a premium on the redemption of debentures.
- (e) In restricted circumstances, to write-off the premium on the redemption of shares.
- (f) To make a bonus issue.

Allotment at a discount (s100 CA85)

Neither a private company nor a public company can issue shares at a discount.

Payment for shares

Shares may be issued for cash or non-cash consideration (property, know-how, services, etc.).

S101 CA85 – Minimum payment

Shares issued by a plc must be paid up to the extent of one quarter of the nominal value plus the whole of the premium: s101 CA85. (This does not apply to shares allotted under an employee share scheme.) Breach of the above rules has the following consequences (s112 CA85).

- (a) The company and its officers are liable to a fine.
- (b) The allottee must pay the deficiency in cash with interest.

On application the court must grant relief if it is just and equitable to do so: s113 CA85.

Loan capital

Types of debenture

In addition to capital raised by the issue of shares, companies may need to borrow. This may be achieved by issuing debentures.

A debenture is a document by which a company acknowledges its indebtedness for a loan. To ensure that the debenture holders are adequately protected, the debenture loan is usually secured by a charge, which may be either fixed or floating.

Fixed charges

The charge relates to a specific asset which may be realised by debentureholders to repay their loan (e.g. land, buildings and fixed plant and machinery). Also the value of the charge is fixed and the charge takes priority over all other creditors. Any amount of loan not satisfied by selling the charged asset will rank as an unsecured creditor.

Floating charges

These are created only by incorporated associations. A floating charge is a charge secured on the company's assets generally (i.e. on present and future assets of the company) or of a generic type (e.g. stock in trade). The company can deal with the charged property in the ordinary course of business until some event occurs which causes the charge to become crystallised and fixed. Debts secured by floating charges are repaid after fixed charges and after preferential creditors.

Crystallisation

This is the process by which the floating charge ceases to float over the assets and instead becomes attached to the assets. This occurs in the following ways.

- (a) when the company defaults on the debenture agreement
- (b) when winding up commences
- (c) when the company ceases business.

In such circumstances the company can no longer deal with any assets subject to the charge.

Remedies of a debentureholder

An unsecured debentureholder ranks as an ordinary trade creditor.

A secured creditor enjoys two remedies in addition to those of an unsecured creditor.

- 1 selling the charged property to recover the debt
- 2 usually a receiver or administrative receiver is appointed to sell the assets on behalf of debentureholders.

Priority of charges

If there are different charges over the same property, it will be necessary to ascertain their rankings.

- (a) similar charges rank in order of creation
- (b) floating charges rank behind fixed charges even if the fixed charges were created later
- (c) floating charges rank behind preferential creditors.

Registration of charges

Particulars of all charges must be registered with the Registrar of Companies within 21 days. Failure to register renders the charge void against the liquidator and any person who acquires an interest in property subject to the charge and the company and its officers may be fined. The charge therefore remains valid but unsecured. A debentureholder can register the charge if it appears that the company is unlikely to do so and charges can be validly registered outside the 21-day period.

Factors affecting a charge's validity

A preference is any transaction undertaken with a desire to improve a creditor's position on a winding up. The preference must have been given within six months of liquidation (two years if in favour of a connected person).

Floating charges created within 12 months of insolvency (two years if in favour of a connected person) will be rendered invalid if:

- (a) the company was insolvent when the charge was created and
- (b) no consideration was given in exchange for the charge.

Shares and debentures compared

Shares

Shareholders are members

A shareholder has an interest in the company

Usually the shareholder can vote at the company's general meeting

Debentures

Debentureholders are creditors

A debentureholder has a claim against the company

No right to vote at the company's general meeting, but has the right to appoint a receiver

Shares

Receives a dividend if declared

Receives the surplus on a winding up after claims of creditors including debentureholders

Shares are capital and the introduction and withdrawal of capital is strictly controlled by the capital maintenance rules

Cannot be issued at a discount

Shareholders' dividends are appropriations of profit

Debentures

Receives interest. Always entitled to his interest, can sue for arrears if not paid

Receives only the amount of debt owed; takes priority over shareholders in the event of winding up

None of the capital maintenance rules apply

May be issued at a discount

Debentureholders' interest is a charge against profit

Capital maintenance

Serious loss of capital in plcs

The creditors buffer

When members contribute capital to their company, it forms what is known as the "creditors buffer", i.e. a pool of funds on which creditors can draw if the company goes into liquidation.

A particular problem in this context is what the Companies Act 1985 calls a serious loss of capital in a public company. This arises when net assets are 50 per cent or less of a plc's called up share capital: s142 CA85. Consider the following balance sheet.

	£m
Fixed assets	1
Net current assets	<u>2</u>
Net assets	<u><u>3</u></u>
Share capital	6
Profit and loss account	(3)
	<u><u>3</u></u>

On becoming aware of this situation, directors have 28 days to call an EGM to consider what steps are to be taken.

The meeting must be held within 56 days of the directors becoming aware of the position. In the event of default, directors are liable to a fine.

Private companies are not required to do so this because they have fewer members.

Capital reduction

Under s135 CA85 a company can buy back or otherwise reduce its share capital. However three authorities are required for this procedure:

- (a) the power must exist in the Articles
- (b) a special resolution must be passed
- (c) the sanction of the court must be obtained.

If the reduction affects the creditors' buffer then their consent too is required.

S135 suggests three circumstances when capital may be reduced.

- (a) to cancel future calls on unpaid capital
- (b) to write-off share capital that is permanently lost
- (c) to repay capital in excess of the company's requirements.

In (a) and (c) above, creditors may object to the reduction but not under (b) since the reduction will represent the true value of the company.

Redemption or purchase of own shares

S143 CA85 provides that companies are not permitted to purchase their own shares and a company cannot be a shareholder of itself (*Trevor v Whitworth* 1887).

- (a) by the members passing a special resolution and
- (b) by cancelling the shares that are to be redeemed and
- (c) maintaining capital by transferring distributable profits to a non-distributable capital redemption reserve.

Financial assistance for the acquisition of shares

Financial assistance means the company lending money, or guaranteeing a loan made by a third party, to someone to enable that party to buy the company's shares.

It is illegal for any company directly or indirectly to provide financial assistance of any sort for the acquisition of shares in itself or its holding company: s151 CA85.

The following consequences arise if s151 is breached.

- (a) The financial assistance (e.g. the guarantee) is void.
- (b) Officers responsible are guilty of a criminal offence.
- (c) Officers of the company in breach of duty are liable to account for any loss suffered by the company as a result.

General exceptions to s151

The rule in s151 does not apply in any of the following circumstances.

- (a) If financial assistance is not the principle purpose of the transaction for the acquisition of shares (e.g. as part of a reconstruction).
- (b) If the purpose of the assistance is the acquisition of own shares but this is an incidental part of a larger purpose of the company (this legalises many management buyouts).
- (c) Where the lending of money is part of the ordinary business of the company.
- (d) It is to or for the benefit of employees.

Private companies

Private companies may give financial assistance if they follow the correct procedure.

- (a) A special resolution must be passed.
- (b) A statutory declaration must be made by the directors outlining particulars of the assistance to be given.

- (c) The auditors must report on the declaration.
- (d) Net assets must not be reduced by the transaction.

Minority shareholders have to right to object.
A minimum of 10 per cent of any class may object to the resolution.
They must not have voted in favour.
They must apply to the court within 28 days.
The court may do as it thinks fit.

Profits available for distribution

Dividends may not be paid out of capital.

S263 CA85 states that profits available for distribution are the aggregate of accumulated realised profits less accumulated realised losses.

Realised profits and losses

Realised profit means realised in accordance with accepted accounting principles in force at the accounting date, of which the most important are the four accounting concepts in SSAP 2.

Realised losses include sums written off to provisions (e.g. bad debts expense, provision for depreciation of fixed assets, provision for obsolete stock).

Unrealised profits and losses

An unrealised profit arises on the revaluation of fixed assets upwards (the profit would be realised if the assets were sold at the revalued price).

Additional restrictions on plcs

A public company may not make a distribution if the effect would be to reduce its net assets below the aggregate of called up share capital plus distributable reserves.

Consequences of an excessive distribution

A member is liable to repay a distribution he has received if he knew, or had reasonable grounds to believe, that it was being paid in contravention of the Acts. Where the dividends cannot be recovered from members, every director who was knowingly a party to the unlawful distribution must pay the company the amount lost plus interest.

Meetings and resolutions

Meetings

General meetings are meetings of the whole company of which there are two types.

- 1 An Annual General Meeting
- 2 Extraordinary General Meeting.

In addition there are class meetings and board meetings.

Annual General Meeting

Once every calendar year, maximum interval of 15 months between meetings. The first one must be held within 18 months of incorporation.

Agenda:

To consider the accounts, directors and auditors reports.

Declaration of a dividend.

Appointment and remuneration of auditors.

Election of directors.

21 days notice for the meeting unless all voting members consent to a shorter notice.

Called by directors or the Secretary of State.

Extraordinary General Meeting

Held whenever business arises between AGMs which requires member's approval.

The agenda being the reason for calling the meeting.

The notice period is 14 days unless a special or elective resolution is to be considered when it is 21 days. Shorter notice period is possible if 95 per cent of the voting shareholders agree.

The board can call such a meeting, or members holding 10 per cent of the voting share capital, or the court can order one.

Class meetings

Held whenever business arises which affects a particular class of shareholders.

The agenda being the variation of class rights.

The notice period being 14 days unless 95 per cent of the voting shareholders agree to a shorter notice.

The board can call the meeting or the court can order one.

Board meetings

These are called by directors. Reasonable notice should be given.

Decisions are by majority.

Such meetings are called to make collective decision on important decisions concerning the running of the company.

The board may elect a Managing Director who has the authority over the day-to-day running of the company.

Resolutions

Both public and private companies can pass the following resolutions.

Special resolution:

Requires a 75 per cent majority of members who are entitled to and do vote or by proxy.

Must be filed with the Registrar within 15 days.

21 days notice is required unless 95 per cent of members agree to a shorter notice. Used for: alter the name, objects, articles and reduce share capital.

Extraordinary resolution

Requires a 75 per cent majority or proxy.

Filing within 15 days.

Same notice as for meeting, i.e. 21 days AGM, 14 days EGM unless 95 per cent of members agree to a shorter notice.

Used for: voluntary liquidation of an insolvent company by creditors.

Ordinary resolutions

Require a simple majority or proxy.

Same notice as for meeting, i.e. AGM 21 days, EGM 14 days.

No general requirement to file but must for increasing share capital and granting authority for directors to allot shares - Filing within 15 days.

Used for: declaring a dividend, appointment of directors and auditors approval of the accounts.

Some ordinary resolutions require special notice of 28 days from the proposer to the Company and 21 days to members.

Used for: removal of directors and removal of auditors, appointment of director over 70 years in a plc.

Since the CA1989 private companies can pass two further resolutions. These are not available to public companies.

Elective resolutions

Require 21 days notice to members.

The resolution must be agreed by 100 per cent of all members eligible to vote and voting. A copy of the resolution must be filed within 15 days.

They can only be used for the following purposes:

- (a) Dispense with the holding of an AGM.
- (b) Dispense with the annual approval of accounts.
- (c) Dispense with the annual appointment of auditors.
- (d) Reduce from 95 per cent to 90 per cent, the majority required to hold an EGM at short notice.
- (e) To grant directors an indefinite authority to allot shares.

Elective resolutions can be revoked by an ordinary resolution.

Written resolutions

- (a) Do not require a meeting.
- (b) All voting members must agree in writing.
- (c) Passed on the date when the last member signs.
- (d) Can be used for all types of resolutions.
- (e) Except: ordinary resolutions with special notice (28 days) i.e. removal of director or auditor.

Minority members' rights

The principle of majority control is often referred to as the rule in *Foss v Harbottle*: the company acts according to the will of the majority.

In this case Foss brought an action against directors who are alleged to have misapplied company property. His action failed as the company was the victim and if it was unwilling to complain the plaintiff has no rights.

The rule therefore recognises:

- (a) that decisions made or ratified by the majority cannot be disputed by the minority
- (b) that directors owe a duty to the company and not to individual members.

Common law exceptions

There are however numerous exceptions to the rule in *Foss v Harbottle*. An individual shareholder may bring an action in any of the following circumstances.

- (a) If the act is illegal or *ultra vires*.
- (b) If the act has been sanctioned only by a simple majority when a special resolution is required.
- (c) If the personal rights of a member have been infringed: *Pender v Lushington* 1877.
- (d) If the majority control the company and are committing fraud on the minority: *Cook v Deeks* 1916.
- (e) When directors have benefited at the expense of the company through their own negligence: *Daniels v Daniels* 1978.

Statutory exceptions to the rule in Foss v Harbottle

A minority shareholder may wish to withdraw his capital by liquidating the company. This is possible under s122 g Insolvency Act 1986. However the following petitions have been successful.

Failure of the main object (Re German Date Coffee Company 1882).

Where there is management deadlock in the running of the business (Re Yenidje Tobacco Company 1916).

Where the practitioner has been expelled from office as director (Ebrahimi *v* Westbourne Galleries 1973).

A more usual remedy available to dissatisfied minorities is that provided by s459 CA85 (relief from unfairly prejudicial conduct).

The Companies Act 1989 amends s459 to cover conduct which is unfairly prejudicial to the interests of "members generally". This will include prolonged payment of low dividends. Re Sam Weller and Sons Limited 1989.

Examples of other minority rights

- (a) 10 per cent can require the directors to convene an EGM.
- (b) 5 per cent or 100 members can require a resolution to be included on the agenda of an AGM.
- (c) 15 per cent can object to an alteration of the objects.
- (d) Any member of a private company can prevent an elective or written resolution.
- (e) If no AGM is called, any member can inform the Department of Trade and Industry.
- (f) 5 per cent or 50 members can object to conversion of a plc to a private company.
- (g) Any member can prevent conversion from a private limited company to a private unlimited company.

? Questions

- 5.1 The directors of a company are considering altering the company's Articles of Association. The alteration must be *bona fide* for the benefit of
- A members and creditors
 - B all current and future members
 - C the company as a whole
 - D the majority of the membership
- 5.2 Gulliver Ltd has recently dismissed one of its directors. Gulliver Ltd wishes to pay Joe compensation for loss of office. Who must approve this payment?
- A the board of directors
 - B the inland revenue
 - C the creditors
 - D the shareholders in a general meeting
- 5.3 Under the Companies Act 1985 a property transaction exceeding £100,000 in value made between the company and one of its directors and not approved by the company in general meeting is
- A valid
 - B voidable at the instance of the company
 - C voidable at the instance of the director
 - D void
- 5.4 What is the quorum for a general meeting of a registered company?
- A Two persons being members of proxies for members
 - B Three persons being members of proxies for members
 - C Two person being members
 - D Three persons being members
- 5.5 Toffee plc has authorised share capital of 50,000 £1 shares of which 25,000 are issued and quoted on the stock exchange at 80 pence per share. Toffee plc now wishes to issue the remaining 25,000. At which of the following prices could the shares be issued?
- A 25 pence per share
 - B 80 pence per share
 - C 95 pence per share
 - D £1 per share
- 5.6 Which one of the following statements is *incorrect*?
- A A director can be an employee of the company
 - B A director can be an independent contractor of the company
 - C A shareholder can be an employee of the company
 - D A partner can be an employee of the firm
- 5.7 A private company, limited by shares must be registered with
- A at least one member, who may also be the sole director and company secretary
 - B at least one member, who may also be the sole director or the company secretary
 - C at least one member, who cannot also act as a director or company secretary
 - D at least two members, one of whom may act as a director and the other as company secretary

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5.8 Which of the following statements is/are *correct*?

- (i) The partners in an ordinary partnership jointly own the firm's assets
- (ii) The shareholders in a company jointly own the company's assets

- A (i) only
- B (ii) only
- C Both (i) and (ii)
- D Neither (i) nor (ii)

5.9 The Articles of Association of ABC Ltd provide that all disputes between ABC Ltd and its directors must be referred to arbitration. Del is a director of ABC Ltd and is in dispute with the company about late payment of his director's fees.

Which of the following is/are *correct*?

- (i) Del is obliged by the Articles of Association to refer the dispute to arbitration whether or not he is a shareholder
- (ii) Del is obliged by the Articles of Association to refer the dispute to arbitration only if he is a shareholder

- A (i) only
- B (ii) only
- C Both (i) and (ii)
- D Neither (i) nor (ii)

5.10 In relation to companies limited by shares, which one of the following statements regarding issue of shares is *correct*?

- A Shares may not be issued at a discount to the market value
- B A public company cannot issue shares in return for work or services
- C A private company may not allot a share unless it is paid up to at least a quarter on the nominal value
- D Neither public nor private companies may issue shares for a non-cash consideration unless that consideration has been independently valued and reported on

5.11 In relation to a floating charge, which one of the following is *incorrect*?

- A It cannot be created over land
- B It is charged over assets present and future
- C The company may freely dispose of the charged assets in the ordinary course of its business
- D The assets subject to the charge will change from time to time

5.12 s309 Companies Act 1985 imposes a fiduciary duty on directors to have regard to the interests of the company's employees. If directors are in breach of this duty, action may be taken against them by

- (i) the company
- (ii) the employees

Which of the above is/are *correct*?

- A (i) only
- B (ii) only
- C Both (i) and (ii)
- D Neither (i) nor (ii)

- 5.13 The liquidator of ABC Ltd has successfully brought proceedings against one of its directors for wrongful trading under s214 of the Insolvency Act 1986. The court may
- (i) Order the director to make contributions to the company's assets
 - (ii) Impose a fine on the director
- A (i) only
 - B (ii) only
 - C Both (i) and (ii)
 - D Neither (i) nor (ii)
- 5.14 s459 of the Companies Act 1985 allows a petition to be made to the court for relief from unfair prejudice. Which one of the following statements as to who may petition is *correct*?
- A Any member
 - B Any director
 - C Any employee
 - D The company
- 5.15 A director who is in breach of his fiduciary duty to the company which does not involve a fraud on the minority may be exempted from liability by:
- A A resolution passed by a general meeting
 - B A resolution passed by the board of directors
 - C A provision in the Memorandum of Association
 - D A provision in the Articles of Association
- 5.16 To what extent is a member of a company limited by guarantee personally liable for the company's debts.
- A He is personally liable for all the company's debts at any time
 - B He is personally liable for all the company's debts on a winding up
 - C His personal liability is limited to the amount stated in the memorandum upon a winding up
 - D His personal liability is limited to the amount stated in the memorandum at any time
- 5.17 Under the Companies Act 1985 what is the consequence of the number of members of a public company falling below two?
- A The company must cease trading within six months
 - B The remaining member becomes jointly and severally liable with the company for the company's debts after six months
 - C The company must notify the Registrar, but otherwise can continue trading as normal
 - D The remaining member automatically takes over personal liability for the company's debts incurred while he is the sole member
- 5.18 Which of the following is a requirement for any public company registered in England?
- A No restriction may be placed on the transfer of its shares
 - B Its shares must be publicly for sale
 - C It must have a minimum paid up capital of £50,000
 - D The final words of the company's name must be 'Public Limited Company' or PLC

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- 5.19 What type of resolution is required at a general meeting to remove a director from office?
- A An ordinary resolution
 - B An ordinary resolution with special notice
 - C A special resolution
 - D A special resolution with special notice
- 5.20 Which of the following share issues would be deemed to be for the proper purpose?
- A An issue to a potential bidder to facilitate his takeover bid for the company
 - B An issue to raise finance for a new building project
 - C An issue to a nominee in order to prevent a takeover bid
 - D An issue to a director to increase his voting power and so to allow him to ratify his actions
- 5.21 A floating charge is a charge:
- A On a class of current assets which can be identified
 - B On the undertaking of a company
 - C On a class of assets which may change in the ordinary course of business
 - D On a class of assets present or future which may change in the ordinary course of business
- 5.22 What is the position of a minority shareholder who wishes to bring an action in the company's name against the directors who are the majority shareholders and have purchased company assets at considerable undervaluation?
- A No action can be brought by the minority
 - B An action may only be brought if there is a deliberate fraud on the part of the directors
 - C An action will be allowed only if the Articles of Association permit
 - D An action will be permitted since the directors have used their position to make a personal gain at the expense of the company
- 5.23 Larry, an entertainer, is a director and a majority shareholder of Lamb Ltd which has no significant assets. He has no contract of employment with Lamb Ltd. John contracts with Lamb Ltd for Larry to appear at a concert. Larry fails to appear and John loses a large sum of money. John has a legal remedy against
- A Lamb Ltd
 - B Larry, as a director of Lamb Ltd
 - C Larry, as the owner of Lamb Ltd
 - D Larry, on the basis that the company is a sham
- 5.24 Immediately prior to the incorporation of Products Ltd, Roberts, one of its promoters, bought property in his own name from Suppliers Ltd. He later sold the property to Products Ltd at a large profit without disclosure.
- To whom is Roberts liable in relation to this secret profit?
- A Suppliers Ltd
 - B Products Ltd
 - C The promoters of Products Ltd
 - D The shareholders of Products Ltd

- 5.25 Which of the following names could not without further consent be a permissible name under the Companies Act for a company, the main object of which is to contract refuse collection services for Westchester City Council?
- A Westchester City Refuse Services Ltd
 - B Council (Refuse Collection) Services Ltd
 - C Refuse Collection (Westchester) Ltd
 - D City Waste Disposal Ltd
- 5.26 The Memorandum of Association of a company must be signed by
- A the subscribers and all the directors
 - B the subscribers and at least one of the directors
 - C the subscribers and the company secretary
 - D the subscribers only
- 5.27 For how long must the accounting records of a company be retained after the year end?
- A Three years in the case of all companies
 - B Three years in the case of a public company and six years in the case of a private company
 - C Six years in the case of a public company and three years in the case of a private company
 - D Six years in the case of all companies
- 5.28 Which of the following is not a legitimate use of the share premium account?
- A Writing-off a discount on the issue of debentures
 - B Writing-off underwriting commission
 - C Writing-off preliminary expenses
 - D Writing-off a discount on the issue of shares
- 5.29 Orpheus has for many years, with the knowledge of the other directors, acted as managing director of Underworld Ltd. Although the Articles of Underworld Ltd empower the directors to appoint one of their member as managing director, they have never actually done so formally. Orpheus, in his capacity as managing director, entered a number of contracts with Hades plc. After a serious internal dispute between Orpheus and the other directors, Underworld is now refusing to honour the contract with Hades plc. What is the legal position?
- A Underworld Ltd will not be bound by the contracts made by Orpheus as he has not been properly appointed as managing director of the company and therefore does not as such have contractual capacity
 - B Neither Orpheus personally nor Underworld Ltd will be bound by the contracts made by Orpheus as his lack of contractual capacity as managing director has effectively rendered the contracts void
 - C Underworld Ltd will be bound by the contracts made by Orpheus as he had apparent authority to make them, having been held out by the board as having the appropriate authority
 - D Underworld Ltd will be bound by the contracts made by Orpheus as he had actual authority to make them by virtue of his position as de facto managing director

- 5.30 Ceres Ltd last held an AGM on 31 October 2004. By what date must the company hold its next AGM?
- A 31 October 2005
 - B 31 December 2005
 - C 31 January 2006
 - D 30 April 2006
- 5.31 For which of the following is an ordinary resolution of the shareholders sufficient authority.
- A To amend a private company's articles
 - B To alter a public company's objects
 - C To change a private company's name
 - D To give directors authority to issue new shares
- 5.32 The clause in the memorandum of association of a company limited by shares sets out the amount of:
- A total authorised capital
 - B authorised capital divided into shares of fixed amount
 - C authorised capital divided into classes of shares of a fixed amount
 - D the issued capital in shares of fixed amount
- 5.33 Who will be liable for wrongful trading on an insolvent winding up?
- A All persons who took part in it
 - B All persons who knew the company was insolvent
 - C Directors of the company
 - D Any officer of the company
- 5.34 What authority is required for a private company to provide financial assistance for the principle purpose of the purchase of its own shares?
- A special resolution
 - B special resolution and statutory declaration
 - C special resolution, statutory declaration and the auditors report
 - D special resolution, statutory declaration, auditors report and court approval
- 5.35 Under s89 CA85 there is a statutory right of pre-emption on allotment of shares by a company. Does this apply when;
- A a shareholder wishes to sell his shares
 - B the company allots shares for cash
 - C the company allots equity shares for cash
 - D the company allots equity shares
- 5.36 What is the liability of a member of an unlimited company?
- A to pay a call without limit on a winding up
 - B for the debts while he is a member
 - C for the debts on a winding up
 - D to pay a call to pay the debts at any time

- 5.37 What is the status of a loan of £20,000 made by Snippet plc, a manufacturing company, to a director to enable him to renovate her kitchen?
- A Prohibited by the Companies Act 1985
 - B Prohibited unless made in the ordinary course of business
 - C Prohibited, unless made for improvements to her residence and available to employers
 - D valid, provided sanctioned by ordinary resolution as not exceeding £20,000
- 5.38 How may a company (i) ratify an *ultra vires* contract entered into by directors and (ii) agree to relieve those directors from liability?
- Is it
- A (i) and (ii) by separate resolution
 - B (i) and (ii) by one special resolution
 - C (i) by special resolution and (ii) by ordinary resolution
 - D (i) cannot be rectified and (ii) by special resolution
- 5.39 In what circumstances may a company director incur personal liability for the debts of a company?
- Is it on
- A wrongful trading
 - B fraudulent trading
 - C winding up
 - D acting as a director contrary to a disqualification order
- 5.40 Popeye is the promoter of Spinach Ltd. He and his wife Olive are the first directors of the company. Popeye sold a plot of land he owned to the company making a profit of £20,000. What is the legal position regarding the profit?
- A Popeye may keep the profit in any event
 - B Popeye may keep the profit as long as it is disclosed to the board of directors
 - C Popeye may keep the profit as long as it is disclosed to the first shareholders of the company
 - D Popeye may not keep the profit under any circumstances
- 5.41 Dave and Sue have applied to have Bideford Ltd registered as a private company limited by shares but failed to submit articles of association to the Registrar. What is the effect of the omission to the Registrar?
- A The Registrar will return the application to Dave and Sue
 - B A provisional registration will be made but Bideford will be unable to commence trading until the submission of its articles
 - C Provisional registration will be permitted pending determination of the articles at the first meeting of the directors
 - D Table A articles will automatically apply to the company
- 5.42 What proportion of a company's shareholders may object to a special resolution passed to change the company's name under the terms of the Companies Act 1985?
- A 15 per cent of any class shareholder
 - B 15 per cent of the shareholders
 - C 10 per cent of any class of shareholder
 - D There is no statutory right of objection

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- 5.43 Minority shareholders who do not vote in favour of an alteration to the company's object clause and who wish to challenge the alteration must petition the court within how many days after the passing of the resolution?
- A 7
 - B 14
 - C 21
 - D 28
- 5.44 Which of the following share issues would be deemed to be for the proper purpose?
- A An issue to a potential bidder to facilitate his takeover bid for the company
 - B An issue to raise finance for a new building project
 - C An issue to a nominee in order to prevent a takeover bid
 - D An issue to a director to increase his voting power and so allow him to ratify his actions
- 5.45 Under s35 Companies Act 1985, what is the position of a person innocently entering into an *ultra vires* contract with a company and decided on by the directors of that company?
- A The contract is void and no action may be taken on it
 - B The validity of the contract cannot be challenged on the ground of lack of capacity
 - C The third party can only sue the directors in person for exceeding their powers
 - D The contract is unenforceable but the third party can retain any property received under it

✓ Answers

5.1 C

5.2 D

5.3 B

5.4 A

5.5 D

5.6 D

5.7 B

5.8 A

5.9 D

5.10 B

5.11 A

5.12 A

5.13 A

5.14 A

5.15 A

5.16 C

5.17 B

5.18 D

5.19 B

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5.20 **B**

5.21 **D**

5.22 **D**

5.23 **A**

5.24 **B**

5.25 **B**

5.26 **D**

5.27 **C**

5.28 **D**

5.29 **C**

5.30 **B**

5.31 **D**

5.32 **A**

5.33 **C**

5.34 **C**

5.35 **C**

5.36 **A**

5.37 **A**

5.38 **A**

5.39 **D**

5.40 **C**

5.41 **D**

5.42 **D**

5.43 **C**

5.44 **B**

5.45 **B**

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Certificate Level

Business Law

Mock Assessment 1

Instructions: attempt all 40 questions

Time allowed 1 hour

Do not turn the page until you are ready to attempt the examination under timed conditions.

Questions

? Question 1

Which *one* of the following is *correct*?

- (A) The House of Lords has a discretion in applying English Law or European Law.
- (B) The House of Lords must apply European Law where it contradicts English Law.
- (C) The House of Lords can apply English Law even if it contradicts European Law.
- (D) The House of Lords must obtain approval to apply European Law where it contradicts English Law.

? Question 2

Which *one* of the following courts has *no* criminal jurisdiction?

- (A) Divisional court of the Queens Bench Division.
- (B) County Court.
- (C) Magistrates Court.
- (D) Crown Court.

? Question 3

With judicial precedent, subject to the hierarchy of the courts, previous court decisions should be followed. However, it can be possible to avoid following precedent.

Which *one* of the following is *incorrect* in relation to avoidance of precedent?

- (A) A higher court can overrule a lower court decision.
- (B) Any court can distinguish the facts from those of an earlier decision.
- (C) Any court can reverse the decision of a previous court.
- (D) Any court need not apply an obiter dicta statement of an earlier court.

? Question 4

In relation to establishing a claim of negligence, which *one* of the following is *incorrect*?

- (A) There must be sufficient proximity between the wrongdoer and the injured party.
- (B) The standard of care required is that expected by the reasonable person.
- (C) The same level of care is owed both adults and children.
- (D) The level of care to be shown varies with the level of seriousness of the likely consequences of breach of duty.

? Question 5

Which *one* of the following is *correct*?

- (A) A professional adviser can be liable to both the client who employs them and any other parties who they know will rely on information provided.

- (B) A professional adviser can be liable to anyone who relies on information they provide.
- (C) A professional adviser will be liable in negligence but not contract for any negligent advice provided.
- (D) A professional adviser cannot be liable where the only form of damage resulting from negligent advice given is financial loss.

? Question 6

The following advertisement appeared in a farming magazine.
 'Plough for sale. Little used, very good condition. £1000'.
 How would this statement be defined at law?

- (A) Advertising puff.
- (B) Offer to sell.
- (C) Invitation to treat.
- (D) Invitation to buy.

? Question 7

An offer was made by A to sell goods on the 1st April for £2,000. B the offeree telephoned A on the 5th April offering to pay £1,800 for the goods. On the 8th April, A offered to sell the goods to C for £1,900, and C accepted this offer on the same day. On the 7th April, B sent a letter to A which was received on the 10th April agreeing to pay the £2,000 asking price for the goods.

- (A) There is a contract between A and B created on the 7th April.
- (B) There is a contract between A and B created on the 10th April.
- (C) There is a contract between A and C.
- (D) There is no contract created.

? Question 8

A coat was displayed in a shop window with a price tag attached which read £10. The price tag should have read £100. X who saw this went into the shop and demanded the coat for £10.

Which *one* of the following is *correct*?

- (A) As the window display is an offer X can demand the coat at £10.
- (B) The window display is merely an invitation to treat and the shopkeeper does not have to sell the coat to X.
- (C) The shopkeeper can refuse to sell the coat for £10, but cannot refuse to sell the coat to X for £100 if X was prepared to pay this sum.
- (D) The shopkeeper would be bound to sell the coat to any customer prepared to pay this £100.

? Question 9

Which *one* of the following is *incorrect*?

- (A) A contract term can be implied by a court on the ground of business efficacy.
- (B) A contract term can be implied by statute.

- (C) A contract term can be implied by a court on the basis of fairness between the parties.
- (D) A contract term can be implied by a court on the basis of trade custom.

? Question 10

Which *one* of the following statements is *incorrect*?

- (A) Statute provides an implied term in sale of goods contracts that the goods are of satisfactory quality.
- (B) Statute provides an implied term in sale of goods contracts that the goods supplied must correspond with description.
- (C) Statute provides that failure to supply goods of satisfactory quality in a sale of goods contract constitutes breach of condition.
- (D) Statute provides that failure to provide goods in a sale of goods contract that correspond with description amounts to a breach of warranty.

? Question 11

Which *one* of the following statements is *correct*?

- (A) In contract breach of a condition will result in the contract being terminated.
- (B) In contract a breach of a condition is a breach of a term of fundamental importance to the contract.
- (C) In contract a breach of warranty entitles the innocent party to terminate the contract.
- (D) In contract a breach of warranty can terminate a contract, but only on the basis of equity.

? Question 12

Which *one* of the following is *incorrect*?

- (A) Exclusion clauses attempting to exclude liability for death or injury are void.
- (B) Statutory implied conditions giving consumers protection in sale of goods contracts can be excluded so long as the exclusion clause is reasonable.
- (C) Where the wording of an exclusion clause is ambiguous it will be interpreted against the party seeking to rely on it.
- (D) An unfair term does not bind a consumer but the contract may continue.

? Question 13

A contract will be discharged as a result of a frustrating event occurring.

Which one of the following will not bring about discharge of a contract?

- (A) Performance becomes radically different from that anticipated.
- (B) Performance becomes more expensive and difficult than anticipated.
- (C) Physical impossibility of performance due to accidental destruction of subject matter.
- (D) If the contract is dependent on a future event which does not occur.

? Question 14

X has contracted with Y to paint a portrait of Y's daughter. Y has for a considerable time wanted X to paint the portrait and is very disappointed when X having started the work states that he is not prepared to complete the painting.

Which of the following remedies is appropriate in these circumstances?

- (A) Damages
- (B) Rescission
- (C) Specific performance
- (D) Injunction.

? Question 15

Which of the following statements is *incorrect* in relation to the determining of damages payable on breach of contract?

- (A) The purpose of providing damages is to compensate the injured party.
- (B) Quantifying damages is determining the actual amount of the award to be made to the injured party.
- (C) The remoteness of damage issue is determined by considering the amount of damages the injured party reasonably expects on the basis of the contract breach and damages suffered.
- (D) An innocent party has a duty to mitigate their loss.

? Question 16

An employer must provide a written statement of particulars to an employee within what period from the commencement of the employment?

- (A) Immediately
- (B) Within 1 week
- (C) Within 1 month
- (D) Within 6 weeks.

? Question 17

In order to determine whether or not a party is an employee or an independent contractor a number of tests have been devised.

Which *one* of the following is *not* a recognised test?

- (A) Organisation test
- (B) Control test
- (C) Multiple test
- (D) Supply and demand test.

? Question 18

Which *one* of the following statements is *incorrect*?

- (A) An employer is normally liable for wrongs committed by employees.
- (B) An independent contractor has no statutory protection in respect of sick pay.

- (C) An independent contractor has no preferential rights over other creditors on the insolvency of the employer.
- (D) Employees and independent contractors are prohibited from delegating work to others.

? Question 19

Which *one* of the following is *incorrect*?

- (A) A limited liability partnership has legal personality.
- (B) A minimum two parties are required to form a limited liability partnership.
- (C) Partners in a limited liability partnership cannot be corporate bodies.
- (D) Individual members of a limited liability partnership will have no contractual liability to creditors of the partnership.

? Question 20

In relation to a private limited company, which *one* of the following is *correct*?

- (A) Annual General Meetings must be held.
- (B) Articles of Association must be filed with a Registrar when seeking registration of the company.
- (C) The company will have perpetual succession.
- (D) Directors of the company would never be liable to company creditors.

? Question 21

Which *one* of the following statements is *incorrect* in relation to a public limited company?

- (A) A company must have a minimum issued share capital of £50,000.
- (B) The company cannot issue only redeemable shares.
- (C) The company must have a certificate of incorporation and a trading certificate before it can validly commence business.
- (D) The company must have at least two members.

? Question 22

Which *one* of the following is *incorrect*?

- (A) Members of a company can ratify any *ultra vires* act of its directors.
- (B) Any member can seek an order preventing a company from carrying out an act not specifically permitted in its objects clause.
- (C) Where an objects clause provides that a company can carry on business as a 'general commercial company', the company can validly carry out any lawful transaction.
- (D) Where a director acts *ultra vires* on behalf of a company the transaction will be void unless it is ratified by the members.

? Question 23

Which *one* of the following is *correct* in relation to an alteration of articles of association where the appropriate procedure is followed?

- (A) Class rights can be altered.
- (B) Shareholder liability can be increased.
- (C) Members must pass an extraordinary resolution.
- (D) The alteration must be *bona fide* and in the best interests of every member.

? Question 24

Which *one* of the following can only be achieved with court approval, in addition to a resolution of the members being passed?

- (A) Change of company name.
- (B) Increase of share capital.
- (C) Reduction of share capital.
- (D) Change of the situation of the company registered office.

? Question 25

Which *one* of the following is *correct*?

- (A) A private company can issue only redeemable shares.
- (B) A private and a public company can issue only redeemable shares.
- (C) A public company can issue redeemable preference shares.
- (D) A private company cannot issue redeemable preference shares.

? Question 26

One of the procedural requirements for the reduction of capital by a private limited company is the passing of a resolution.

Which *one* of the following resolutions must be passed?

- (A) Special
- (B) Elective
- (C) Written
- (D) Ordinary.

? Question 27

Which *one* of the following is *incorrect*?

- (A) A private company can accept any form of consideration in return for shares so long as it is real.
- (B) A private company can accept consideration in a contract of allotment of shares of a lower value than that of the shares.
- (C) A public company can only accept money as consideration on an allotment of shares.
- (D) A private company and public company can increase its authorised share capital figure by passing a resolution.

? Question 28

Where company articles do not identify a specific type of resolution appropriate, a company can increase its share capital if the members pass which *one* of the following types of resolution?

- (A) Ordinary
- (B) Special
- (C) Extraordinary
- (D) Special with extra notice.

? Question 29

In relation to a company purchasing its own shares, which *one* of the following is *correct*?

- (A) Capital can be used by both private and public companies.
- (B) Capital cannot be used by either private or public companies.
- (C) Public companies only can use capital to satisfy some of the debt.
- (D) Private companies only can use capital to satisfy some of the debt.

? Question 30

In relation to a company providing financial assistance for the acquisition of its own shares, which *one* of the following is *incorrect*?

- (A) A private company may provide financial assistance for the purchase of its own shares so long as it follows the correct procedure.
- (B) A public or private company can give assistance where the assistance is a dominant part of some larger purpose.
- (C) A bank is permitted to provide financial assistance for an acquisition of shares in the bank itself.
- (D) A company can provide assistance to employees by providing loans which are used to purchase shares in the company.

? Question 31

Which *one* of the following statements is *incorrect*?

- (A) A private company can have only one member who is also the only director.
- (B) A sole director in a private company can also be the company secretary.
- (C) A sole member is distinct from the company at law.
- (D) A director who is also sole shareholder in the company can waive their own breach of duty.

? Question 32

A minority of members can give written, signed notice to the directors requiring them to hold an Extraordinary General Meeting.

Which *one* of the following is the *correct* minimum shareholding this minority must have?

- (A) 5 per cent
- (B) 10 per cent
- (C) 15 per cent
- (D) 25 per cent.

? Question 33

Which *one* of the following is *correct* in relation to the use of an ordinary resolution with special notice?

- (A) It will only be used for the removal of a director.
- (B) It will only be used for the removal of directors or auditors.
- (C) It will only be used for the removal of directors and appointment of directors aged over 70 years.
- (D) It will be used for the removal of directors and auditors, and also the appointment of directors aged over 70 years.

? Question 34

In relation to directors which *one* of the following statements is incorrect?

- (A) A director is an agent of the company.
- (B) A director is an officer of the company.
- (C) A company has a duty to have executive directors.
- (D) A shadow director is the main type of *de facto* director.

? Question 35

Directors do not owe a duty to which *one* of the following?

- (A) Members individually
- (B) Members as a body
- (C) Creditors
- (D) Employees.

? Question 36

Where a director is guilty of wrongful trading which *one* of the following is a possible consequence for the individual?

- (A) Being required to contribute to the assets of the company in liquidation.
- (B) A possible fine.
- (C) Imprisonment.
- (D) Being subject to an equitable remedy.

? Question 37

Which *one* of the following is *incorrect* where a director is in breach of fiduciary duty?

- (A) The members can pass a resolution ratifying what has been done.
- (B) If the director in breach is also a member, he can vote in support of the ratification.
- (C) Articles can exempt directors from liability for breach of duty.
- (D) A director in breach can be liable to account for any secret profit obtained.

? Question 38

Alan, Barbara and Clive are the only members of Beeceedee Ltd. with equal shareholdings. They are also the only directors of the company. Relations between the three parties have in the past been good. However, now, Alan and Barbara always vote against Clive at board meetings and are not prepared to listen to Clive's views. Further, on numerous occasions Alan and Barbara have refused to attend meetings. The quorum for board meetings and members meetings is two. Clive is unhappy generally with the way in which the company is now being run and wishes to petition for a winding up order.

Which *one* of the following is the appropriate action to obtain a winding up order?

- (A) A derivative action.
- (B) An action on the basis of unfairly prejudicial conduct.
- (C) An action on the just and equitable ground.
- (D) A representative action.

? Question 39

Sec. 461 Companies Act 1985 identifies a number of remedies which can be introduced by a court where an action for unfairly prejudicial conduct is brought.

Which *one* of the following is *not* a remedy identified in this section?

- (A) An order regulating company affairs in the future.
- (B) Authorising criminal proceedings to be brought in the name of and on behalf of the company.
- (C) Authorising civil proceedings to be brought in the name of and on behalf of the company.
- (D) Requiring the company to buy the petitioner's shares at fair value.

? Question 40

Which *one* of the following is *incorrect* in relation to the company secretary?

- (A) They can never contract on behalf of the company.
- (B) Qualification requirements attach to a company secretary of a public company but not a private company.
- (C) Details of the company secretary are entered in the same register as that used to register director details.
- (D) Some statutory provisions can render the company secretary criminally liable.

 **Solutions**

Solution 1 (B)	Solution 15 (C)	Solution 29 (D)
Solution 2 (B)	Solution 16 (C)	Solution 30 (B)
Solution 3 (C)	Solution 17 (D)	Solution 31 (B)
Solution 4 (C)	Solution 18 (D)	Solution 32 (B)
Solution 5 (A)	Solution 19 (C)	Solution 33 (D)
Solution 6 (C)	Solution 20 (C)	Solution 34 (C)
Solution 7 (C)	Solution 21 (A)	Solution 35 (A)
Solution 8 (B)	Solution 22 (D)	Solution 36 (A)
Solution 9 (C)	Solution 23 (A)	Solution 37 (C)
Solution 10 (D)	Solution 24 (C)	Solution 38 (C)
Solution 11 (B)	Solution 25 (C)	Solution 39 (B)
Solution 12 (B)	Solution 26 (A)	Solution 40 (A)
Solution 13 (B)	Solution 27 (C)	
Solution 14 (C)	Solution 28 (A)	

Certificate Level

Business Law

Mock Assessment 2

Instructions: attempt all 40 questions

Time allowed 1 hour

Do not turn the page until you are ready to attempt the examination under timed conditions.

Questions

? Question 1

Which of the following statements apply to the criminal but not the civil law?

- (A) The main aim of the law is to compensate the claimant.
- (B) The case must be proved beyond reasonable doubt.
- (C) An action may be brought in the County Court or High Court.
- (D) A claimant may terminate the proceedings at any stage.

? Question 2

Which of the following is *incorrect* in relation to judicial precedent?

- (i) The House of Lords may ignore its own previous decisions.
 - (ii) The Court of Appeal is bound by the decisions of the Judicial Committee of the Privy Council.
 - (iii) The High Court is bound by the decisions of superior courts in other common law jurisdictions.
- (A) (i) only
 - (B) (ii) only
 - (C) (ii) and (iii) only
 - (D) (iii) only

? Question 3

Which of the following types of European law is binding on Member States as to the result to be achieved?

- (A) A Regulation
- (B) A Decision of the European Court
- (C) A Directive
- (D) A Recommendation

? Question 4

In relation to the tort of negligence, which of the following statements is correct?

- (i) A doctor owes a duty of care to a patient.
 - (ii) An accountant owes a duty of care to a client.
 - (iii) A police officer does not owe a duty of care to other road users if he is speeding to a road accident
- (A) (i) only
 - (B) (i) and (ii) only
 - (C) (ii) and (iii) only
 - (D) (i), (ii) and (iii)

? Question 5

Which of the following may render a contract void at common law?

- (A) Fraudulent misrepresentation
- (B) A fundamental mistake of fact
- (C) Undue influence
- (D) Duress

? Question 6

Goods are priced in a shop window £200. Which of the following is *incorrect*?

- (A) The shopkeeper must sell the goods to a person who offers to buy them for £200.
- (B) Even if the shopkeeper gives a customer 7 days to decide whether to buy the goods he can still sell the goods to someone else before the 7 days have elapsed.
- (C) The goods for sale in the window constitute an invitation to treat.
- (D) When the goods are sold, terms will be implied into the contract by the Sale of Goods Act 1979.

? Question 7

Which of the following amounts to executory consideration on the part of the customer?

- (A) A customer hands over cash to purchase some goods.
- (B) A customer agrees to purchase goods 'cash on delivery'.
- (C) A customer is given 10 per cent discount for purchasing goods in cash.
- (D) A customer who pays cash for goods is given a discount because he buys goods from the shop every week.

? Question 8

In which of the following situations will the law presume that the businessman intended to create legal relations?

- (A) He agrees to pay his son a weekly allowance.
- (B) He signs a commercial agreement which is 'binding in honour only'.
- (C) He orally agrees to employ a secretary.
- (D) He signs a 'letter of comfort' agreeing that his company will pay the outstanding debts of its subsidiary company.

? Question 9

Every breach of contract entitles the innocent party to

- (A) refuse further performance of the contract.
- (B) the award of a decree of specific performance.

- (C) claim damages.
- (D) The award of an injunction.

? Question 10

A court is unlikely to grant a decree of specific performance in respect of a contract for the sale of

- (A) shares
- (B) land
- (C) antique furniture
- (D) carpets

? Question 11

Paul agreed to buy a number of cases of fruit from Seller Ltd at a price of £1,000. Paul could have bought them elsewhere for £800 at that time, but decided to buy from Seller Ltd as the company had agreed to make an immediate delivery and Paul wanted to sell the fruit to Jack for £1,200. Seller Ltd knew nothing of the resale to Jack. If Seller Ltd failed to deliver the fruit and Paul had to pay £1,100 for the fruit, which of the following amounts would form the basis of an award in damages?

- (A) Nominal damages only
- (B) £100
- (C) £200
- (D) £1,000

? Question 12

On 1 October X Ltd wrote to Y Ltd offering to sell some plant and machinery for £5,000 and giving Y Ltd 7 days to decide. On 2 October X Ltd wrote withdrawing its offer but this letter was delayed in the post and did not reach Y Ltd until 5 October. On 3 October Y Ltd received the first letter and posted a letter of acceptance on the same day. This letter reached X Ltd on 6 October.

Which of the following statements is correct?

- (A) The offer came to an end on 2 October.
- (B) A contract was concluded on 3 October.
- (C) The offer came to an end on 5 October.
- (D) A contract was concluded on 6 October.

? Question 13

Which of the following is correct?

- (i) The Sale of Goods Act 1979 implies terms into consumer sales.
- (ii) The Sale of Goods Act 1979 implies terms into non-consumer sales.
- (iii) Terms implied by the Sale of Goods Act 1979 cannot be excluded.

- (A) (i) only
- (B) (i) and (ii) only
- (C) (i) and (iii) only
- (D) (i), (ii) and (iii)

? Question 14

Which of the following must be established to obtain relief under the Misrepresentation Act 1967?

- (i) The innocent party was induced to enter into a contract with the person who made the untrue statement.
 - (ii) The other party deliberately made an untrue statement.
 - (iii) The innocent party suffered loss as a result of the statement.
- (A) (i) only
 - (B) (i) and (ii) only
 - (C) (i) and (iii) only
 - (D) (ii) and (iii) only

? Question 15

Which of the following correctly summarises the *contra proferentem* rule?

- (A) Contractual losses lie where they fall.
- (B) A person cannot be bound by an exclusion clause written in small print.
- (C) An exclusion clause written on the back of an invoice cannot be valid.
- (D) An ambiguous clause will be read against the person seeking to rely on it.

? Question 16

Which of the following promises would be unenforceable in the law of contract because of a lack of consideration?

- (A) A promise to pay £1,000 for a car worth £1,200.
- (B) A promise to pay £50 to a person who has returned a lost credit card.
- (C) A promise to pay a debt of £2,000 by paying £1,800 one week before the debt becomes due and payable.
- (D) A promise to pay a police authority for providing extra police officers at a pop concert.

? Question 17

In which of the following situations would an employer be vicariously liable?

- (A) He failed to provide a safe system of work in accordance with health and safety legislation.
- (B) The employer injured an employee when carrying out his business operations.
- (C) An employee injured a third party when acting within the ordinary course of his employment.
- (D) The employer injured a third party when carrying out his business operations.

? Question 18

Harry is employed as a Senior Scientist with Wye plc, a large chemical company. Harry's contract of employment contains a clause which provides that if he should leave Wye plc he will not work '... in the chemical or engineering industry in Europe for a period of ten years'. If the clause is challenged in court and it is decided that the clause is too wide, which of the following actions is open to the court?

- (i) Reduce the 10-year restriction to 1 year.
 - (ii) Reduce the geographical area so that the restriction applies to the United Kingdom rather than Europe.
 - (iii) Delete 'or engineering'.
- (A) (i) only
 - (B) (ii) only
 - (C) (ii) and (iii) only
 - (D) (iii) only

? Question 19

Andy, a manager employed by BEE plc, carelessly instructed another employee, Chris, to carry out a wrongful act. Chris carried out the act and injured Danny in the process. Who may Danny take action against?

- (A) Andy only
- (B) Bee plc only
- (C) Andy and Chris only
- (D) Andy, Bee plc and Chris

? Question 20

Carol was injured by a worker carrying out road repairs and has decided to take action against MAC Ltd on the ground that the company is vicariously liable for the wrongful actions of the workers. Assuming the following to be true, which would be most likely to succeed as a defence?

- (A) The worker was a trainee.
- (B) The worker had been told not to do the act which caused the injury.
- (C) The worker was acting outside his employment.
- (D) The worker was entirely to blame for the injury.

? Question 21

Which of the following is not a legal person at law?

- (A) A public company
- (B) A corporation
- (C) A partnership
- (D) A private company

? Question 22

What does the expression 'limited by shares' mean?

- (A) The company's liability to pay its debts is limited.
- (B) The members' liability to discharge the company's debts is limited.
- (C) The company's ability to issue shares is limited to the number stated in the memorandum of association.
- (D) The company is limited to issuing shares and cannot issue debentures.

? Question 23

The memorandum of association of XYZ Ltd states that the company's authorised share capital is £50,000 divided into 100,000 ordinary 50p shares. The directors have the necessary authority to allot shares. Which of the following is *incorrect*?

- (A) The company may allot shares at 40p each.
- (B) The company may allot shares at 50p each.
- (C) The company may allot shares at 60p each.
- (D) The company may allot shares at £50 each.

? Question 24

PQR plc has an authorised capital of £400,000 divided into 400,000 ordinary £1 shares. To date the company has issued 100,000 shares at a premium of £1. In order to be authorised to commence trading, what is the minimum amount which must be paid up?

- (A) £100,000
- (B) £112,500
- (C) £400,000
- (D) £200,000.

? Question 25

What is the minimum number of persons needed to establish a single-member company?

- (A) One
- (B) Two
- (C) Three
- (D) Four.

? Question 26

In order for a private company to be able to purchase its own shares out of capital the directors must make a statutory declaration of solvency stating that the company will be able to

pay all its debts within a period not exceeding

- (A) 6 months
- (B) 12 months
- (C) 18 months
- (D) 24 months

? Question 27

Following the enactment of the Enterprise Act 2002, which of the following cannot stand as a preferential creditor?

- (i) Employees in respect of unpaid wages.
 - (ii) The Inland Revenue.
 - (iii) Employees in respect of unpaid holiday pay.
- (A) (i) only
 - (B) (i) and (ii) only
 - (C) (ii) only
 - (D) (iii) only

? Question 28

ABC Ltd is about to be incorporated. Tom, the person promoting the company, has entered into a contract with Seller Ltd, 'for and on behalf of ABC Ltd'. Who is liable if the contract with Seller Ltd is breached?

- (A) Tom
- (B) ABC Ltd
- (C) The directors of ABC Ltd
- (D) Tom and ABC Ltd jointly

? Question 29

Which of the following statements is correct? Under Section 89 of the Companies Act 1985

- (A) all new equity shares must be offered to the existing members first.
- (B) any new shares must be offered to the existing shareholders first.
- (C) equity shares issued for cash must be offered to the existing members first.
- (D) preference shares issued for cash must be offered to the existing members first.

? Question 30

Which of the following is correct? To allot unissued shares

- (i) the directors must be authorised by the articles of association or the shareholders.
- (ii) the company must have sufficient authorised capital available for the issue.
- (iii) the directors must pass a board resolution.

- (A) (i) only
- (B) (i) and (ii) only
- (C) (iii) only
- (D) (i), (ii) and (iii)

? Question 31

Max carried on business as a sole trader for a number of years. He decided to incorporate his business and transferred the premises and other assets to Max Ltd in return for shares. Max decided to maintain insurance for his business premises in his own name. The premises have been destroyed by fire. Which of the following is correct?

- (A) Max Ltd can claim on the insurance policy.
- (B) Max can claim on the insurance policy.
- (C) The company is not validly insured for this loss.
- (D) The insurance company must compensate Max or the company for the damage.

? Question 32

Who may the liquidator take action against in the event of 'wrongful trading'?

- (i) Directors and former directors.
 - (ii) Shadow directors.
 - (iii) All persons knowingly a party to the wrongful trading.
- (A) (i) only
 - (B) (i) and (ii) only
 - (C) (iii) only
 - (D) (i), (ii) and (iii)

? Question 33

Which of the following is correct in relation to the rule in *Foss v. Harbottle* (1843)?

- (A) Where a wrong is alleged to have been done to the company, the company is the proper claimant.
- (B) Where a wrong is alleged to have been done to the company, the holders of 10 per cent of the shares may claim on behalf of the company.
- (C) Where a wrong is alleged to have been done to the company, the directors may take proceedings in their own names.
- (D) Where a wrong is alleged to have been done to the company, no action can be taken without the approval of the majority shareholders.

? Question 34

XYZ Ltd has borrowed money from A Bank plc and provided security in the form of a fixed charge. Within how many days must the charge be registered at Companies House in order to fully valid?

- (A) 7 days
- (B) 14 days
- (C) 21 days
- (D) 28 days

? Question 35

Which of the following is not a characteristic of a floating charge?

- (A) A charge over specific identifiable property.
- (B) The company can deal freely with the asset in the ordinary course of business.
- (C) The assets change from time to time.
- (D) A charge over a class of assets.

? Question 36

Zed Bank plc issued a floating charge before the provisions of the Enterprise Act 2002 came into force. The Bank wishes to enforce its security. Who will the Bank appoint?

- (A) A Liquidator
- (B) An Administrative Receiver
- (C) An Administrator
- (D) The Official Receiver

? Question 37

Which of the following is correct in relation to administration orders?

- (i) An administration order may be made to ensure a fair distribution of a company's assets in liquidation.
 - (ii) The order prevents a company from being placed in liquidation.
 - (iii) The directors of a company may apply for an administration order.
- (A) (i) only
 - (B) (i) and (iii) only
 - (C) (ii) and (iii) only
 - (D) (iii) only

? Question 38

Which of the following is *incorrect*?

- (A) Directors cannot delegate their authority.
- (B) A person can act as a director and as a company secretary.
- (C) Directors do not owe fiduciary duties to individual shareholders.
- (D) A person may be classified as a director if he acts as such, even if he has not been validly appointed as a director.

? Question 39

What is the minimum amount which a person must be owed before he can present a winding up petition against a company?

- (A) £500
- (B) £750
- (C) £1,000
- (D) £5,000

? Question 40

Which of the following is *incorrect*?

- (A) The memorandum of association may be altered by a written or special resolution.
- (B) The articles of association may be altered by a written or special resolution.
- (C) The authorised shared capital may be increased by ordinary or written resolution.
- (D) The directors may be dismissed by ordinary or written resolution.

 **Solutions**

Solution 1 (B)	Solution 15 (D)	Solution 29 (C)
Solution 2 (C)	Solution 16 (B)	Solution 30 (D)
Solution 3 (C)	Solution 17 (C)	Solution 31 (C)
Solution 4 (B)	Solution 18 (D)	Solution 32 (B)
Solution 5 (B)	Solution 19 (D)	Solution 33 (A)
Solution 6 (A)	Solution 20 (C)	Solution 34 (C)
Solution 7 (B)	Solution 21 (C)	Solution 35 (A)
Solution 8 (C)	Solution 22 (B)	Solution 36 (B)
Solution 9 (C)	Solution 23 (A)	Solution 37 (C)
Solution 10 (D)	Solution 24 (B)	Solution 38 (A)
Solution 11 (B)	Solution 25 (B)	Solution 39 (B)
Solution 12 (B)	Solution 26 (B)	Solution 40 (D)
Solution 13 (B)	Solution 27 (C)	
Solution 14 (A)	Solution 28 (A)	

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