CHIEF EXAMINER COMMENTS WITH SUGGESTED POINTS FOR RESPONSES

JUNE 2021
LEVEL 6 – UNIT 1 - COMPANY AND PARTNERSHIP LAW

Note to Candidates and Learning Centre Tutors:

The purpose of the suggested points for responses is to provide candidates and learning centre tutors with guidance as to the key points candidates should have included in their answers to the June 2021 examinations. The suggested points for responses sets out a response that a good (merit/distinction) candidate would have provided. Candidates will have received credit, where applicable, for other points not addressed by the marking scheme.

Candidates and learning centre tutors should review the suggested points for responses in conjunction with the question papers and the Chief Examiners' **comments contained within this report,** which provide feedback on candidate performance in the examination.

CHIEF EXAMINER COMMENTS

General issues to be noted are as follows:

In the good scripts, candidates provided plenty of detail, accurate reference to statute and case law, and had carefully and correctly answered the question. There were some excellent answers, showing a good appreciation of the subject with a practical and professional element.

With the less good answers, candidates failed to include case law and sufficient and/or accurate reference to statute. In addition, candidates did not adequately take note of what the question was actually asking, and, for the Part B questions, failed to apply the law to the relevant facts. Answers tended to lack detail as well.

These candidates tend to focus too much on what they see to be the topic and regurgitate what they have learned rather than giving careful consideration to what the question was asking, or the facts were presenting.

All candidates need to be as accurate as possible especially with statutory and case law references, as well as ensuring they refer to correct terms.

For this paper, the tendency to merely repeat pre-learned answers was much less evident and candidates overall gave more considered answers. This is very welcome.

Overall, the advice continues to be, to read the question carefully and ensure all elements are addressed, with application of the facts for Part B questions. For both Parts, detailed and accurate references to and application of relevant statute and case law are essential. Read statutory provisions fully to ensure correct understanding.

CANDIDATE PERFORMANCE FOR EACH QUESTION

SECTION A

Question 1

This was the third most popular question and was generally well-answered. Some candidates provided commendable comparison between the types of business media and outlined the relevant advantages and disadvantages thoroughly. The poorer answer lacked detail and tended to merely repeat the key legal issues in relation to the types of business without comparison.

Question 2

This was the most popular question. Interestingly, although apparently quite straightforward, answers varied more than other questions. Some candidates did not give sufficient detail on statute or fully appreciate the different types of authority in part (a). Part (b) was generally well answered.

Question 3

Four candidates answered this question, making it the least popular. Most answers were adequate to good and covered the relevant issues.

Question 4

Five candidates answered this question. Part (a) answers tended to be rather thin on detail. Similarly, in part (b) candidates did not explore the elements of the offence of insider dealing in sufficient detail.

SECTION B

Question 1

The second most popular question, for which there were some thorough and well-considered answers. Most answers were merely adequate, lacking sufficient reference to case law and analysis in relation to the facts.

Question 2

This was answered by five candidates. Overall answers were poor, being sketchy and lacking precision.

Question 3

This was the fourth most popular question. Answers varied but generally candidates tackled it quite well with some application and references to case law. The better candidates presented the arguments accurately and analysed the scenario appropriately.

Question 4

About 13 candidates answered this question, with varying results. It suffered occasionally, timing-wise, from being the last question answered. There were a few strong answers, but most were average. Answers lacked sufficient detail on the whole.

SUGGESTED POINTS FOR RESPONSES LEVEL 6 – UNIT 1 - COMPANY AND PARTNERSHIP LAW
The purpose of this document is to provide candidates and learning centre tutors with guidance as to the key points candidates should have included in their answers to the June 2021 examinations. The Suggested Points for Responses do not for all questions set out all the points which candidates may have included in their responses to the questions. Candidates will have received credit, where applicable, for other points not addressed. Candidates and learning centre tutors should review this document in conjunction with the question papers and the Chief Examiners' reports which provide feedback on candidate's performance in the examination.

Section A

Question Number	Suggested points for responses	Max Marks
Q1	The answer consists of reasoned evaluation, offering a comparison of the types of media, their advantages and disadvantages, supported by examples. Responses should include: Liability issues: • Unlimited partnership: individual partners liable without limit for the debts and other liabilities of the partnership (s9 Partnership Act 1890 (PA 1890)). • Private companies: shareholders' liability is limited to the amount, if any, outstanding on shares (CA 2006). • Limited liability partnership (LLP): liability of partners is limited to amount agreed to contribute to assets of partnership in the event of it being wound up. • Linked to the above, private limited companies and LLPs have separate legal personality (Salomon v Salomon & Co Ltd [1897]) distinct from their members: legal entities in own right so they can enter into contracts, sue and be sued and are liable without limit for their own debts and liabilities. Comparison of regulation: • Companies and LLPs are highly regulated by statute – Companies Act 2006, Insolvency Act 1986, Limited Liability Partnerships Act 2000 and associated regulations. • For partnerships, the PA 1890 provides only a default set of rules in absence of agreement to contrary among partners (s24 PA 1890). • Company and LLP formation – statute regulates a clear-cut form and procure. No such formalities for partnerships exist: • Companies and LLPs are formed by a statutory process of registration of documents with Companies House	25 marks

	• There are also ongoing requirements under the CA 2006 eg to file annual accounts and to register other documents at Companies House recording changes in the company's directors, share capital, etc. • No formalities required for the formation of a partnership; a partnership exists if it satisfies the statutory test of two or more persons carrying on business with a view of profit (s1 PA 1890). Partnerships should have partnership agreement which adds to costs. (Kahn v Miah) Examples of advantages and disadvantages: • Disadvantage: Unlimited partnership: if the business fails the partners risk losing all property. • Advantage of using private company or LLP: shareholders/members know how much they may lose. • Companies are commercially flexible vehicles through which to conduct business without disadvantages of personal liability. • Disadvantage: a limited company does not always provide such security for members. Eg banks may insist upon personal guarantees from directors. • Lack of formality (and thus cost) of formation of partnerships can be a benefit. Cost of compliance with regulations can be relatively high for companies and LLPs. • The lack of required publication and disclosure of information can be a benefit for partnerships. • Documents filed at Companies House open to inspection by public; partnership is a private affair. This means that if secrecy is an issue for the members, partnership may be a more attractive option than a company or LLP. • Partners in LLP are not subject to statutory duties in CA 2006 that apply to directors (ss170-177 CA 2006). Responses could include: • Discussion of income: dividends for shareholders – but only as far as available and declared by the company; profits for partners – directly accessible if the business makes a profit. • Avoidance of liability for partners: transfer property into names of spouse to put it out of creditors • Potential for personal liability of the company directors through breach of duties under the CA 2006 and the Insolvency Act 1986. • LLP normally liable for own contractual obligations and tortious acts of members and employees. Partners of LLP may incur personal liability in tort for negligence. • Relations among shareholders and between shareholders and company governed by a combination of CA 2006 and company's articles of association.	

	• Re borrowing, only companies and LLPs can grant floating charges • Brief discussion of piercing the corporate veil – as a disadvantage of limited liability (Adams v Cape, and other such case law) • Reasoned conclusion to summarise briefly the balance of advantages and disadvantages	
	Total	**25 marks**
Question Number	**Suggested points for responses**	**Max Marks**
Q2(a)	The answer examines closely the nature of a partner's authority and how it arises, with reference to statute and case law as appropriate. Responses should include: • Partner is an agent of the partnership when acting on behalf of it (s5 PA 1890) • Authority can be actual (express or implied) or apparent/ostensible • Implications of a partner acting within their authority: the partnership is liable in contract • Actual authority can arise from express agreement, eg set out in a partnership deed; or from course of dealings. Reference to ss 6 and 7PA 1890 • If a partner acts outside their actual authority, sections 5 and 8 must be applied as apparent authority is to be considered. [Allow for reference to 'implied' authority as academic interpretations differ.] • Each of the elements of section 5 PA should be discussed carefully, and case law referenced. (Eg Polkinghorne and Mercantile Credit). • Consequently, liability can still fall on a partnership, because the partner's authority is 'apparent' to a third party. Responses could include: • Examples of how express or implied authority can arise: express provision in a partnership agreement; activity accepted impliedly by other partners. • Where the partnership is bound, if partnership assets are insufficient to meet partnership liabilities, the partners may have to use their own assets to meet such liabilities • If a partner binds a firm through apparent authority, the partnership may be able to recover from the partner for breach of actual authority – eg as a breach of the partnership agreement. • Partnership agreement may require a partner to indemnify the partnership for breach of actual authority • Even if a partner exceeds their actual and apparent authority, the other partners may ratify a transaction which that partner purports to make on behalf of the firm.	17 marks

2(b)	Discussion of the two situations, with reference to statute as appropriate Responses should include: • Incoming partner: not liable for debts before they join (s17(1) PA), unless they are held out (knowingly) or hold self out to be a partner in a transaction (s14 PA). Third party/creditor must show reliance on such representations. • Retiring partner is not liable for debts incurred after leaving the partnership; only those incurred while they were still a partner (s17(2) PA). • Also s36 PA applies – a person dealing with a firm is entitled to treat all apparent members as still part of partnership unless they have notice of any change. • Section 36: actual notice of the change to parties who have previously dealt with the partnership • Notice in the London Gazette to other potential third parties. Responses could include: • S 14 and holding out could also apply to retiring partner. • Possible indemnity to be sought by retiring partner from partnership • Novation agreement to be entered into between retiring partner, remaining partners and the creditor/third party	8 marks
	Total	**25 marks**

Question Number	Suggested points for responses	Max Marks

Q3	The answer consists of reasoned discussion of the relevant issues, emphasising the potential consequences of wrongful and fraudulent trading, breach of directors' duties and possible disqualification, with reference to statute and case law throughout.
	
	Responses should include:
	• Discussion of the meaning of insolvency for the purposes of s214
	• A detailed analysis of section 214 (IA 1986), including the conditions for the section to apply: the company is insolvent; the person was a director at the relevant time; what the director knew or should have concluded and the tests applied to the director's knowledge
	• Sanction for breach of s214 – namely the order to contribute and how the contribution is to be calculated on a 'compensatory' basis (per Re Produce Marketing).
	• A detailed analysis of section 213 (IA 1986), including the meaning of fraudulent trading and the requirement for intent to defraud
	• The most relevant directors' duties under CA 2006: s172 and the duty to promote the success of the company
	• Explanation of the duty and application in circumstances where the company has a duty to act in the interests of creditors
	• Sanctions for breach of the s172 duty
	• Possible disqualification under the CDDA 1986, including the relevant grounds – eg where a director is found to act in breach of company or insolvency law
	• Potential outcomes of a disqualification: prohibition from being involved in the management of a company as they are considered 'unfit'
	• Possible compensation order under s15A CDDA
	• Up to date case law throughout to illustrate the application of the different provisions. Eg Re Produce Marketing Consortium (No 2) Ltd, Brooks v Armstrong and Grant v Ralls
	• Throughout there should be clear identification of the possible consequences of the above actions, including:
	  ○ reference to any possible defences, such as the taking of every step to minimise loss to creditors under s214
	  ○ action that a liquidator or administrator could take
	  ○ for s214 for example, order by the court for a director to contribute to the assets of the company
		25

	Responses could include: • A brief critique of the relative success, or otherwise of actions under section 214 IA 1986 • A mention of the historical reason for the introduction of section 214 • Directors' personal guarantees could be enforced, leading to potential bankruptcy of the director • Action for wrongful /fraudulent trading assignable under s246ZD IA 1986 **Total**	**25 marks**

Question Number	Suggested points for responses	Max Marks
Q4(a)	The answer consists of a detailed discussion of the process of transferring a company's shares and how such transfer may be restricted by a company's articles, with reference to relevant statutory provisions throughout. Responses should include: The process • Requirement of a stock transfer form (STF) (under Stock Transfer Act 1963) completed by transferor. Section 770 CA 2006 • Delivery of the STF with a share certificate (if there is one) to the transferee • Transferee pays any consideration to transferor Transferee is responsible for getting STF stamped and paying stamp duty. • Once stamped, delivery of the STF to the company with any share certificate. Company issues new share certificate, and adds new member (transferee) to register of members. • Model article 26 provides regulations on share transfer The restrictions on transfer found in the articles • Possible limited restriction: refusal by a company's directors to register a transfer under MA 26 • Smaller companies may also include in the articles pre-emption requirement: shares to be first offered to existing shareholders before they are offered to an outsider • Possible requirement that a director must sell any shares in company to existing shareholders when they cease to be a director Responses could include: • A company cannot register a transfer of shares without a proper instrument • Directors must act in good faith in making decision to refuse to register a transfer (Smith v Fawcett) • S771: directors must either register transfer, or give notice of refusal, within 2 months.	12 marks

	• Pre-emption provisions may include detailed requirements for valuation of the shares and identification of the share price	
Q4(b)	The answer analyses how liability for insider dealing can arise under the CJA, with detailed reference to the relevant provisions and a breakdown of the elements of the definitions. Possible penalties are also included. Responses should include: • Reference to the relevant CJA provisions, ss 52 to 58 • The criminal offence is for individuals only • Behaviour must occur in the UK • Behaviour – dealing in (buying or selling) price affected securities on a regulated market (eg the London Stock Exchange) as an insider - s52(1) and s55 • Discussion of the meaning of the following: – 'insider': has information from an inside source, s57, eg company director or employee – 'inside information' and all its elements s56, s58 (where information is 'public') • The FCA has the power to impose penalties • Penalties include: a fine or imprisonment • Statutory defences: s53 Responses could include: • Discussion of the secondary offences of unlawful disclosure of inside information and of encouraging • Difficulty of bringing successful prosecutions under the CJA • Possible disqualification under CDDA	13 marks
	Total	**25 marks**

Section B

Question Number	Suggested points for responses	Max Marks
Q1	The answer consists of clear advice, with reference to the facts, on the implications of being a company 'promoter' and entering into pre-incorporation contracts Responses should include: • The meaning of promoter and the case of Twycross • Normally a person entering into contract on behalf of company acts as the company's agent, and so the company is liable. With a pre-	25 marks

	incorporation contract, not so as there is no company in existence to act as principal. • Mention of Margo's position as a fiduciary and the Erlanger case • Therefore there is potential personal liability of a promoter on entering into a pre-incorporation contract • Discussion of s51 CA 2006 - promoter is personally liable, subject to any 'agreement to the contrary'. • Clarification of the meaning of 'agreement to the contrary' and reference to case law, such as Phonogram Ltd v Lane: any such 'agreement to the contrary' must be expressly and clearly included within the contract. The court will not *imply* such agreement to the contrary. Words added to a signature that a person is signing as agent for and on behalf of a company being formed are not sufficient to exclude liability. Margo's protection: • First - as above, enter into an express agreement 'to the contrary' with the software company • Or enter into a contract with the company she is forming once incorporated; the company promises to perform obligations under licence (with third party), and to indemnify Margo against liability under initial contract. • A better option - a novation agreement: the company once formed agrees to perform on the same terms as in original contract, and the third party releases Margo from previous personal liability. • But the software company may not agree to this. • Include a term in the original contract that Margo's liability will cease at some point in future if company is incorporated and if company agrees to take over promoter's liability: this is close to 'agreement to the contrary' (in s51) although there is the disadvantage of creating (temporary) personal liability of promoter. • Finally, simply create a company as quickly as possible. Either a shelf company might be used or use the fast-track incorporation procedure at Companies House achieves now a similar effect. Responses could include: • S51 not clear whether Margo, promoter, will be entitled personally to enforce any pre-incorporation contract such as the software licence. • Braymist Ltd v Wise Finance Co Ltd [2002]: Court of Appeal held: not only does s51 impose obligations on promoter, but it can also confer rights on the promoter, against the third party, which the promoter can enforce. • If Margo enters into a contract with the company she forms, but the company cannot then to perform its obligations (eg it becomes insolvent), the third party can then sue Margo.	
	Total	**25 marks**

Question Number	Suggested points for responses	Max Marks
Q2(a)	The answer sets out clearly the principle of maintenance of capital, relevant case law and statutory provisions Responses should include: • The principle itself: derived from common law and the case of Trevor v Whitworth (1887): a company cannot return money to its shareholders, except after payment of all the company's creditors in a winding up or as permitted in the CA 2006 • The share capital is maintained to protect the interests of creditors • Shareholders are not liable to contribute to the debts of a company apart from any amount unpaid on their shares • Significant statutory regulation of the principle, imposing a number of restrictions • Two or three examples of restrictions – see below Responses could include: • Prohibition on reduction of capital or purchase of own shares, s658 CA 2006 • Payment of dividends – only where a company has available distributable profits, s830 CA 2006 • Prohibition on financial assistance – public companies only, s678 CA 2006 • Shares to have fixed nominal amount and shares cannot be issued at a discount to the nominal value	9 marks
Q2(b)	The answer consists of a detailed explanation of the procedure for buy back of the shares, with through reference to statutory provisions. Responses should include: • S690 permits a company to buy back its own shares, subject to requirements • Requirements: shares to be fully paid (as they are here) and no restrictions in the articles - Model Articles contain no such restrictions • Company can use distributable profits or the proceeds of a fresh issue of shares. Sufficient profits here • Purchase will be off market, s694 • A board meeting should approve the buy back and the contract subject to shareholder approval and convene the GM or propose a written shareholder resolution • A contract is required that must be approved by the shareholders by ordinary resolution, s 694 (in general meeting, on 14 clear days' notice, or by written resolution).	16 marks

	• Contract to be available for inspection 15 days before the GM, s696 (thus short notice of the GM is not possible) or sent with the written resolution to the members eligible to receive the written resolution • Geraldine cannot vote on the contract. Otherwise the resolution could be invalidated • Approval of the contract authorises the buy back (up to a limit of 5 years) • Following completion and payment to Geraldine, the shares will be cancelled • Geraldine should return any share certificate to the company Responses could include: • That the company can use capital as it is a private company but that would not be necessary as there are sufficient distributable profits • Accounts would need to be updated to reflect the buyback	
	Total	**25 marks**

Question Number	**Suggested points for responses**	**Max Marks**
Q3	The answer advises with reference to the facts, legislation and case law on the nature of fixed and floating charges and what the proposed charges would mean for Paul. Responses should include: • The nature of fixed and floating charges, with reference to the Panama and Woolcombers cases • a floating charge can only be created by a company and is an equitable charge created over a generic class of assets (such as Ecowork's undertaking here): Re Panama, New Zealand and Australian Royal Mail Co. • on creation, the floating charge does not attach to specific items within the class of assets. The charge attaches to particular assets only when it 'crystallises' into a fixed charge: Illingworth v Holdsworth. • That until crystallisation, the chargor company is free to deal with the assets under the charge without reference to the chargee: Re Yorkshire Woolcombers Association Ltd. • Discussion of the possible difficulties of creating a fixed charge over the company's book debts – i.e. the debts owed to the company and payments received in respect of such debts • Discussion of the case law on creation of charges over book debts: Re Spectrum Plus Ltd (2005), (and SIebe Gorman and Re New Bullas): whether there is the necessary control for the lender (Paul) over the charged assets to give rise to a fixed	25 marks

	charge and whether the borrower is able to use the moneys received to carry on the business. • in Spectrum the court overruling previous cases (Siebe Gorman (1979) and Re New Bullas (1994)): for a fixed charge to be created over book debts a lender must exert a high degree of control over the charged assets – for example requiring the borrower to pay sums received into a specified account, and from which the borrower could withdraw sums only with the consent of the lender. Likelihood that Paul will have little control over the charge or assets secured by it • Paul's protections: the charge will be a 'qualifying floating charge' giving the charge holder the right to appoint an administrator. • a degree of priority over other, in particular unsecured, creditors regarding the proceeds of sale of the assets subject to the charge. • this priority is restricted by rules (i) governing the registration and priority of different charges over the same asset, and (ii) designed to ensure a fairer treatment of unsecured creditors. Paul's charges would rank behind the bank's existing fixed charge, as fixed charges generally rank in order of creation and above floating charges. • Advice to register the charge with Companies House within the relevant time period after its creation. If not registered within the specified time limit (21 days of the creation of the charge: s859A(4) CA 2006), then it is void against an administrator or liquidator or any creditor of the company. • However, even if the charge is properly registered, it takes effect subject to any earlier (and properly registered) equitable charge over the same asset. • Unsecured creditors taking priority - preferential creditors: employees owed for example unpaid wages and accrued holiday remuneration (175 IA 1986); possible expenses of the winding up paid out of proceeds of sale of assets covered by a floating charge, s176ZA IA 1986. • Risk of any floating charge being set aside under s245 IA 1986, when the company goes into insolvency, if the charge was given to secure a 'pre-existing debt' owed by the company. Here the original loan is a 'pre-existing debt'. • New additional loan could also be treated as a pre-existing debt if that additional loan is made to the company before the floating charge is *actually* created: see Re Shoe Lace Ltd (1992). Paul should ensure that the new loan is only made *after* the floating charge has been created. • Then the floating charge would be valid insofar as it provides security for the additional loan, but would be potentially void	

	insofar as it provides security for the existing loan of £150,000 – only in event of company's insolvency within a certain period. • To be set aside under s245, the charge given to secure the earlier loan must be created within 12 months of the onset of insolvency in favour of an unconnected person (here Paul), and only if the company is unable to pay its debts at this time (or becomes unable as a result of creating the charge). • Detail is not known about Ecowork's finances, but they seem profitable. unknown Responses could include: • Administrators' rights: eg rights to take control over the company's undertaking to protect the interests of the charge holder. • Priority of any later properly registered legal charge over the floating charge. • Reference to protection of the floating charge at the Land Registry, as regards the freehold property. • Paul could an obligation on Ecoworks not to grant, over the same assets, a later charge which would take priority over it: a 'negative pledge', but only where that charge holder has actual notice of the earlier floating charge and the relevant negative pledge. • to increase the chance of 'ordinary' unsecured creditors receiving something from the company, the Enterprise Act 2002 requires that a proportion of assets secured by a floating charge must (subject to various exceptions) be set aside to pay off unsecured creditors. The proportion of the assets which must be used in this way varies according to the amount of the company's 'net property'.	
	Total	**25 marks**

Question Number	**Suggested points for responses**	**Max Marks**
Q4(a)	The answer will address in detail the relevant statutory provisions that provide the steps for appointment of a director and the approval of a service contract Responses should include: • Appointment by the board or in general meeting (by ordinary resolution), under MA 17 • If by shareholders, convene a general meeting or use a written resolution • Enter name on register of directors • Notify Companies House on form AP01	14 marks

	• Service contract: because it is for a fixed term over 2 years, shareholder approval required of the term, s188 CA 2006. • Ordinary resolution by GM or written resolution • Memorandum of contract to be provided to shareholders. • If approval not obtained, the term of 3 years is void, contract becomes terminable on reasonable notice, but contract still otherwise valid. • Note of duty of director to disclose interest in transaction with company, s177 • But even if Abdul is appointed before his service contract is approved, s177(6)(c) provides an exception to this • MA 14 still applies Responses could include: • Detail on the procedure such as board meetings to approve the appointment and the service contract, notice of GM, memorandum being available for inspection, or sent with written resolution • Mention of Atlas Wright case	
Q4(b)	The answer will analyse the facts and apply the law on directors to them, reaching a conclusion and setting out the consequential duties in the relation to the lease Responses should include: • Reference to the fact that Katerina has not been formally appointed • Seems to be de facto director (Re Hydrodam and s250 CA 2006) • Not a shadow director as she does not appear to be giving instructions to the company that it follows, s251 CA 2006 • Katerina will, if found to be a director, subject to duties under CA. • Most significant: Section 177 – duty disclose interest in the contract for this lease, but almost certainly s177(6)(b) would apply. • Must declare for example at the board meeting at which the contract is considered and approved - MA 14 also applies: she be counted in a quorum on the vote on the lease, nor can she vote it, unless an ordinary resolution is passed to waive MA 14 for this transaction Responses could include: • Question if she is part of the corporate governing structure (Hollier) • Reference to duty to promote the success of the company, s172 CA 2006 • A mention of s182 • The grant of the lease being an SPT.	11 marks

	Total	**25 marks**