

CHIEF EXAMINER COMMENTS WITH SUGGESTED POINTS FOR RESPONSES

LEVEL 6 - UNIT 1 – COMPANY AND PARTNERSHIP LAW

JUNE 2022

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 2022 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

Most of the issues below have been commented on in previous reports. Strong answers were coherent, detailed, with plenty of statutory and case law references where necessary. Close attention was paid to what the question was actually asking. In Part B answers, many answers were thorough and accurate in their application to the facts, whereas the weaker answers merely stated the law, with little if any reference to the case studies.

It is really important to refer to the facts, setting out how the law applies to them – care must be taken when answering the question to consider thoroughly all implications that arise from the facts.

Candidates are encouraged to read the facts and questions very carefully and think what they are being asked to do. Work through issues methodically, with plenty of detail. Try to write as coherent answers as possible. Include relevant and accurate references to statute.

Candidates are encouraged to check statutory provisions and ensure during revision that they are comfortable with what the sections say. For example, a common error is in the application of section 245 IA 1986 – floating charges only become invalid under this provision on insolvency when the charge is taken over a pre-existing debt. It is important to note this point. Further, candidates should review their understanding of the rules on authority to allot and statutory pre-emption rights.

To conclude, read the question, pay careful attention to detail, give plenty of case and statutory references and, for part B questions, refer to the facts and apply the law carefully.

CANDIDATE PERFORMANCE FOR EACH QUESTION

SECTION A

Question 1:

Strong candidates methodically worked through the issues, with plenty of reference to case law, actually answered to problem set, and came to a conclusion. The poorer answers lacked coherence and/or adequate detail.

Question 2:

This was the most popular question, but a fair few were quite mediocre answers. They lacked detail and case law and provided little explanation; rather just a list of the duties.

Question 3:

The poor results were surprising as this question should have been relatively straightforward. Unfortunately, candidates missed that there were 2 distinct parts to the answers.

Question 4:

(a) – candidates generally failed to address issues of pre-emptions rights, not fully addressing the restrictions imposed on directors in relation to allotment.

(b) – this was generally answered better than (a) as the relevant procedure is straightforward.

SECTION B

Question 1:

The strongest answers again worked methodically through the issues, addressed relevant statute and case law, and most importantly, applied the law to the facts in detail. The weaker scripts tended to repeat the law without much reference to the facts. This applied across all three parts of the question.

Question 2:

The same issues apply here as for Question B1, but also a number of the weaker candidates failed to address section 33 CA 2006 in sufficient detail. Answers to part (c) tended to be very superficial. A number of candidates discussed promoters and pre-incorporation contracts in part (a), but these were not relevant to the question.

Question 3:

The top marked script covered all the relevant issues and applied them carefully to the facts. The remaining scripts were very variable in their application, and several candidates missed a couple of crucial points.

Question 4:

Most answers were quite adequate, and many were careful to apply the law to the facts in detail. The weakest answers merely stated the law without consideration of the implications of the facts.

SUGGESTED POINTS FOR RESPONSE

LEVEL 6 - UNIT 1 – COMPANY AND PARTNERSHIP LAW

Question Number	Suggested Points for Responses	Marks (Max)
1	<p>Responses should include:</p> <ul style="list-style-type: none"> • Separate legal personality • <u>Salomon v Salomon</u> • Company is responsible for its own debts • Case law to include: <u>Adams v Cape</u>, Prest and Nutritek • Detailed discussion of the grounds including shams/facades; statutory provisions and agency • Insufficient grounds such as the interests of justice or separate economic entity • Possible liability in tort and the circumstances required to exist: <u>Chandler v Cape and Vedanta</u>. <p>Responses could include:</p> <ul style="list-style-type: none"> • Discussion of restrictive approach of the courts • Most recent decisions such as Okpabi, and Hurstwood Properties 	25 marks
Question 1 Total: 25 marks		

Question Number	Suggested Points for Responses	Marks (Max)
2	<p>Responses should include discussion of:</p> <ul style="list-style-type: none"> • Background to duties and common law equitable principles • Reference to section 170 CA 2006 • S171, Duty to act within powers and associated case law • S172, Duty to promote the success of the company and associated case law • The different stakeholders for consideration under s172 • S173, Duty to exercise independent judgment and associated case law • S174, Duty to exercise reasonable skill and expertise and associated case law • S175, Duty to avoid conflicts of interest and associated case law • Where a director benefits, there is no need to show that company was deprived of that benefit • S176, Duty not to accept benefits and associated case law • Directors should account for profits gained • Service contracts may provide for consequences of breach • Company is the party to sue for breach (Foss v Harbottle) • A mention of derivative claims <p>Responses could include:</p> <ul style="list-style-type: none"> • Authority derived from the articles • Comment that section 172 has prompted much debate • More detail on derivative claims • Directors' disqualification • Removal of directors under s168 CA 2006 • Relief from liability under s1157 CA 2006 	25 marks
Question 2 Total:25 marks		
Question Number	Suggested Points for Responses	Marks (Max)
3	<p>Responses should include discussion of the requirements in relation to:</p> <ul style="list-style-type: none"> • Disclosure of transactions under sections 177 and 182 • Model article 14 and avoidance of conflict of interest – director may not be able to vote or count in a quorum at the relevant board meeting • Service contract approval and section 188 etc • Shareholder approval by OR of a fixed term of a service contract of over 2 years • Memorandum of the contract to accompany the shareholder resolution and to be available for 15 days prior to a GM or attached to a written resolution • Substantial property transactions and section 190, etc • Requirement for shareholder approval (OR) • Sale or purchase of substantial asset (over £100,000 or 10% of the company's assets) to or from a director or a person connected with them 	25 marks

	<ul style="list-style-type: none"> Loans to directors and section 197 etc Shareholder approval by OR Possible methods of shareholder approval for each of the above Each can be passed in General Meeting or by written resolution Exemptions to requirements for shareholder approval – thresholds and exemption where loan is given for purpose of carrying out duties <p>Responses could include:</p> <ul style="list-style-type: none"> Brief mention of section 175 (avoidance of conflict of interest) Criminal sanctions under s182 Where a memorandum is required, any GM cannot be held on short notice to avoid breach of the 15 day inspection rule 	
Question 3 Total:25 marks		
Question Number	Suggested Points for Responses	Marks (Max)
4(a)	<p>Responses should include discussion of:</p> <ul style="list-style-type: none"> Basic requirement for authority to allot (s549) Automatic authority for private companies with one class of share (s550) Section 551 authority and its elements (max number of shares and time limit) Need for shareholder approval by ordinary resolution Pre-emption requirements under s561 Possible disapplication under s570 or 571 Requirement for shareholder approval by special resolution Filing of resolutions at Companies House <p>Responses could include:</p> <ul style="list-style-type: none"> Reference to disapplication under ss 567 or 569 Possible approvals in GM or by written resolution Registration of allotments – both internal and at Companies House (ss554 and 555) 	14 marks
4(b)	<p>The answer consists of a discussion of the process of transferring shares and possible restrictions placed on such transfer in a company's articles</p> <p>Marks should be distributed in the following areas:</p> <ul style="list-style-type: none"> The process of transfer by means of a stock transfer form; the responsibilities of the transferor and transferee; stamp duty (max 5 marks) Possible restrictions in a company's articles, including Model Article 26 and potential pre-emption rights (max 5 marks) Reasoned conclusion (max 1 mark) <p>Answers should include: The process</p>	11 marks

	<ul style="list-style-type: none"> • 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, and 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 <p>The restrictions on transfer found in the articles</p> <ul style="list-style-type: none"> • Model article 26 provides regulations on share transfer • Possible limited restriction: refusal by a company's directors to register a transfer • 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 <p>Answers could include:</p> <ul style="list-style-type: none"> • 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 (<u>Smith v Fawcett</u>) • S771: directors must either register transfer, or give notice of refusal, within 2 months. • Pre-emption provisions may include detailed requirements for valuation of the shares and identification of the share price 	
Question 4 Total: 25 marks		

SECTION B

Question Number	Suggested Points for Responses	Marks (Max)
1(a)	<p>Responses should include discussion of:</p> <ul style="list-style-type: none"> • Unlimited partnership: relation that subsists between persons carrying on business in common with a view of profit (s1 PA 1890). A written agreement is not necessary provided the s1 definition is satisfied. • Key elements to this definition • Two or more persons carrying on a business in common. There are 2 partners in the scenario • Business is defined fairly widely by s45 PA 1890 as including every trade, occupation or profession. There is a trade providing distribution services • Section 2 PA 1890 provides some guidance: co-ownership (a joint tenancy, tenancy in common, joint property, common property or part ownership) does not of itself create a partnership. These provisions are indicative only and not determinative of the existence of a partnership. Evidence: the lease of the property to the business • A business may consist of a single venture or, perhaps more frequently, a series of continuing activities. <u>Khan and Another v Miah and Another</u> (2001) • There must however be more than mere agreement to form a partnership (<u>Ilott v Williams</u> (2013)). They are carrying on the business – 4 years so far. • Concept of a business being carried on “in common” implies shared responsibility for decision making. Management shared equally • Must be intention to carry on business “with a view of profit” • Section 2 (3) PA 1890 provides that the receipt by a person of a share of profits is prima facie evidence that he is a partner • Here profits are shared equally <p>Conclusion:</p> <ul style="list-style-type: none"> • Strong grounds that A and L are in partnership. <p>Responses could include:</p> <ul style="list-style-type: none"> • Profit-sharing – one of several factors to be taken into account – but is a strong indicator • Lack of written agreement is not a factor • Contrast with employer/employee relationship • A mention of what ‘unlimited’ refers to 	12 marks

Question Number	Suggested Points for Responses	Marks (Max)
1(b)	<p>Responses should include discussion of:</p> <ul style="list-style-type: none"> No requirement for a written agreement PA 1890 will imply certain rights and obligations Benefits of a written agreement clarify arrangements Management roles can be provided for and respective rights and obligations set out Helpful to set out capital input Profit and loss sharing ratios can be specified as PA would imply equal sharing if no agreement to the contrary <p>Responses could include:</p> <ul style="list-style-type: none"> Possibility of provision for salaries, drawings, interest, expulsion and what constitutes partnership property 	8 marks
1(c)	<p>The answer consists of a brief discussion of what partnership property is under the PA 1890.</p> <p>Marks should be distributed in the following areas:</p> <ul style="list-style-type: none"> Discussion of sections 20 and 21 PA 1890 and application to the facts Reasoned conclusion <p>Responses should include discussion of:</p> <ul style="list-style-type: none"> Elements of section 20 PA 1890 Property brought into the partnership stock or acquired on account of the firm Need to ask question if the partnership will pay for the van Will the van count as part of M's capital contribution? Section 21: if the van is paid for out of partnership money, it will be deemed as partnership property 	5 marks
Question 1 Total:25 marks		
Question Number	Suggested Points for Responses	Marks (Max)
2(a)	<p>Responses should include discussion of:</p> <ul style="list-style-type: none"> Requirement for registration to create the company Filing of forms with Companies House Details of director(s) Shareholders and shareholdings Company constitution (memorandum and articles) Model Articles or tailored articles Payment of a fee Company exists once certificate of incorporation has been issued <ul style="list-style-type: none"> Name must end in 'limited' or 'ltd' 	11 marks

	<ul style="list-style-type: none"> Name must not be the same as or similar to that of another company Need to check the register for this <p>Responses could include:</p> <ul style="list-style-type: none"> Possibility of use of a shelf company The need for a business transfer agreement as A will effectively sell the business to the company in return for shares Possibility of use of a business name as well as the registered name 	
Question Number	Suggested Points for Responses	Marks (Max)
2(b)	<p>Responses should include discussion of:</p> <ul style="list-style-type: none"> Section 33 CA: articles form a contract between the company and each member General provisions concerning membership Key case law on s33 – eg <u>Rayfield v Hands</u>; <u>Hickman v Kent</u> Enforcement of the contract by a member whose rights are being infringed Protection for minority shareholders Regulation of the internal management of the company Model articles (default articles) give wide powers to directors Directors can manage the company as they see fit (MA 3) Articles can be altered only by special resolution <p>Responses could include:</p> <ul style="list-style-type: none"> Articles can be the Model articles or can be tailored Specific restrictions can be imposed on directors; for example on powers to borrow 	8 marks
Question Number	Suggested Points for Responses	Marks (Max)
2(c)	<p>Responses should include discussion of:</p> <ul style="list-style-type: none"> Unlimited liability of a sole trader No separation of the business from Amelia Personal assets can be at stake Liability of a shareholder limited to any amount unpaid on shares received On winding up, A will receive capital back if company is solvent <p>Responses could include:</p> <ul style="list-style-type: none"> Amelia should effectively pay in full for the shares that are issued to her when she transfers the business to the company Shareholder is at bottom of list for asset distribution on a winding up 	6 marks
Question 2 Total:25 marks		

Question Number	Suggested Points for Responses	Marks (Max)
3	<p>Responses should include discussion of:</p> <ul style="list-style-type: none"> • Possible wrongful trading by the directors • The elements of section 214 • Objective and subjective tests • Individual directors and their potential liability • What each director should have known for example and the standard applied to each • Sam – limited experience so for example objective test • Higher standard expected of Joshua as an accountant • Application of facts: did the directors take every step to minimise loss? Possibility not as Joshua and Kamal went on holiday • Possibility of contribution to the company’s assets • The elements of a transaction at undervalue (s238 IA) • Relevant time (s240) – application – within 2 years of onset of insolvency (ie when the company goes into liquidation). Transaction was less than 2 years before • Company was unable to pay its debts at the time of the transaction – it was in financial difficulty • Transaction is for consideration considerably less than the value of the asset • Defence if the transaction was in good faith • Consequences: possible return of the asset to the company by order of the court (s241) <ul style="list-style-type: none"> • The elements of a preference (section 239 IA) • Relevant time (s240) – application. Within 2 years of onset of insolvency where the preference is in favour of a connected person. Otherwise 6 months. • Here there is a connected person – the father of a director – section 249 and 435 IA • Muhammed was a creditor of the company • He was put into a better position than other creditors • Payment must have been influenced by a desire to prefer the creditor (Re MC Bacon). • Order of the court similar to that under s238 and 241 <p>Responses could include:</p> <ul style="list-style-type: none"> • Details of financial position would be helpful to ascertain when company ceased to be able to pay its debts, eg re the transaction at undervalue • Influence is presumed where payment is to a connected person • Reference to the temporary ‘suspension’ of wrongful trading during the period 1/3/2020 to 1/6/2021 by virtue of s12 CIGA 2020. 	25 marks
	Question 3 Total: 25 marks	



Question Number	Suggested Points for Responses	Marks (Max)
4	<p>Answers should include:</p> <ul style="list-style-type: none"> • The nature of fixed and floating charges, with reference to the Panama and Woolcombers cases • only a company can create a floating charge which is an equitable charge over a generic class of assets (such as GO's undertaking here): <u>Re Panama, New Zealand and Australian Royal Mail Co.</u> • the charge attaches to particular assets only when it 'crystallises' into a fixed charge: <u>Illingworth v Holdsworth</u>. Not on creation of the charge • until crystallisation, the chargor company is free to deal with the assets under the charge without reference to the chargee: <u>Re Yorkshire Woolcombers Association Ltd</u> • the possible difficulties of creating a fixed charge over the company's book debts – ie the debts owed to the company and payments received in respect of such debts • the case law on creation of charges over book debts: <u>Re Spectrum Plus Ltd (2005)</u>, (and <u>Siebe Gorman</u> and <u>Re New Bullas</u>): whether there is the necessary control for the lender (David) over the charged assets to give rise to a fixed charge and whether the borrower is able to use the moneys received to carry on the business. • in Spectrum the court overruling previous cases (<u>Siebe Gorman (1979)</u> and <u>Re New Bullas (1994)</u>): for a fixed charge to be created over book debts a lender must exert a high degree of control over the charged assets • likelihood that David will have little control over the charge or assets secured by it • 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 governing the registration and priority of different charges over the same asset. David'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 (21 days: s859A(4) CA 2006). Non-registration means charge is void against an administrator or liquidator or any creditor of the company • Unsecured creditors may take priority – eg preferential creditors: employees owed for example unpaid wages and accrued holiday remuneration (175 IA 1986) • Risk of any floating charge being set aside as void 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' 	25 marks

	<ul style="list-style-type: none"> • David should also ensure that the new loan is only made <i>after</i> the floating charge has been created (Re Shoe Lane) • 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 David), and only if the company is unable to pay its debts at this time (or becomes unable as a result of creating the charge). <p>Answers could include:</p> <ul style="list-style-type: none"> • Even if the charge is properly registered, it takes effect subject to any earlier (and properly registered) equitable charge over the same asset. • 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. • Discussion of a negative pledge 	
	Question 4 Total: 25 marks	