Answers

1 *Tutorial note:*

In order to apply any piece of legislation, judges have to determine its meaning. In other words they are required to interpret the statute before them in order to give it meaning. The difficulty, however, is that the words in statutes do not speak for themselves and interpretation is an active process, and at least potentially a subjective one depending on the situation of the person who is doing the interpreting.

Judges have considerable power in deciding the actual meaning of statutes, especially when they are able to deploy a number of competing, not to say contradictory, mechanisms for deciding the meaning of the statute before them. There are, essentially, two contrasting views as to how judges should go about determining the meaning of a statute – the restrictive, literal approach and the more permissive, purposive approach.

(a) The literal approach

The literal approach is dominant in the English legal system, although it is not without critics, and devices do exist for circumventing it when it is seen as too restrictive. This view of judicial interpretation holds that the judge should look primarily to the words of the legislation in order to construe its meaning and, except in the very limited circumstances considered below, should not look outside of, or behind, the legislation in an attempt to find its meaning.

Within the context of the literal approach there are two distinct rules:

(i) *The literal rule*

Under this rule, the judge is required to consider what the legislation actually says rather than considering what it might mean. In order to achieve this end, the judge should give words in legislation their literal meaning, that is, their plain, ordinary, everyday meaning, even if the effect of this is to produce what might be considered an otherwise unjust or undesirable outcome (*Fisher* v *Bell* (1961)) in which the court chose to follow the contract law literal interpretation of the meaning of offer in the Act in question and declined to consider the usual non-legal literal interpretation of the word (offer).

(ii) *The golden rule*

This rule is applied in circumstances where the application of the literal rule is likely to result in what appears to the court to be an obviously absurd result. It should be emphasised, however, that the court is not at liberty to ignore, or replace, legislative provisions simply on the basis that it considers them absurd; it must find genuine difficulties before it declines to use the literal rule in favour of the golden one. As examples, there may be two apparently contradictory meanings to a particular word used in the statute, or the provision may simply be ambiguous in its effect. In such situations, the golden rule operates to ensure that preference is given to the meaning that does not result in the provision being an absurdity. Thus in *Adler* v *George* (1964) the defendant was found guilty, under the Official Secrets Act 1920, with obstruction 'in the vicinity' of a prohibited area, although she had actually carried out the obstruction 'inside' the area.

(b) The purposive approach

The purposive approach rejects the limitation of the judges' search for meaning to a literal construction of the words of legislation itself. It suggests that the interpretative role of the judge should include, where necessary, the power to look beyond the words of statute in pursuit of the reason for its enactment, and that meaning should be construed in the light of that purpose and so as to give it effect. This purposive approach is typical of civil law systems. In these jurisdictions, legislation tends to set out general principles and leaves the fine details to be filled in later by the judges who are expected to make decisions in the furtherance of those general principles.

European Community (EC) legislation tends to be drafted in the continental manner. Its detailed effect, therefore, can only be determined on the basis of a purposive approach to its interpretation. This requirement, however, runs counter to the literal approach that is the dominant approach in the English system. The need to interpret such legislation, however, has forced a change in that approach in relation to Community legislation and even with respect to domestic legislation designed to implement Community legislation. Thus, in *Pickstone* v *Freemans plc* (1988), the House of Lords held that it was permissible, and indeed necessary, for the court to read words into inadequate domestic legislation in order to give effect to Community law in relation to provisions relating to equal pay for work of equal value. (For a similar approach, see also the House of Lords' decision in *Litster* v *Forth Dry Dock* (1989) and the decision in *Three Rivers DC* v *Bank of England (No 2)* (1996).) However, it has to recognise that the purposive rule is not particularly modern and has its precursor in a long established rule of statutory interpretation, namely the mischief rule.

The mischief rule

This rule permits the court to go behind the actual wording of a statute in order to consider the problem that the statute is supposed to remedy.

In its traditional expression it is limited by being restricted to using previous common law rules in order to decide the operation of contemporary legislation. Thus in *Heydon's case* (1584) it was stated that in making use of the mischief rule the court should consider what the mischief in the law was which the common law did not adequately deal with and which statute law had intervened to remedy. Use of the mischief rule may be seen in *Corkery* v *Carpenter* (1950), in which a man was found guilty of being drunk in charge of a carriage although he was in fact only in charge of a bicycle.

2 **(a)** The effect of the postal rule is such that where acceptance of a contractual offer is through the postal service, acceptance is complete as soon as the letter, properly addressed and stamped, is posted. The contract is concluded, even if the letter subsequently fails to reach the offeror. Thus in *Adams* v *Lindsell* (1818), the defendant made an offer to the plaintiff on 2 September. Due to misdirection, the letter was delayed. It arrived on 5 September and Adams immediately posted an acceptance. On 8 September, Lindsell sold the merchandise to a third party. On 9 September, the letter of acceptance from Adams arrived. It was held that a valid acceptance took place when Adams posted the letter. Lindsell was, therefore, liable for breach of contract.

The postal rule applies equally to telegrams (*Byrne* v *Van Tienhoven* (1880)), but it does not apply when means of instantaneous communication are used (*Entores* v *Far East Corp* (1955)). Also the postal rule will apply only where it is in the contemplation of the parties that post will be used as the means of acceptance. If the parties have negotiated either face-to-face, for example in a shop, or over the telephone, then it might not be reasonable for the offeree to use the post as a means of communicating their acceptance and they would not gain the benefit of the postal rule.

Where acceptance is by e-mail, it has been argued that this situation should be treated as a 'face-to-face' situation where receipt only occurs when the recipient reads the e-mail (*Brinkibon Ltd* v *Stahag Stahl und Stahlwarenhandelsgesellshaft mbH* (1983)). Where the agreement is conducted on the Internet, regulation 11 of the Electronic Commerce (EC Directive) Regulations 2002 indicates that the contract is concluded when the service provider's acknowledgment of receipt of acceptance is received by electronic means.

(b) Privity of contract

The doctrine of privity in contract law provides that a contract can only impose rights or obligations on persons who are parties to it. Its operation may be seen in *Dunlop* v *Selfridge* (1915). Dunlop sold tyres to a distributor, Dew and Co, on terms that the distributor would not sell them at less than the manufacturers list price, and that they would extract a similar undertaking from anyone they supplied with tyres. Dew and Co resold the tyres to Selfridge who agreed to abide by the restrictions and to pay Dunlop £5 for each tyre they sold in breach of them. When Selfridge sold tyres at below Dunlop's list price, Dunlop sought to recover the promised £5 per tyre sold. It was held that Dunlop could not recover damages on the basis of the contract between Dew and Selfridge to which they were not a party.

There are a number of ways in which consequences of the application of strict rule of privity may be avoided to allow a third party to enforce a contract. These occur at both common law and under statute.

(i) *Common law:*

– The beneficiary sues in some other capacity.

A person who was not originally a party to a particular contract may, nonetheless, acquire the power to enforce the contract where they are legally appointed to administer the affairs of one of the original parties. An example of this can be seen in *Beswick* v *Beswick* (1967) where a coal merchant sold his business to his nephew in return for a consultancy fee of £6·10 shillings (in pre-decimal currency) during his lifetime, and thereafter an annuity of £5 per week payable to his widow. After the uncle died, the nephew stopped paying the widow. When she became administratrix of her husband's estate, she sued the nephew for specific performance of the agreement in that capacity as well as in her personal capacity. It was held that, although she was not a party to the contract and therefore could not be granted specific performance in her personal capacity, such an order could be awarded to her as the administratrix of the deceased person's estate.

– The situation involves a collateral contract.

A collateral contract arises where one party promises something to another party if that other party enters into a contract with a third party, for example, A promises to give B something if B enters into a contract with C. In such a situation, the second party can enforce the original promise, that is, B can insist on A complying with the original promise. In *Shanklin Pier* v *Detel Products Ltd* (1951), the plaintiffs contracted to have their pier repainted. On the basis of promises as to its quality, the defendants persuaded the pier company to insist that a particular paint produced by Detel be used. The painters used the paint but it proved unsatisfactory. The plaintiffs sued for breach of the original promise as to the suitability of the paint. The defendants countered that the only contract they had entered into was between them and the painters to whom they had sold the paint, and that as the pier company were not a party to that contract they had no right of action against Detel. The pier company were successful. It was held that, in addition to the contract for the sale of paint, there was a second collateral contract between the plaintiffs and the defendants by which the latter guaranteed the suitability of the paint in return for the pier company specifying that the painters used it.

– There is a valid assignment of the benefit of the contract.

A party to a contract can transfer the benefit of that contract to a third party through the formal process of assignment. The assignment must be in writing, and the assignee receives no better rights under the contract than the assignor possessed. The burden of a contract cannot be assigned without the consent of the other party to the contract.

– Where it is foreseeable that damage caused by any breach of contract will cause a loss to a third party.

In *Linden Gardens Trust Ltd* v *Lenesta Sludge Disposals Ltd* (1994), the original parties had entered into a contract for work to be carried out on property with the likelihood that it would subsequently be transferred to a third party. The defendant's poor work, amounting to a breach of contract, only became apparent after the property had been transferred. There had been no assignment of the original contract and, normally, under the doctrine of privity, the new owners would have no contractual rights against the defendants and the original owners of the property would have suffered only a nominal breach as they had sold it at no loss to themselves. Nonetheless, the House of Lords held that, under such circumstances, and within a commercial context, the original promisee should be able to claim full damages on behalf of the third party for the breach of contract.

– One of the parties has entered the contract as a trustee for a third party.

There exists the possibility that a party to a contract can create a contract specifically for the benefit of a third party. In such limited circumstances, the promisee is considered as a trustee of the contractual promise for the benefit of the third party. In order to enforce the contract, the third party must act through the promisee by making them a party to any action. For a consideration of this possibility, see *Les Affreteurs Reunis SA* v *Leopold Walford (London) Ltd* (1919).

The other main exception to the privity rule at common law is agency, where the agent brings about contractual relations between two other parties even where the existence of the agency has not been disclosed.

(ii) *Statute*

The first area in which statute has intervened in relation to the doctrine of privity is in relation to motor insurance where third parties claim directly against the insurers of the party against whom they have a claim.

The most significant alteration of the operation of the doctrine of privity however, has been made by the *Contracts (Rights of Third Parties) Act* 1999 which sets out the circumstances in which third parties can enforce terms of contracts. In order for the third party to gain rights of enforcement, the contract in question must, either, expressly confer such a right on them or, alternatively, it must have been clearly made for their benefit (s.1). The contractual agreement must actually identify the third party, either by name, or as a member of a class of persons, or answering a particular description. The third person need not be in existence when the contract was made, so it is possible for parties to make contracts for the benefit of as yet unborn children. This provision should also reduce the difficulties relating to pre-incorporation contracts in relation to registered companies. The third party may exercise the right to any remedy which would have been available had they been a party to the contract. Such rights are, however, subject to the terms and conditions contained in the contract and they can get no better right than the original promisee.

Section 2 of the Act provides that, where a third party has rights by virtue of the Act, the original parties to the contract cannot agree to rescind it or vary its terms without the consent of the third party; unless the original contract contained an express term to that effect.

Section 3 allows the promisor to make use of any defences or rights of set-off they might have against the promisee in any action by the third party. Additionally, the promisor can also rely on any such rights against the third party.

Section 5 removes the possibility of the promisor suffering from double liability in relation to the promisor and the third party. It provides, therefore, that any damages awarded to a third party for a breach of the contract be reduced by the amount recovered by the original promisee in any previous action relating to the contract.

The Act does not alter the existing law relating to negotiable instruments, contracts of employment, or contracts for the carriage of goods or the statutory contracts constituted by to companies' constitutional documents.

3 This question requires an explanation of two aspects the law relating to damages for breach of contract. Every failure to perform a primary obligation is a breach of contract. The secondary obligation on the part of the contract-breaker, by implication of the common law, is to pay monetary compensation to the other party for the loss sustained by him in consequence of the breach (*Photo Productions Ltd* v *Securicor Transport Ltd* (1980)). Such monetary compensation for breach of contract is damages. There are, however, two distinct aspects to this general concept that have to be considered.

(a) *Liquidated damages and penalty clauses*

It is possible, and common in business contracts, for the parties to an agreement to make provisions for possible breach by stating in advance the amount of damages that will have to be paid in the event of any breach occurring. Damages under such a provision are known as liquidated damages. They will only be recognised by the court if they represent a genuine pre-estimate of loss, and are not intended to operate as a penalty against the party in breach. If the court considers the provision to be a penalty, it will not give it effect, but will award damages in the normal way.

In *Dunlop* v *New Garage and Motor Co* (1915), the plaintiffs supplied the defendants with tyres, under a contract designed to achieve resale price maintenance. The contract provided that the defendants had to pay Dunlop £5 for every tyre they sold in breach of the resale price agreement. When the garage sold tyres at less than the agreed minimum price, they resisted Dunlop's claim for £5 per tyre, on the grounds that it represented a penalty clause. On the facts of the situation, the court decided that the provision was a genuine attempt to fix damages, and was not a penalty. It was, therefore, enforceable.

In deciding the legality of such clauses, the courts will consider the effect, rather than the form, of the clause as is seen in *Cellulose Acetate Silk Co Ltd* v *Widnes Foundry (1925) Ltd* (1933). In that case, the contract expressly stated that damages for late payment would be paid by way of penalty at the rate of £20 per week. In fact, the sum of £20 was in no way excessive and represented a reasonable estimate of the likely loss. On that basis, the House of Lords enforced the clause in spite of its actual wording.

(b) *The duty to mitigate losses*

This rule relates to the rule that the injured party in the situation of a breach of contract is under a duty to take all reasonable steps to minimise their loss. The operation of the rule means that the buyer of goods that are not delivered, as required under the terms of a contract, has to buy the replacements as cheaply as possible. Correspondingly, the seller of goods that are not accepted in line with a contractual agreement has to try to get as good a price as they can when they sell them.

In *Payzu* v *Saunders* (1919), the parties entered into a contract for the sale of fabric, which was to be delivered and paid for in instalments. When the purchaser, Payzu, failed to pay for the first instalment on time, Saunders refused to make any further deliveries unless Payzu agreed to pay cash on delivery. The plaintiff refused to accept this and sued for breach of contract. The court decided that the delay in payment had not given the defendant the right to repudiate the contract. As a consequence, he had breached the contract by refusing further delivery. The buyer, however, should have mitigated his loss by accepting the offer of cash on delivery terms. His damages were restricted, therefore, to what he would have lost under those terms, namely, interest over the repayment period.

In *Western Web Offset Printers Ltd* v *Independent Media Ltd* (1995), the parties had entered into a contract under which the plaintiff was to publish 48 issues of a weekly newspaper for the defendant. In the action, which followed the defendant's repudiation of the contract, the only issue in question was the extent of damages to be awarded. The Court of Appeal decided that as the claimant had been unable to replace the work due to the recession in the economy and, therefore, had not been able to mitigate the loss, it was entitled to receive the full amount that would have been due in order to allow it to defray the expenses it would have had to pay during the period the contract should have lasted.

However, in relation to anticipatory breach of contract the injured party can wait until the actual time for performance before taking action against the party in breach. In such a situation, they are entitled to make preparations for performance, and claim the agreed contract price, even though this apparently conflicts with the duty to mitigate losses (*White and Carter (Councils)* v *McGregor* (1961)).

4 Whilst there is a contractual relationship between an auditor and his client the company as a legal entity, on which the client company can sue, the contentious legal area arises in respect of other people who may rely on reports made or advice given in a non-contractual capacity. Indeed, in many situations, the potential plaintiff may be unknown to the accountant. Although it is apparent that the law of negligence allows individuals in non-contractual relationships to sue for damages sustained as result of the negligent behaviour of another party, the success of any such action in relation to company auditors appears to depend upon the purpose for which reports are made or accounts prepared and on establishing a duty of care between the auditor and the person making the claim in negligence. The applicable law may derived from a number of important cases.

In *JEB Fasteners* v *Marks, Bloom and Co* (1983), the defendants, a firm of accountants, negligently overstated the value of stock in preparing audited accounts for their client. At the time of preparation, the accountants were aware that their client was in financial difficulties and actively seeking financial assistance. After seeing the accounts, the plaintiffs decided to take over the company. They then discovered the true financial position and sued the accountants for negligent misstatement. It was held that a duty of care was owed by the accountants as it was foreseeable that someone contemplating a takeover might rely on the accuracy of the accounts, but that they were not liable as their negligence had not caused the loss to the plaintiffs. The evidence revealed that, when they took over the company, they were not interested in the value of the stock but in acquiring the expertise of the directors, so, although they relied on the accounts, the accounts were not the cause of the loss as they would have taken over the company in any respect.

The case of *Caparo Industries plc* v *Dickman* (1990) served to limit the potential liability of auditors in auditing company accounts. Accounts were audited in accordance with the Companies Act 1985. The respondents, who already owned shares in the company, after seeing the accounts, decided to purchase more shares and take over the company. They then incurred a loss which they blamed on the inaccurate and negligently audited accounts. It was held that when the accounts were prepared, a duty of care was owed collectively to members of the company, that is, the shareholders, but only so far as to allow them to exercise proper control over the company; enabling the shareholders collectively to question the past management of the company, vote for or against the appointment of directors and take other decisions affecting the company. This duty did not extend to members as individuals, even when they used the accounts as the basis for purchasing more shares in the company, and it certainly did not extend to potential outside purchasers of shares. The onus was clearly on the appellants in these circumstances to make their own independent enquiries as it was unreasonable to rely on the auditors.

However, in *Morgan Crucible Co plc* v *Hill Samuel Bank Ltd* (1991), it was held that, where express representations are made about the accounts and the financial state of the company by directors or financial advisers of that company, with the intention that the person interested in the takeover will rely on them, then a duty of care is owed, and the auditor will be responsible for consequential losses. This was also the situation in *ADT* v *BDO Binder Hamilton* (1995) where a partner in the defendant accountancy firm told the plaintiff company that he stood by the audited accounts of BSG, the company that the ADT were in the process of taking over. This was taken as an assumption of responsibility and as the accounts had been prepared negligently, Binder Hamilton were held libel to repay the amount that ADT had overpaid for BSG a total of £65 million.

Following *Caparo Industries plc* v *Dickman* (1990) it can be stated that a company's auditors certainly do owe a duty of care to shareholders collectively as a body to allow them to exercise proper control over the management of the company.

As regards members individually, then again following *Caparo*, normally the auditors do not owe them a duty of care, even when they use the information supplied to purchase more shares in the company.

Following from the foregoing it can be seen that auditors owe no duty of care to non-members unless they actually assume responsibility for the accuracy of information they supply (*Morgan Crucible Co plc* v *Hill Samuel Bank Ltd* (1991) and *ADT* v *BDO Binder Hamilton* (1995)).

5 This question requires candidates to explain the concept of limited liability and to consider three alternative categories of companies; the first unlimited in nature, whilst the second and third are limited in different ways.

(a) In this context, liability refers to the extent to which shareholders in companies are responsible for the debts of their companies and limited liability indicates that a limit has been placed on such liability. The point is that the limitation on liability is enjoyed by the member shareholders rather than the company. One of the major advantages of forming a company is that the members of the company may achieve limited liability. The great majority of registered companies are limited liability companies. This means that the maximum liability of shareholders is fixed and cannot be increased without their agreement. As will be seen below there are two ways of establishing limited liability.

(b) Section 3 of the Companies Act (CA) 2006 sets out the various types of companies that can be registered in term of different liabilities.

(i) Companies can be formed without limited liability. These, by virtue of s.3(4) CA 2006, are referred to as unlimited companies. Such companies are incorporated under the Companies Acts and receive all the benefits that flow from incorporation except limited liability. Consequently the shareholders in such unlimited companies remain liable to the full extent of their personal wealth for any unpaid debt of the company. It should be noted that, in line with the doctrine of separate personality, even in the case of unlimited companies any subsequent debt is owed to the company and not directly to the creditors of the company. The compensating benefit enjoyed by such companies is that they do not have to submit their accounts and make them available for public inspection.

(ii) The company limited by guarantee (s.3(3) CA 2006) is usually restricted to non-trading enterprises such as charities and professional and educational bodies. It limits the shareholders' liability to an agreed amount which is only called on if the company cannot pay its debts on being wound up. In reality, the sum guaranteed is usually a nominal sum, so no real risk is involved on the part of the guarantor.

(iii) The more common procedure is to limit liability by reference to shares (s.33(2)). The effect of this is to limit liability to the amount remaining unpaid on shares held (Insolvency Act 1986 s.74(2)(d)). If the shareholder has paid the full nominal value of the shares to the company, then that is the end of responsibility with regard to company debts. Consequently, if the company should subsequently go into insolvent liquidation the shareholders cannot be required to contribute to its assets in order to pay off its outstanding debts.

6 This question requires candidates to explain the meaning of the terms 'compulsory winding up' and 'administration'.

(a) Winding up, or liquidation, is the process whereby the life of the company is terminated. It is the formal and strictly regulated procedure whereby the business is brought to an end and the company's assets are realised and distributed to its creditors and members. The procedure is governed by the Insolvency Act (IA)1986 and may be divided into three distinct categories:

Member's voluntary winding up,
Creditors' voluntary winding up,
Compulsory winding up.

This question requires attention to be focused on the last of these three. A compulsory winding up is a winding up ordered by the court under s.122 of the IA 1986. Although there are seven distinct grounds for such a winding up, the most common reason for the winding up of a company is its inability to pay its debts. Section 123 provides that, if a company with a debt exceeding £750 fails to pay it within three weeks of receiving a written demand, then it is deemed unable to pay its debts.

On the presentation of a petition to wind a company up compulsorily, the court will normally appoint the Official Receiver to be the company's provisional liquidator. The Official Receiver will require the present or past officers, or indeed employees of the company to prepare a statement of the company's affairs. This statement must reveal:

- particulars of the company's assets and liabilities;
- names and addresses of its creditors;
- any securities held by the creditors (fixed or floating charges) and the dates on which they were granted;
- any other information which the Official Receiver may require.

After his appointment, the Official Receiver calls meetings of the company's members and creditors in order to select a liquidator to replace him and to select a liquidation committee if required. Once again, in the event of disagreement, the choice of the creditors prevails.

Section 142 of the IA 1986 states that the functions of the liquidator are 'to secure that the assets of the company are got in, realised and distributed to the company's creditors and, if there is a surplus, to the persons entitled to it'. Once the liquidator has performed these functions, he must call a final meeting of the creditors, at which he gives an account of the liquidation and secures his release from the creditors. Notice of the final meeting has to be submitted to the registrar of companies and, three months after that date, the company is deemed to be dissolved.

(b) Administration, on the other hand is a means of safeguarding the continued existence of business enterprises in financial difficulties, rather than merely ensuring the payment of creditors. Administration was first introduced in the Insolvency Act 1986. The aim of the administration order is to save the company, or at least the business, as a going concern by taking control of the company out of the hands of its directors and placing it in the hands of an administrator. Alternatively, the procedure is aimed at maximising the realised value of the business assets.

Once an administration order has been issued, it is no longer possible to commence winding up proceedings against the company or enforce charges, retention of title clauses or even hire-purchase agreements against the company. This major advantage was in no small way undermined by the fact that, under the previous regime, an administration order could not be made after a company has begun the liquidation process. Since companies are required to inform any person who is entitled to appoint a receiver of the fact that the company is applying for an administration order, it was open to any secured creditor to enforce their rights and to forestall the administration procedure. This would cause the secured creditor no harm, since their debt would more than likely be covered by the security, but it could well lead to the end of the company as a going concern.

The Enterprise Act 2002 introduced a new scheme, which limited the powers of floating charge holders to appoint administrative receivers, whose function had been essentially to secure the interest of the floating charge holder who had appointed them, rather than the interests of the general creditors. By virtue of the Enterprise Act 2002, which amends the previous provisions of the Insolvency Act 1986, floating charge holders no longer have the right to appoint administrative receivers, but must now make use of the administration procedure as provided in that Act. As compensation for this loss of power the holders of floating charges are given the right to appoint the administrator of their choice.

The function of the administrator is to:

– Rescue the company as a going concern, or
– Achieve a better result for the company's creditors as a *whole* than would be likely if the company were to be wound up, or
– Realise the value of the property in order to make a distribution to the secured or preferential creditors.

The administrator is only permitted to pursue the third option where:

– He thinks it is not reasonably practicable to rescue the company as a going concern, and
– Where he thinks that he cannot achieve a better result for the creditors as a whole than would be likely if the company were to be wound up, and
– If he does not unnecessarily harm the interests of the creditors of the company as a whole.

An application to the court for an administration order may be made by a company, the directors of a company, or any of its creditors, but in addition the Enterprise Act allows the appointment of an administrator without the need to apply to the court for approval. Such 'out of court' applications can be made by the company or its directors, but may also be made by any floating charge holder.

During the administration process the administrator has the powers to:

– do anything necessary for the management of the company
– remove or appoint directors
– pay out monies to secured or preferential creditors *without the need to seek the approval of the court*
– pay out monies to unsecured creditors *with the approval of the court*
– take custody of all property belonging to the company
– dispose of company property. This power includes property which is subject to both fixed and floating charges, which may be disposed of without the consent of the charge holder, although they retain first call against any money realised by such a sale.

The administration period is usually 12 months, although this may be extended by six months with the approval of the creditors, or longer with the approval of the court. When the administrator concludes that the purpose of their appointment has been achieved, a notice to this effect is sent to the creditors, the court and the companies registry. Such a notice terminates the administrator's appointment. If the administrator forms the opinion that none of the purposes of the administration can be achieved, the court should be informed and it will consider ending the appointment. Creditors can always challenge the actions of the administrator through the courts.

7 **(a)** Although a contract of employment need not be in writing, the employer must provide the employee with particulars of the main terms of the contract in writing as required by the Employment Rights Act 1996. Such express terms are agreed upon by the employer and employee on entering into the contract of employment. However, in the absence of stated terms the law will impose duties on both employer and employee. Such implied terms have to be read subject to any express terms to the contrary. Although where the implied term is necessary to give efficacy to the contract, the implied term will take precedence over the express term (*Johnstone* v *Bloomsbury Health Authority* (1991)).

Duties of the employer

(i) *To provide work*

The employer normally will be expected to provide work for the employee and where the employee is skilled and needs practice to maintain those skills, there may be an obligation to provide a reasonable amount of work *Langston* v *Amalgamated Union of Engineering Workers* (1974). No breach of this implied duty will occur so long as the employee continues to be paid even though there may be no work available.

(ii) *To pay wages*

Normally the rate of pay is expressly stated in the contract of employment. However, in the absence of an express provision, the law will impose the duty to pay a reasonable remuneration for the work done. Following from (i) above, an employer must pay employees their wages even if there is no work available, although an express term to the contrary may be included in the contract of employment. Where workers, in the pursuit of an industrial dispute, offer only part performance by working to rule or adopting a 'go-slow' policy, the employer can refuse to accept such part performance and can refuse to make any payment for work done.

(iii) *To indemnify the employee*

Where the employee in the course of his or her employment incurs any legal liability or necessary expenses on behalf of the employer, the employee is entitled to be indemnified or reimbursed.

(iv) *Mutual respect*

The employment relationship is assumed to be based on mutuality of respect, trust and confidence and the employer must not act in a way calculated to damage such mutuality. As will be seen this is a reciprocal relationship, but it is clear that employers cannot treat their employees in an abusive manner (*Isle of Wight Tourist Board* v *Coombes* (1976)) and must be prepared to address any grievances they might have (*WA Goold (Pearmak) Ltd* v *McConnell* & *Another* (1995)).

(v) *To provide a safe system of work*

At common law the employer is required to take reasonable care for the health and safety of his employees. Failure to comply will render the employer liable for an action in negligence. The duty extends to the provision of competent fellow employees, safe plant and equipment, a safe place of work and a safe system of work. If the employer has taken all reasonable steps to comply with the duty of care then they will not be liable for any injury sustained (*Latimer* v *AEC Ltd* (1953)).

(b) There are a number of implied duties imposed on employees, which may all be understood as deriving from their relationship of trust and confidence with their employer and the consequential duty of loyalty and faithful service that derives from that relationship. The specific duties may be cited as:

(i) *to act faithfully*

This is the fundamental duty and it covers such aspects of confidentially, i.e. not passing on information derived from one's employment to outsiders and not competing with the employer either directly or indirectly.

The courts are reluctant to accept that what workers do in their spare time should be of any concern to their employer (*Nova Plastics Ltd* v *Froggett* (1982)). However, sometimes an employer's interests may be harmed by an employee's spare-time work if this involved direct competition with the employer's business (*Hivac Ltd* v *Park Royal Scientific Instruments Ltd* (1946)).

An employee may not do anything while still employed, which is in breach of the duty to act faithfully. However, it is perfectly lawful for ex-employees to canvass customers of their former employer after leaving service. Moreover, they are entitled to make use of any knowledge and skills acquired while in the former employer's business, apart from such information which can be classified as a trade secret. In this sense the implied duty of confidentiality for ex-employees is narrower than in the case of an existing employee (*Faccenda Chicken Ltd* v *Fowler* (1986)).

(ii) *to obey reasonable orders*

Employees must obey any reasonable and lawful instruction given to them by their employer. Whether any instruction fulfils these criteria is a matter of fact in each instance. The classic case in this area is *Pepper* v *Webb* (1969) in which a gardener not only indicated that he was not willing to follow an instruction but actually swore at his employer. In a subsequent action it was held that as the order was both lawful and reasonable the gardener had breached his implied duty.

(iii) *to use skill and care*

Should an employee not exercise the level of skill and care that may reasonably be expected, then they will not only be liable to dismissal, but they may also lose the protection of the employer's duty to indemnify them for losses (see part (a) above), and be made personally liable for claims for compensation. The classic case in this instance is *Lister* v *Romford Ice and Cold Storage Ltd* (1957) in which an employee lorry driver, rather than his employer, was held liable to compensate a fellow worker, due to his gross negligence in driving his lorry, which was held to breach his implied duty of skill and care.

(iv) *not to take bribes or make a secret profit*

This duty almost goes without saying, as an example of the general duty of good faith, but it covers the situation where an employee has received money or gifts from customers or clients. In this instance the classic case is *Boston Deep Sea Fishing Ice Co* v *Ansell* (1888) in which a managing director of a company was held to have been properly dismissed for having taken money as commission from the company's suppliers for orders he placed with them.

8 Given that the question scenario clearly states that the exclusion clause was incorporated into the contract between Andy and Bash Ltd (and there can be no doubt that it is), it is only necessary to consider the effect of the clause. On the basis of the clear wording, it would appear that the wording of the exclusion clause is sufficiently clear and specific to cover Bash Ltd's negligence. As a consequence, it only remains to consider how the legislation governing exclusion clauses would be likely to deal with this particular clause in the context of the question.

The Unfair Contract Terms Act 1977 (UCTA) is the original statutory attempt to control exclusion clauses. The original Unfair Terms in Consumer Contracts Regulations (UTCCR) were enacted in 1994 to implement the European Unfair Contract Terms Directive and were subsequently replaced by the current regulations in 1999.

Section 2(1) of UCTA provides an absolute prohibition on exemption clauses in relation to liability in negligence resulting in death or injury. It is therefore apparent that Bash Ltd cannot avoid responsibility for the injury sustained by Andy and will be liable for the injuries and the consequential loss he suffered.

Section 2 also provides that any exemption clauses relating to liability for other damage caused by negligence will only be enforced to the extent that they satisfy the 'requirement of reasonableness'; and s.11 provides that the requirement of reasonableness means 'fair and reasonable … having regard to the circumstances …'.

In looking at the circumstances of the case the court will take into account matters relating to the relative strength of bargaining power: inducements to accept the restrictions: whether the customer knew or ought to have known of the exclusion: whether the goods involved were specially made or adapted. The final outcome, therefore, is dependent on judicial interpretation. The onus of showing reasonableness rests with the party relying on the clause (*St Alban's CDC* v *International Computers Ltd* (1994)). If one were to ask the question: 'Was it reasonable for Bash Ltd to deny responsibility for the consequence of their negligence in this case?' the answer is likely to be no. Consequently Bash Ltd is likely to be liable for all the damages consequent upon its vicarious negligence, and the exclusion clause to have no effect (see *George Mitchell* (*Chesterhall*) *Ltd* v *Finney Lock Seeds Ltd* (1983) and *Smith* v *Bush* (1989)).

Although the Unfair Terms in Consumer Contracts Regulations 1999 do not affect the outcome of the situation in any material way, it is worth mentioning them at this point. The regulations are potentially wider in scope than UCTA, in that they cover all terms and not just exclusion clauses. Regulation 3(1) states that it applies to 'any term in a contract concluded between a seller or supplier and a consumer where the term has not been individually negotiated'. Under regulation 4(i), a term is unfair 'if contrary to the requirements of good faith, it causes a significant imbalance in the parties' rights and obligations arising under the contract to the detriment of the consumer'. Consequently reg.5(1) provides that if a term is found to be unfair it will not be binding on the consumer, although the remainder of the contract will continue to operate if it can do so after the excision of the unfair term.

9 This question requires candidates to analyse a problem scenario and explain and apply the law relating to directors' contracts with their companies.

As a consequence of the position they hold, company directors owe fiduciary duties to their companies. One such duty is *the duty not to permit a conflict of interest and duty to arise*. This equitable rule is strictly applied by the courts and the effect of its operations may be seen in *Regal (Hastings)* v *Gulliver* (1942). In that case, the directors of a company owning one cinema provided money for the creation of a subsidiary company to purchase two other cinemas. After the parent and subsidiary companies had been sold at a later date, the directors were required to repay the profit they had made on the sale of their shares in the subsidiary company on the grounds that they had only been in the situation to make that profit because of their positions as directors of the parent company. It is not necessary to prove an actual conflict of interest, merely the possibility of such a conflict, and the rigorous nature of this principle may be seen in *Boardman* v *Phipps* (1967).

One obvious area where directors place themselves in a position involving a conflict of interest is where they have an interest in a contract with the company. The common law position was that in the event of any such situation arising, any contract involved was voidable at the instance of the company (*Aberdeen Rly Co* v *Blaikie* (1854)). However, s.182 of the Companies Act 2006 places a duty on directors to declare any interest, direct or indirect, in any contracts with their companies, and provides for a fine if they fail in this regard. A director's disclosure can take the form of a general declaration of interest in a particular company, which is considered sufficient to put the other directors on notice for the future. Any declaration of interest must be made at the board meeting that first considers the contract, or if the director becomes interested in the contract after that, at the first meeting thereafter. Failure to disclose any interest renders the contract voidable at the instance of the company and the director may be liable to account to the company for any profit made in relation to it.

Applying the above to the problem scenario, it appears that Caz did not declare her interest in either Era Ltd generally, or the particular contract in question. Dull plc could have avoided the contract had they found out earlier and acted sooner, but in any case Caz can be held liable to account to Dull plc for any profit she made on the deal. Caz will also be liable to prosecution and a fine under s.183 of the Companies Act 2006, which criminalises any failure to comply with the requirements of s.182.

10 This question requires candidates to consider fraudulent trading both under s.993 of the Companies Act 2006 and s.213 of the Insolvency Act 1986, and wrongful trading under s.214 of the Insolvency Act 1986.

(a) There has long been civil liability for any activity amounting to fraudulent trading. Thus, s.213 of the Insolvency Act (IA) 1986 governs situations where, in the course of a winding up, it appears that the business of a company has been carried on with intent to defraud creditors, or for any fraudulent purpose. In such cases, the court, on the application of the liquidator, may declare that any persons who were knowingly parties to such carrying on of the business are liable to make such contributions (if any) to the company's assets as the court thinks proper. There is a major problem in making use of s.213, however, and that lies in meeting the very high burden of proof involved in proving dishonesty on the part of the person against whom it is alleged. It should be noted that there is also a criminal offence of fraudulent trading under s.993 of the Companies Act 2006, which applies to anyone who has been party to the carrying on of the business of a company with intent to defraud creditors or any other person, or for any other fraudulent purpose.

Given that it is stated that Gram and Hen hid the fact that Ire Ltd was insolvent it is possible that they might be liable under the fraudulent trading provisions both civil and criminal. As a consequence they may well be liable for a maximum prison sentence of 10 years and may have to contribute to the assets of the company to cover any loss sustained by creditors as a result of their actions. There is no evidence to support either action against Fran.

(b) Wrongful trading does not involve dishonesty but, nonetheless, it still makes particular individuals potentially liable for the debts of their companies. Section 214 applies where a company is being wound up and it appears that, at some time before the start of the winding up, a director knew, or ought to have known, that there was no reasonable chance of the company avoiding insolvent liquidation. In such circumstances, then, unless the directors took every reasonable step to minimise the potential loss to the company's creditors, they may be liable to contribute such money to the assets of the company as the court thinks proper. In deciding what directors ought to have known, the court will apply an objective test, as well as a subjective one. As in common law, if the director is particularly well qualified, they will be expected to perform in line with those standards. Additionally, however, s.214 of the IA 1986 establishes a minimum standard by applying an objective test which requires directors to have the general knowledge, skill and experience, which may reasonably be expected of a person carrying out the same functions as are carried out by that director in relation to the company.

The manner in which incompetent directors will become liable to contribute to the assets of their companies was shown in *Re Produce Marketing Consortium Ltd* (1989), in which two directors were held liable to pay compensation from the time that they ought to have known that their company could not avoid insolvent liquidation, rather than the later time when they actually realised that fact. Interestingly, the common law approach to directors' duty of care has been extended to accommodate the requirements of s.214 (*Re D'Jan of London Ltd* (1993)).

It is clearly apparent that both Gram and Hen will be personally liable under s.214 for the increase in Ire Ltd's debts from £10,000 to £100,000. However, as a director of the company Fran will also be liable to contribute to the assets of the company under s.214.

1 This question requires candidates to consider the powers of judges to interpret legislation and the rules they apply in exercising such interpretative powers. Although the question requires answers to focus on the two main general approaches, it also requires an explanation of the various traditional rules of statutory interpretation employed by the courts.

(a) requires a consideration of the literal approach, including the golden rule.

3–5 marks	Full detailed explanation with supporting cases or examples.
1–2 marks	Limited knowledge of the topic; perhaps lacking detail or cases/examples.
0 mark	No knowledge on the topic under consideration.

(b) requires a consideration of the purposive approach, including the mischief rule.

3–5 marks	Full detailed explanation with supporting cases or examples.
1–2 marks	Limited knowledge of the topic; perhaps lacking detail or cases/examples.
0 mark	No knowledge on the topic under consideration.

Candidates may simply produce a global answer considering the traditional rules and will be marked according to the content provided.

2 This question is divided into two parts relating to distinct aspects of the law of contract.

(a)	4–5 marks	A good to excellent understanding of the postal rule demonstrated by references to cases or examples.
	2–3 marks	Some, but limited, understanding of the topic, or clear understanding of only one aspect.
	0–1 mark	Little or no knowledge of the topic.
(b)	4–5 marks	A good to excellent understanding of privity demonstrated by references to cases or examples.
	2–3 marks	Some, but limited, understanding of the topic, or clear understanding of only one aspect.
	0–1 mark	Little or no knowledge of the topic.

3 This question requires an explanation of two aspects the law relating to damages for breach of contract. It is split into two parts with 7 marks being available for part (a) and 3 marks for part (b).

(a)	5–7 marks	A good explanation of the difference between liquidated damages and penalty clauses with perhaps some examples or cases.
	3–4 marks	Some, but limited, understanding of the topic, or clear understanding of only one aspect.
	0–2 marks	Little knowledge of either element of the question or unbalanced in only dealing with one of the elements.
(b)	2–3 marks	A thorough explanation of the duty the duty to mitigate losses with examples or cases.
	0–1 mark	Some, if little, knowledge of the duty but not clear or lacking in detail.

4 This question requires candidates to explain the extent of a company auditor's duty of care and to whom such a duty is owed.

8–10 marks	A thorough understanding of how professional negligence applies to auditors demonstrated by references to cases or examples.
5–7 marks	A clear understanding of the topic, perhaps lacking in detail. Alternatively an unbalanced answer showing good understanding of one part but less in the others.
2–4 marks	Some, but limited, understanding of the topic, or clear understanding of only one aspect.
0–1 mark	Little or no knowledge of the topic.

5 This question is likely to be answered in a global way and marks will be awarded inline with points made.

(a) Up to 3 marks for a general explanation of limited liability.

(b) **(i)** Up to 2 marks for an explanation of unlimited liability and why it might be used.

(ii) Up to 2 marks for knowledge of companies limited by guarantee. What they are, where they are used and the nature of liability.

(iii) Up to 3 marks for a thorough explanation of liability limited by reference to the amount unpaid on shares and how it operates.

6 This question, in two parts, carrying 4 marks for part (a) and 6 marks for part (b), requires candidates to explain the meaning of the terms 'compulsory winding up' and 'administration'.

(a)	3–4 marks	A good explanation of the meaning and effect of winding up generally and compulsory winding up in particular.
	0–2 marks	Some, if little knowledge of winding up, or perhaps too general or unbalanced in not dealing specifically with compulsory winding up.
(b)	4–6 marks	A good explanation of the meaning and effect of administration generally and contrasting its purpose with that of compulsory winding up.
	2–3 marks	Some, if little, explanation of administration, but perhaps too general or lacking in detail.
	0–1 mark	Little or no knowledge of the topic.

7 This question requires an explanation of the common law duties owed by both employers and employees.

(a)	5–6 marks	Good awareness of the implied duties imposed on employers. Examples used to highlight answers.
	3–4 marks	Sound understanding but perhaps no examples.
	0–2 marks	Limited knowledge only about the topic.
(b)	3–4 marks	Good awareness of the implied duties imposed on employees.
	0–2 marks	Limited knowledge about the topic.

8 This question requires candidates to apply the law realting to exclusion clauses to a specific problem scenario. Marks will be awarded for both knowledge and application, but application is essential.

8–10 marks	The best candidates should provide a clear understanding of the legal control of exclusion clauses and be able to apply the law. Some detailed reference should be made to the provisions of the Unfair Contract Terms Act (UCTA) 1997 and the very best answers will at least mention the Unfair Terms in Consumer Contracts Regulations 1999. Cases or examples should be used to demonstrate points made.
5–7 marks	Weaker candidates may show little detailed knowledge of the legislation but be able to consider the UCTA generally.
3–4 marks	Some but limited knowledge of the appropriate law or lacking in application.
0–2 marks	The poorest candidates will provide nothing but the briefest reference to the legislation.

9 This question requires candidates to analyse a problem scenario and explain and apply the law relating to directors' contracts with their companies.

8–10 marks	A good analysis of the scenario with a clear explanation of the law relating to contracts between directors and their companies, both at common law and under statute. Cases and/or references to the Companies Act will be provided.
5–7 marks	Some understanding of the situation but perhaps lacking in detail or reference to the statute.
3–4 marks	Weak answer lacking in knowledge or application, with little or no reference to the Companies Act.
0–2 marks	Little if any knowledge of the appropriate legal principles.

10 This question requires candidates to consider fraudulent trading both under s.993 of the Companies act 2006 and s.213 of the Insolvency Act 1986, and wrongful trading under s.214 of the Insolvency Act 1986.

(a) 4–5 marks Clear explanation of operation of the law relating to fraudulent trading, under both criminal and civil law, but with the emphasis on the Insolvency Act provisions.

2–3 marks Some to good understanding but lacking detail.

0–1 mark Little or no knowledge.

(b) 4–5 marks Clear explanation of the law relating to wrongful trading, probably, but not necessarily referring to case law.

2–3 marks Some to fair understanding but lacking detail.

0–1 mark Little if any knowledge.