Law Society of Scotland

THE LAW SOCIETY OF SCOTLAND EXAMINATIONS

BUSINESS ORGANISATIONS

Friday 11 August 2017

1330 – 1530
(Two Hours)

Candidates should answer any THREE questions. Give authority for all answers.

Each question has 100 marks.

LAW SOCIETY OF SCOTLAND
EXAMINATIONS

BUSINESS ORGANISATIONS

Friday 11 August 2017
(Two hours)

Candidates should answer THREE questions. Please ensure you use appropriate authority for your answers.

Question 1

Beth acts as the agent for a wealthy socialite, Cathy. It is Beth's job to organise grand parties, arrange travel, book accommodation and other tasks for Cathy. Beth is careful not to be Cathy's employee, since she wishes to have the freedom to work for other people if she wishes. Cathy is too busy and trusting to check up on Beth's activities. Beth has not asked for a contract of agency and Cathy has not offered one. Cathy merely pays Beth on a flat rate per hour, depending on the number of hours Beth has been working for her.

Cathy wishes to have a party for her infant daughter. Beth is told to organise a one-man band, catering, and goodie-bags for well-behaved children. Beth asks her brother, an entertainer, to be the one-man band. Cathy invites her old friend, Alice, who runs a catering business, to do the catering, for the good reason that Alice will give Beth a commission of 5% of the contract price. As for the goodie-bags, Beth supplies these herself for a fair price, which Cathy pays without question.

Cathy's husband is interested in modern pottery. He wants to commission a potter to make an urn to fill a particular spot in his garden, but he knows that if he does this, the potter, knowing of Cathy's wealth, will put up his fee. The husband asks Beth to approach the potter without revealing his interest. Beth duly commissions the potter to produce the artefact, and keeps quiet about Cathy's husband's involvement. The urn is so carefully designed that it would only work within Cathy's husband's garden and in no other place. The potter completes the urn and is waiting to hand it over.

Beth is asked to arrange for the valuation of some of Cathy's jewels for insurance purposes. Beth takes the jewels to a well-known jeweller's. The valuer, who is the owner of the jeweller's, takes the jewels for a couple of days to value them. He then produces a certificate for the benefit of the insurers and returns the jewels to Beth. Beth checks that the valuer has handed over the correct number of items, but fails to notice that the valuer has substituted some of the precious stones with fakes. Beth returns the jewels to Cathy. Meanwhile, the jeweller's closes down at short notice. The valuer has fled abroad with all his stock, including Cathy's stones.

Shortly afterwards, Beth has a row with her boyfriend, who had been behaving badly. She throws him out of the house. In retaliation, he writes to Cathy telling her that Beth is not quite as Cathy might think. Cathy discovers about the party arrangements. She checks the jewels and finds that they are fake. On top of that, Cathy's husband, having invested unwisely in a cloud-founded project, finds himself bankrupt and unable to pay the potter. Meanwhile, Beth insists on her rights under the Commercial Agents (Council Directive) Regulations 1993.

Explain the law relating to these matters.

Question 2

In June 2015 Alpha Ltd, a company registered in Scotland, bought a warehouse in an industrial development zone. To acquire the warehouse the Bank of Falkirk lent Alpha Ltd some of the purchase price, its loan being secured by a standard security over the warehouse. The disposition and standard security over the warehouse were registered in the Land Register on the same day, and in due course the standard security was also properly registered at the Register of Companies.

Alpha Ltd started to make a new brand of robot lawnmowers in its warehouse. The robots proved successful, but the costs of production were high. Alpha Ltd needed to borrow more money. The Bank of Falkirk agreed to take a floating charge over Alpha Ltd's assets and undertaking. The floating charge contained a negative pledge prohibiting Alpha Ltd from granting any further charge ranking ahead of the Bank of Falkirk's floating charge. The floating charge was registered at the Registrar of Companies in May 2016.

In August 2016 Alpha Ltd is approached by Beta Ltd which indicates that it is willing to provide a short-term loan to Alpha Ltd provided it is given a floating charge as security for the loan. The directors of Alpha Ltd indicate that this charge would have to be postponed to the Bank of Falkirk's charge. Beta Ltd is happy to accept this. The loan is made and the floating charge documentation prepared in-house by the in-house lawyer at Beta Ltd. Unfortunately he is severely injured while on business abroad and is unable to register the floating charge within the required time limit. He remains ill abroad, too poorly to be moved back to the UK and not in a position to communicate clearly, at least for the time being. The charge remains unregistered.

The wife of the managing director of Alpha Ltd also decided to help Alpha Ltd and agreed to pay a debt of £25,000 payable by Alpha Ltd to a supplier. In return she obtained a floating charge over Alpha Ltd's assets and undertaking. This was both properly registered and intimated to the Bank of Falkirk in June 2017.

Alpha Ltd then suffered an unfortunate court case. One of the robot lawnmowers severely injured a child – whose injuries were fortunately covered by insurance. This attracted damaging publicity and demand for Alpha Ltd's products immediately ceased. Alpha was swiftly put into liquidation in September 2017.

The liquidator discovered that Alpha Ltd at the time of liquidation owed about £1,000 to each employee. A small group of ordinary creditors were owed a little money, but the main creditor was the HMRC. The wife of the managing director put in a claim for £50,000. Some of the robots had been delivered to a distributor who in turn was to deliver them to various purchasers, in particular golf clubs and football stadiums. Alpha Ltd's directors were aware that the ultimate purchasers had paid the distributor but that the distributor had not paid

Alpha Ltd for the robots. The warehouse turned out to be more valuable than expected and it is likely that while there is insufficient to repay all creditors, most will get something.

Advise the liquidator on the distribution of the estate and the ranking of the various creditors. You may assume that liquidator decided against making any claims against the directors. You are not expected to produce any calculations.

Question 3

Jim, Angie, Pran and Faisal operate a domestic letting agency in partnership together. Jim checks the domestic flats that they let out for their clients, and deal with emergency repairs. Angie is good at the paperwork. Pran is good at dealing with the landlords and tenants. Faisal is good at the accounts. They share the profits equally, and they each have a one-quarter share in the management of the partnership. They make a point of not incorporating in order to give their clients confidence in their management of their own business. They have a partnership agreement. Amongst other things it states that Jim must never instruct emergency repairs or other disbursements without consulting the other partners. This is because Jim is known to be so keen to do a good job in a hurry that he does not always stop to take account of any wider considerations. Even he agrees that this is a sensible provision in the partnership agreement. The partnership agreement has no provisions for the dissolution of the partnership.

One day, Jim receives a call saying that a pipe is apparently leaking from one of the managed flats into the flat below. Unable to see the leak in the managed flat, he goes to the flat below and sees that there is indeed water coming through the ceiling. The occupier is very upset. Jim immediately summons an emergency plumber at considerable expense to go to the managed flat. The plumber establishes that there is no leak from the managed flat and that the problem is with the pipework in the flat below. The plumber sends in his invoice in due course. Faisal says that they should not pay it and that it is the problem of the downstairs flat-owner. He also says that Jim was not authorised to instruct the plumber and so the agency does not need to pay the invoice.

Although on the whole the agency is quite profitable, it can be a bit seasonal. During the summer months, there is less demand for flats as students and others go away. During one of these lull periods the agency appears to have a short-term cash-flow problem. Angie's mum says that she will lend the agency a sum of money to tide it over, but she wants the loan to be repaid in monthly tranches starting in six months' time, with the interest rate being calculated according to the level of profitability of the agency at the time of the repayment – all as carefully worked out in a formula agreed by her and the partnership.

Pran is approached by one of the landlords who is impressed by Pran's good way with people.He asks Pran if he would be willing to negotiate a rent review with one of his commercial clients. As already indicated, the agency only does domestic letting, not commercial letting. Pran does not think that there would be any difficulty with this.

Faisal is going through the books, as he does every Friday. He notices some suspicious transactions. He thinks Angie's expenses are either inflated or bogus. He summons a meeting of the partnership, and indicates that they should have a vote there and then to expel her from the partnership. She says that in the absence of any term to allow this in the partnership agreement, they may not vote to expel her.

The plumber is fed up at not being paid. He instructs solicitors to sue the partnership, and includes Angie's mum as one of the liable partners.

Explain the law relating to these various circumstances.

Question 4

Bingo Ltd, a family company, growing apples and pears for making fruit juice, cider and perry, is run by three directors, and has ten shareholders. The directors collectively own 60% of the shares.

As the company has been profitable to date, none of the non-directorial shareholders has been paying much attention to the company's activities nor to the directors' management of the company. However, one of the shareholders, Tam, having retired from his former employment, now has time to devote to the family company. He is not impressed by what he discovers. As far as he can see, the two remaining directors always support whatever the managing director says, and there is no evidence of reasoned discussion as to future strategies or developments. Because there is a reasonably constant demand for fruit juice cider and perry, the company has continued to produce apples and pears, without considering the fact that the trees are getting near the end of their productive lives, that there are new roads being built near the orchards which may affect the quality of the fruit, and that consumers' tastes may change. Tam is also worried that the company is not paying its fruit-pickers a reasonable wage and that as a result the quality of the picking will decrease. If that happens the quality of the company's products will go down. Tam notices that Bingo Ltd used to have excellent relations with the local community, not least because it used to donate some casks of cider to the local village fête. This practice has recently ceased, and Tam wonders if this may impinge on the company's standing in the community. Al these matters, he contends, may ultimately affect the value of his shares and the dividends he receives.

Tam does not wish to sell his shares. In terms of company law, what may he do to improve matters? What difficulties may he face in trying to do so?

Question 5

(a) When a company (private or public) reduces its capital, the process can either be very complex and expensive, or relatively simple. In this time of economic crisis, explain why some companies might wish to reduce their capital, how both public and private companies would go about doing so, and what advantages and disadvantages there would be in doing so.

.

(b) Explain why a company might wish to undertake a scheme of arrangement, how a company might do so, and what factors the company would need to take account of in order to ensure that the scheme is approved by the court.

N.B. These questions require more than a mere recitation of the legislation.

Question 6

(a) Taking account of the existing case law on the matter, explain the requirements of s.123(1)(e) of the Insolvency Act 1986, which refers to the inability of the company to pay its debts as they fall due.

(b) A liquidator or administrator of a company may consider that a director of a company that has become insolvent should be required to contribute to the company's assets if his or her actions in running the company in the period leading up to the company's insolvency amounted to wrongful trading in terms of s.214 of the Insolvency Act 1986. Explain what factors the courts will take into account when deciding whether or not a director should be required to make such a contribution.

Question 7

To what extent is the leading case, *Prest* v *Petrodel Resources Ltd* [2013] 2 A.C. 415, a shield that protects directors, and indeed members, from the consequences of their own sometimes discreditable behaviour?

END OF QUESTION PAPER