Answers

1 (a) (i) Criminal law relates to conduct which the State considers with disapproval and which it seeks to control. Criminal law involves the *enforcement* of particular forms of behaviour, and the State, as the representative of society, acts positively to ensure compliance. Thus, criminal cases are brought by the State in the name of the Crown and cases are reported in the form of *Regina* v … (*Regina* is simply Latin for 'queen' and case references are usually abbreviated to *R* v …). In criminal law the prosecutor prosecutes a defendant (or 'the accused') and is required to prove that the defendant is guilty *beyond reasonable doubt*.

(ii) Civil law on the other hand, is a form of private law and involves the relationships between individual citizens. It is the legal mechanism through which individuals can assert claims against others and have those rights adjudicated and enforced. The purpose of civil law is to settle disputes between individuals and to provide remedies; it is not concerned with punishment as such. The role of the State in relation to civil law is to establish the general framework of legal rules and to provide the legal institutions to operate those rights, but the activation of the civil law is strictly a matter for the individuals concerned. Contract, tort and property law are generally aspects of civil law. Civil cases are referred to by the names of the parties involved in the dispute, for example, *Smith* v *Jones*. In civil law, a claimant sues (or 'brings a claim against') a defendant and the degree of proof is *on the balance of probabilities*.

In distinguishing between criminal and civil actions, it has to be remembered that the same event may give rise to both. For example, where the driver of a car injures someone through their reckless driving, they will be liable to be prosecuted under the Road Traffic legislation, but at the same time, they will also be responsible to the injured party in the civil law relating to the tort of negligence.

(b) The essential criminal trial courts are the *magistrates' courts* and *Crown Courts*. In serious offences, known as *indictable offences*, the defendant is tried by a jury in a Crown Court; for *summary offences*, he is tried by magistrates; and for 'either way' offences, the defendant can be tried by magistrates if they agree, but he may elect for jury trial.

When defendants under 18 are tried by magistrates, the procedure will take place in special *Youth Courts*. There will generally be three justices to hear the case, of whom at least one must be a man and one a woman. These justices will have had special training to deal with such cases. There are also special provisions relating to punishments for this age group.

Criminal appeals from the magistrates go to the Crown Court or to the Queen's Bench Division (QBD) Divisional Court 'by way of case stated' on a point of law or on the ground that the magistrates went beyond their proper powers.

From the Crown Court, appeals against conviction and sentence lie to the Court of Appeal (Criminal Division) with the possibility of an appeal to the House of Lords on a point of law of general public importance.

Magistrates' courts have a significant civil jurisdiction, especially under the Children Act 1989 as 'family proceedings courts'.

County courts
There are about 220 county courts in England and Wales. They are presided over by District Judges and circuit judges. County courts hear small claims, that is, those whose value is £5,000 or under, and fast track cases.

In the High Court the Queens Bench Division deals with contract and tort, etc; its Divisional Court deals with judicial review and criminal appeals from magistrates' courts and Crown Courts. Chancery deals with cases involving land, mortgages, bankruptcy and probate, etc; its Divisional Court hears taxation appeals. The Family Division hears matrimonial and child related matters and its Divisional Court hears appeals from magistrates' courts and county courts on these issues.

The Court of Appeal (Civil Division) usually has three judges whose decision is by majority. For many purposes, it is the de facto final appeal court but on important points of law of general public importance, a final appeal may be made to the House of Lords.

2 This question requires candidates to consider two of the elements required for the creation of a binding contractual agreement.

(a) Privity
As a general rule contractual agreements can only affect those persons who have entered into the agreement expressed in the terms of the contract. Thus, it is normally the case that no third party can rely on, or enforce, any terms in a contractual agreement to which they are not themselves a party (*Dunlop* v *Selfridge* (1915)).

However, it is possible to formally transfer the benefit of a contract to a third party. This process, known as assignment, must be in writing. It should be noted that the burden of a contract cannot be assigned without the consent of the other party to the contract.

It is also possible for a person to 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 (*Les Affreteurs Reunis SA* v *Leopold Walford (London) Ltd* (1919)).

A third party may enforce a contract in the following circumstances:

(i) the beneficiary sues in some other capacity. Although not a party to the original agreement, individuals may, nonetheless, acquire the power to enforce the contract where they are legally appointed to administer the affairs of one of the original parties (*Beswick* v *Beswick* (1967)) where a widow, appointed administratrix of her late husband's estate, was able to successfully sue her nephew for specific performance of a beneficial agreement in that capacity.

(ii) the situation involves a collateral contract. This situation arises where one party promises something to another party if that other party enters into a contract with a third party: e.g. A promises to give B something if B enters into a contract with C. In such a situation B can insist on A complying with the original promise (*Shanklin Pier* v *Detel Products Ltd* (1951)).

(iii) it is foreseeable that damage caused by any breach of contract will cause a loss to a third party (*Linden Gardens Trust Ltd* v *Lenesta Sludge Disposals Ltd* (1994)).

The other main common law exception to the privity rule is agency, where the whole point is for the agent to bring about contractual relations between their principal and a third party.

In the area of motoring insurance Statute law has intervened to permit third parties to claim directly against insurers, but much wider statutory intervention has been introduced by the Contracts (Rights of Third Parties) Act 1999.

(b) Intention to create legal relations

A contract is defined as a binding agreement, however in order to limit the number of cases that might otherwise be brought, the courts will only enforce those agreements which the parties intended to have legal effect. Although expressed in terms of the parties' intentions, the test for the presence of such intention is an objective, rather than a subjective, one. Agreements can be divided into two categories, in which different presumptions apply.

(i) Domestic and social agreements
In these agreements, there is a presumption that the parties do not intend to create legal relations (*Balfour* v *Balfour* (1919)). However, any such presumption against the intention to create legal relations in such relationships may be rebutted by the actual facts and circumstances of a particular case as may be seen in *Merritt* v *Merritt* (1970).

(ii) Commercial agreements
In these situations, the strong presumption is that the parties intend to enter into a legally binding relationship in consequence of their dealings (*Edwards* v *Skyways* (1964)). However, as with other presumptions, this one is also open to rebuttal. In commercial situations, however, the presumption is so strong that it will usually take express wording to the contrary to avoid its operation as may be seen in *Rose and Frank Co* v *Crompton Bros* (1925).

3 Even where someone has been held to owe a duty of care to another person and to have breached that duty in such a way as to cause them to sustain loss or injury it does not follow as a matter of course that the person so responsible will be liable to provide recompense for all the loss sustained. Just as in contract law, the position in negligence is that the person ultimately liable in damages is only responsible to the extent that the loss sustained was considered not to be too remote. This was not always the case as may be seen in *Re Polemis and Furness, Withy and Co* (1921), in which it was held that the defendants were liable for the loss of a ship, even though the circumstances under which it was lost were unforeseen. It was held that as the fire, which destroyed the ship, was the direct result of a breach of duty, the defendant was liable for the full extent of the damage, in spite of the fact that the manner in which it took place was unforeseen. The Court of Appeal held that as damage would result from the act of negligence, the party responsible was liable for the whole extent of the damage, even though they could not have been aware of the extent of the damage that was actually caused.

However, the *Re Polemis* test has been replaced by a less draconian test involving an assessment of the remoteness of the damage actually sustained. The current test was established in *The Wagon Mound (No 1)* (1961). As the facts will demonstrate the way in which the current doctrine operates they will be set out in more detail than is usual. The defendants negligently allowed furnace oil to spill from a ship into Sydney harbour. The oil spread and came to lie beneath a wharf, which was owned by the plaintiffs. The plaintiffs had been carrying out welding operations and, on seeing the oil, they stopped welding in order to ascertain whether it was safe. They were assured that the oil would not catch fire, and so resumed welding. Cotton waste, which had fallen into the oil, caught fire. This in turn ignited the oil and a fire spread to the plaintiff's wharf. It was held that the defendants were in breach of duty. However, they were only liable for the damage caused to the wharf and slipway through the fouling of the oil. They were not liable for the damage caused by fire because damage by fire was at that time unforeseeable. This particular oil had a high ignition point and it could not be foreseen that it would ignite on water. The Privy Council refused to apply the rule in *Re Polemis* and its formulation of the rules of causation and remoteness has prevailed since then.

The test of reasonable foresight arising out of *The Wagon Mound* clearly takes into account such things as scientific knowledge at the time of the negligent act. The question to be asked in determining the extent of liability is, 'is the damage of such a kind as the reasonable man should have foreseen?'. This does not mean that the defendant should have foreseen precisely the sequence or nature of the events. Lord Denning in *Stewart* v *West African Air Terminals* (1964) said:

> 'It is not necessary that the precise concatenation of circumstances should be envisaged. If the consequence was one which was within the general range which any reasonable person might foresee (and was not of an entirely different kind which no one would anticipate), then it is within the rule that a person who has been guilty of negligence is liable for the consequences.'

This is illustrated in the case of *Hughes* v *Lord Advocate* (1963), where employees of the Post Office, who were working down a manhole, left it without a cover but with a tent over it and lamps around it. A child picked up a lamp and went into the tent. He tripped over the lamp, knocking it into the hole. An explosion occurred and the child was burned. The risk of the child being burned by the lamp was foreseeable. However, the vapourisation of the paraffin in the lamp and its ignition were not foreseeable. It was held that the defendants were liable for the injury to the plaintiff. It was foreseeable that the child might be burned and it was immaterial that neither the extent of his injury nor the precise chain of events leading to it was foreseeable.

The test of remoteness is not easy to apply. The cases themselves highlight the uncertainty of the courts. For example, in *Doughty* v *Turner Manufacturing Co Ltd* (1964), an asbestos cover was knocked into a bath of molten metal. This led to a chemical reaction, which was at that time unforeseeable. The molten metal erupted and burned the plaintiff, who was standing nearby. It was held that only burning by splashing was foreseeable and that burning by an unforeseen chemical reaction was not a variant on this. It could be argued that the proper question in this case should have been, 'was burning foreseeable?', as this was the question asked in *Hughes*.

4 Before incorporation, companies are required to submit a memorandum of association to the registrar of companies, which must be signed by at least two subscribers from amongst the company's first shareholders. The memorandum mainly governs the company's external affairs. Amongst the clauses required to be contained in a company's memorandum of association are the following:

(a) The registered office clause
This is the company's legal address. It is the place where legal documents such as writs or summonses can be served on the company. It is also the place where statutory documents and registers, such as the register of members, are required to be kept available for inspection. The memorandum does not state the actual address of the registered office, but only the country within which the company is registered, whether Scotland or England and Wales. The precise location of the registered office however, has to be stated on all business correspondence (s.351).

(b) The authorised share capital clause
This states the maximum amount of share capital that a company is authorised to issue. The authorised capital must be divided into shares of a fixed monetary value and it follows, therefore, that United Kingdom company law does not recognise no-fixed-value shares as do other jurisdictions. As companies do not have to issue shares to the full extent of their authorised capital, it is imperative to distinguish authorised capital from issued capital, which is the amount of shares actually issued. The current minimum value of issued capital in relation to a public limited company is £50,000.

(c) The name clause
Except in relation to specifically exempted companies such as those involved in charitable work, companies are required to indicate that they are operating on the basis of limited liability. Thus private companies are required to end their names either with the word 'limited' or the abbreviation 'ltd'; and public companies must end their names with the words 'public limited company' or the abbreviation 'plc' (CA 1985 ss.25,27 & 30).

The Registrar of Companies will not register any company with a name that is the same as one already on the index of business names index (CA 1985 s.26(c)). Certain categories of names are, subject to the decision of the Secretary of State, unacceptable *per se*, as follows:

(i) names which in the opinion of the Secretary of State constitute a criminal offence (s.26(1)(e)).
(ii) names which in the opinion of the Secretary of State are offensive (s.26(1)(e)).
(iii) names which are likely to give the impression that the company is connected with either government or local government authorities (s.26(2)(a)).
(iv) names which include a word or expression specified under the Company and Business Names Regulations 1981 (s.26(2)(b)).

The name of a company can always be changed by a special resolution of the company so long as it continues to comply with the above requirements (s.28 (1)).

5 (a) Dividends are the return received by shareholders in respect of their investment in a company. Subject to any restriction in the memorandum of association, every company has the implied power to apply its profits in the distribution of dividend payments to its shareholders. Although the directors recommend the level of dividend payment, it is for the company in a general meeting to declare the dividend. This is one of the items conducted at the annual general meeting. If the directors decline to recommend a dividend then it is not open to the general meeting to overrule that decision and declare a dividend.

The long standing common law rule is that dividends must not be paid out of capital (*Flitcroft's case* 1882). The current rules relating to the payment of dividends were introduced by the Companies Act 1980, now the Companies Act 1985. These rules represent a considerable strengthening of the previous situation, which was notoriously lax in the way in which dividend payments could be determined. The present Act governs and imposes restrictions on distributions made by all companies, both public and private. Section 263 defines distribution as **any** payment, cash or otherwise, of a company's assets to its members, except for the categories stated in the section, which include the issue of bonus shares, the redemption of shares, authorised reductions of share capital, and the distribution of assets on winding up.

Section 263 also provides the basic condition for distribution applying to **all** companies, which, in essence, is that they must have profits available for that purpose. This term is defined as accumulated realised profits less accumulated realised losses, with profit or loss being either revenue or capital in origin.

It is important to note that the use of the term accumulated means that any previous years' losses must be included in determining the distributable surplus, and that the requirement that profits be realised prevents payment from purely paper profit resulting from the mere revaluation of assets. Section 275 provides that all losses are to be treated as realised except where a general revaluation of all fixed assets has taken place.

(b) As has been stated, the foregoing realised profits test applies to both private and public companies, but public companies face an additional test in relation to distributions, in that s.264 requires that any distribution must not reduce the value of the company's net assets below the aggregate of its total called up share capital plus any undistributable reserves. The effect of this rule is that public companies have to account for changes in the value of their fixed assets, and are required to apply an essentially balance-sheet approach to the determination of profits.

(c) Under the rule in *Flitcroft's case* any directors of a company who breached the distribution rules, and knowingly paid dividends out of capital, were held jointly and severally liable to the company to replace any such payments made. The fact that the shareholders might have approved the distribution did not validate the illegal payment (*Aveling Barford Ltd* v *Perion Ltd* (1989)). Also at common law, shareholders who knowingly received, or ought to have known that they had received an unlawful dividend payment were required to repay the money received, or to indemnify the directors for payments they might have already been required to have made (*Moxham* v *Grant* (1900)). Section 277 of the Companies Act 1985 restates the common law rule, providing that shareholders, who either know or have reasonable grounds for knowing that any dividend was paid from capital, shall be liable to repay any such money received to the company.

6 **(a)** Normally employees who resign deprive themselves of the right to make a claim for redundancy or other payments. However s.136 Employment Rights Act 1996 (ERA) covers situations where 'the employee terminates the contract with, or without, notice in circumstances which are such that he or she is entitled to terminate it without notice by reason of the employer's conduct'. This provision relates to what is known as 'constructive dismissal' which covers the situation where an employer has made the situation of the employee such that the employee has no other option than to resign. In other words the unreasonable actions of the employer force the employee to resign. In such a situation the employee is entitled to make a claim for unfair dismissal no matter the fact that they actually resigned. In *Simmonds* v *Dowty Seals Ltd* (1978) Simmonds had been employed to work on the night shift. When his employer attempted to force him to work on the day shift he resigned. It was held that he could treat himself as constructively dismissed because the employer's conduct had amounted to an attempt to unilaterally change an express term of his contract. An employee may also be able to claim constructive dismissal where the employer is in breach of an implied term in the contract of employment (*Gardner Ltd* v *Beresford* (1978)). In *Woods* v *WM Car Services (Peterborough)* (1982) it was further held that there is a general implied contractual duty that employers will not, without reasonable or proper cause, conduct themselves in a manner that is likely to destroy the relationship of trust and confidence between employer and employee and that such obligation is independent of and in addition to the express terms of the contract.

The action of the employer, however, must go to the root of the employment contract if it is to allow the employee to resign. In other words it must be a breach of some significance. In *Western Excavating Ltd* v *Sharp* (1978), Sharp was dismissed for taking time off from work without permission. On appeal to an internal disciplinary hearing, he was reinstated but was suspended for five days without pay. He agreed to accept this decision but asked his employer for an advance on his holiday pay as he was short of money: this was refused. He then asked for a loan of £40: that was also refused. Consequently Sharp decided to resign in order to get access to his holiday pay. Sharp instituted a claim for unfair dismissal on the basis that he had been forced to resign because of his employer's unreasonable conduct. The employment tribunal found in Sharp's favour on the grounds that his employer's conduct had been so unreasonable that Sharp could not be expected to continue working there. However, on appeal the Court of Appeal held that before a valid constructive dismissal can take place the employer's conduct must amount to a breach of contract, which is such that it entitles the employee to resign. In Sharp's case there was no such breach and therefore there was no constructive dismissal. However, in *British Aircraft Corporation* v *Austin* (1978) a failure to investigate a health and safety complaint was held to be conduct amounting to a breach of contract on the part of the employer which was sufficient to entitle the employee to treat the contract as terminated.

If the employee does not resign in the event of a breach by the employer the employee will be deemed to have accepted the breach and waived any rights. However, they do not need to resign immediately and may, legitimately, wait until they have found another job (*Cox Toner (International) Ltd* v *Crook* (1981)).

(b) In relation to a successful claim for unfair dismissal, an Employment Tribunal may award any one of the following remedies:

(i) reinstatement,
(ii) re-engagement or
(iii) compensation.

Reinstatement is where the dismissed employee is treated as not having been dismissed in the first place.

Re-engagement means that the dismissed employee is re-employed under a new contract of employment.

The calculation of a *basic* award of compensation is calculated in the same way as for redundancy payments and is subject to the same maximum level of payment. The actual figures are calculated on the basis of the person's age, length of continuous service and weekly rate of pay subject to statutory maxima. Thus employees between the ages of 18 and 21 are entitled to $^{1}/_{2}$ week's pay for each year of service, those between 22 and 40 are entitled to 1 week's pay for every year of service, and those between 41 and 65 are entitled to $1^1/_2$ weeks' pay for every year of service. The maximum number of years of service that can be claimed is 20 and as the maximum level of pay that can be claimed is £310, the maximum total that can be claimed is £9,300, (i.e. 1·5 x 20 x 310).

In addition, however, a *compensatory* award of up to £60,600 may be made at the discretion of the tribunal and an *additional* award of up to £16,160 may be made where the employer ignores an order for re-employment or re-engagement, or the reason for dismissal was unlawful discrimination.

7 This question requires candidates to consider the crucially important role of the auditor in relation to companies and the way in which the behaviour of such businesses function and are overseen. The corporate governance structure specifies the distribution of rights and responsibilities among different participants in the corporation, such as, the board, managers, shareholders and other stakeholders, and spells out the rules and procedures for making decisions on corporate affairs. Auditors have an extremely important role to play in that regard: they are appointed to ensure that the interests of the shareholders in a company are being met. Their key function is to produce independent and authoritative reports confirming, or otherwise, that the accountancy information provided to shareholders is reliable. The law relating to company auditors is to be found in ss.384–394 Companies Act (CA) 1985 as altered by CA 1989. Even where a company has passed an elective resolution to dispense with laying accounts, the accounts are still required to be prepared, audited and circulated. Consequently every company, only excepting dormant private companies, is required to appoint an auditor, who must be appropriately qualified and in other respects eligible (s.384(1) CA 1985).

Qualifications

The essential requirement for any person to act as a company auditor is that they are eligible under the rules, and a member of, a recognised supervisory body (s.25 CA 1989). This in turn requires them to hold a professional accountancy qualification. 'Supervisory bodies' are ones established in the UK to control the eligibility of potential company auditors and the quality of their operation (s.30 CA 1989). The recognised supervisory bodies are:

(a) the Institute of Chartered Accountants in England and Wales;
(b) the Institute of Chartered Accountants of Scotland;
(c) the Institute of Chartered Accountants in Ireland;
(d) the Association of Chartered Certified Accountants; and
(e) the Association of Authorised Public Accountants.

The first four bodies mentioned above are also recognised as 'qualifying bodies', meaning that accountancy qualifications awarded by them are recognised professional qualifications for auditing purposes. There still is the small possibility of unqualified but appropriately experienced individuals acting as auditors in relation to what used to be known as 'exempt private companies' (s.3 CA 1989).

A person is ineligible for appointment as auditor if they are either:

(a) an officer or employee of the company (the auditor being specifically declared not to be an officer or employee); and/or
(b) a partner or employee of a person in (a) above, or is in a partnership of which such a person is a partner (CA 1989, s.27).

It is a criminal offence to act while ineligible.

Appointment and removal

Auditors are appointed annually (s.385 CA 1985), generally, at each annual general meeting. Where a company has passed an elective resolution to dispense with the annual reappointment of auditors, they are, nonetheless, deemed to be re-appointed automatically for each year. The first auditors are usually appointed by the directors or, in default, by the company in general meetings (s.385 CA 1985). The first auditors hold office until the conclusion of the first meeting at which accounts are laid, although they can, of course, be re-elected. If auditors are not appointed, or re-appointed, then the Secretary of State may appoint auditors to act (s.387(1)/CA 1985).

Under the Combined Code on Corporate Governance, a company's audit committee must be involved in the appointment and dismissal of both the external and internal auditors. Audit committees must have annual procedures to ensure the independence and objectivity of the external auditor which should involve a consideration of all relationships between the company and the firm carrying out the external audit.

An auditor may be removed at any time by an ordinary resolution of the company (s.391(1)). This does, however, require special notice. Any auditor who is to be removed or not re-appointed is entitled to make written representations and require these to be circulated or have them read out at the meeting (s.391A CA 1985).

An auditor may resign at any time (s.392 CA 1985). Notice of resignation must be accompanied by a statement of any circumstances that the auditor believes ought to be brought to the attention of members and creditors, or alternatively a statement that there are no such circumstances (s.394 CA 1985). The company is required to file a copy of the notice with the registrar of companies within 14 days (s.392 CA 1985). Where the auditor's resignation statement states that there are circumstances that should be brought to the attention of members, then he may require the company to call a meeting to allow an explanation of those circumstances to the members of the company (s.392A(1)/CA 1985).

Rights and duties
The auditors have the right of access at all times to the company's books and accounts, and officers of the company are required to provide such information and explanations as the auditors consider necessary (s.389A CA 1985). It is a criminal offence to make false or reckless statements to auditors (s.389A CA 1985).

It should be noted that the *Companies (Audit, Investigations And Community Enterprise) Act* 2004 (C(AICE)A) significantly strengthened the power of auditors. Under s.389A of the Companies Act 1985 a company's auditors were entitled to require from the company's officers such information and explanations as they thought necessary for the performance of their duties as auditors. It always was a criminal offence for an officer of the company to provide misleading, false or deceptive information or explanations. However, it was not an offence for them to fail to provide any information or explanation that the auditors required of them. That anomaly has been remedied by the (C(AICE)A) as follows:

– section 8 of C(AICE)A makes it a criminal offence to fail to provide information or explanations required by the auditor;
– section 8 also entitles the auditor to require information and explanations from a wider group of people than merely the officers of the company. Consequently employees may now be subject to the auditor's authority;
– subsection 8(4) makes it an offence for a parent company to fail to take all steps reasonably open to it to obtain the information or explanations which the auditor has required it to obtain from its non-UK subsidiary and those associated with it; and the offence applies also to any officer of the company who knowingly and wilfully authorises or permits the failure;
– section 9 requires that Directors' Reports must contain a statement that the directors are not aware of relevant information which has not been disclosed to the company's auditors. The directors are placed under the duty to ensure that they have taken all the steps they should have taken as a director to make themselves aware of such information and to establish that the auditors are aware of it. It will be a criminal offence to issue a false statement. The stated purpose of s.9 is to ensure that each director will have to think hard about whether there is any information that they know about or could ascertain which is needed by the auditors in connection with preparing their report.

Auditors are entitled to receive notices and other documents in connection with all general meetings, to attend such meetings and to speak when the business affects their role as auditors (s.390 CA 1985). Where a company operates on the basis of written resolutions rather than meetings, then the auditor is entitled to receive copies of all such proposed resolutions as are to be sent to members (s.381B CA 1985).

Auditors are required to make a report on all annual accounts laid before the company in a general meeting during their tenure of office (s.235 CA 1985). They are specifically required to report on certain issues:

(a) whether the accounts have been properly prepared in accordance with the Act; and
(b) whether the individual and group accounts show a true and fair view of the profit or loss and state of affairs of the company and of the group, so far as concerns the members of the company;
(c) whether the information in the Directors' Report is consistent with the accounts presented.

Under s.237 CA 1985 auditors are required to investigate:

(a) whether the company has kept proper accounting records and obtained proper accounting returns from branches.
(b) whether the accounts are in agreement with the records; and state:
    (i) whether they have obtained all the information and explanations that they considered necessary;
    (ii) whether the requirements concerning disclosure of information about directors and officers' remuneration, loans and other transactions have been met; and rectify any such omissions.

The Companies Act places further duties on auditors relating to such issues as:

(a) the valuation of non-cash consideration for share allotment by a public company or a company converting to a public company (ss.44 & 108 CA 1985);
(b) purchase or redemption of own shares by payment out of capital (s.173 CA 1985);
(c) financial assistance for purchase of own shares (s.156 CA 1985).

Potential liabilities
In *Caparo Industries plc* v *Dickman* (1990) company accounts were audited in accordance with the Companies Act 1985. The respondents, who already owned shares in the company, decided to purchase more shares and take over the company after seeing the accounts. The accounts were inaccurate. The respondents then incurred a loss, which they blamed on the negligently audited accounts. It was held that, when the accounts were prepared, a duty of care was owed to members of the company (that is, the shareholders), but only so far as to allow them to exercise proper control over the company. This duty did not extend to members as individuals and potential purchasers of shares. The onus was clearly on the appellants in these circumstances to make their own independent inquiries, as it was unreasonable to rely on the auditors.

8 This question requires candidates to analyse the problem scenario from the perspective of contract law paying particular regards to the rules relating to: invitation to treat, offers, counter offers, option contracts, the postal rule of acceptance. The scenario involves three distinct cases which should be dealt with in turn in applying the following rules of contract law.

In spite of its wording the sign in the window does not constitute a legal offer, it is merely an invitation to treat. As such it is not an offer to sell but merely an invitation to others to make offers. The point of this is that the person extending the invitation is not bound to accept any offers made to them as may be seen in *Fisher* v *Bell* (1961) in which it was held that having switch-blade knives in the window of a shop was not the same as offering them for sale.

A counter-offer arises where the offeree tries to change the terms of an original offer. The counter-offer has the same effect as an express rejection of an offer (*Hyde* v *Wrench* (1840)) and as a result the offeree cannot subsequently accept the original offer.

Where acceptance is made through the postal service, it 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 (*Adams* v *Lindsell* (1818)).

A contract may be entered into through the exchange of executory consideration; i.e. a promise for a promise. Although the actual exchange of concrete consideration may not take place until a later time, the agreement is none the less binding from the time of the exchange of promises.

Ali and Ben
As stated above, the sign in the window was merely an invitation to treat and the postal rule only applies to offers and does not apply to invitations to treat. Consequently as Ben was in fact making an offer to Ali when he sent his letter, it was for Ali to accept or reject the offer on receipt of the letter, providing he had not already bound himself to any alternative contractual agreement.

Ali and Chet
The first real offer is made by Chet when he says that he would give Ali £400 for the vase. Ali responded by making a counter-offer to sell the vase for £450 to which Chet restated his original offer, this time in the form of a counter-offer to Ali's new offer. As a result Chet, by insisting on his offer of £400, cannot at a later time attempt to accept Ali's offer of £450.

At first look it might appear that Chet may have taken advantage of the postal rule; however, when it is realised that it was not open to him to make any acceptance as he had rejected Ali's offer, it is apparent that the postal rule is of no avail to Chet, so he has no contract with Ali. Once again Ali might have accepted the offer on receipt of the letter, providing he had not already bound himself to any alternative contractual agreement.

Ali and Di
In line with the preceding analysis Di made an offer to Ali, which he readily accepted. The parties entered into a binding contract by their mutual exchange of promises: Di to bring the £400 on the following Monday and Ali to give her the vase. As a result although Ali might prefer to accept Ben's offer, he is nonetheless contractually bound to deliver the vase to Di if and when she brings the agreed sum of £400 to him on Monday. Of course if Di does not provide the money by the agreed time Ali would be at liberty to sell the vase to either Ben or Chet, as he chose.

9 Earl clearly finds himself in an awkward situation in that he holds a number of concurrent relationships with Flash Ltd; for he is at one and the same time, a member of the company through his shareholding, a creditor of the company through his debentures and its employee. All of these relationships involve different legal rules and result in different consequences: as an employee he has not been paid the wages due to him and consequently is looking for payment, as a creditor he is also owed money, which he will look to be repaid. However, as a member of the company, holding partly paid up shares he may be liable to contribute to the company's debts. Each of these relationships will be considered in turn.

(a) Earl's unpaid wages
As an employee Earl's situation is governed by s.175 and Schedule 6 of the Insolvency Act 1986, which sets out what are to be treated as preferred payments and specifically relates to the wages of employees together with all accrued holiday pay (£800 maximum). It should be noted that the Enterprise Act 2002 removed the Crown from those who can claim preference. Consequently, the state can no longer take any priority over non-secured creditors in relation to monies due to such as unpaid value added tax, national insurance or income tax. However, it should also be noted that Earl's rights are limited to a maximum payment of £800 as an employee and he would then have to claim against the company as an ordinary unsecured creditor for the remainder of the money owed to him.

(b) Earl's partly paid up share-holding
The nominal value of a share normally fixes the amount which the shareholder is required to contribute to the assets of the company. Section 1(2) of the Companies Act 1985 provides that members' liability is limited to the amount (if any) remaining unpaid on their shares.

Shareholders must pay at least the full nominal value of any shares issued to them (i.e. shares must not be issued at a discount s.100). Where, however, the company issues shares at a premium, i.e. at more than the nominal value of the shares, as is quite common, then the holders of those shares will be liable to pay the amount owed, over and above the nominal value. The excess will still form part of the company's capital but will be included in a distinct share premium account (s.130) and may only be used for limited purposes.

Applying these rules, it can be seen that Earl has only paid 75 pence per £1 nominal share. Consequently he is liable to contribute the amount remaining unpaid per share, i.e. a maximum of 25 pence per share (£1,250 in total), to the assets of the company if such payment is necessary to satisfy the outstanding debts of Flash Ltd upon winding up.

(c) Earl's debentures
In relation to a fixed charge, a specific asset of the company, in this instance the land on which the business stands, is made subject to a charge in order to secure a debt. If the company fails to honour the commitments to the secured debenture holders, they can appoint a receiver who will if necessary sell the asset charged to recover the money owed. In the case of a company liquidation, the asset charged is realised and the sum of money raised goes to pay off the outstanding debts owed to the debenture holders. If the value of the asset that is subject to the charge is greater than the debt against which it is

charged then the excess goes to pay off the rest of the company's debts. If it less than the value of the debt secured then the debenture holders will become unsecured creditors for the amount remaining outstanding. It should be emphasised that fixed charge holders take priority over any other creditors in the event of company liquidation.

Thus in this instance, Earl is secure in the knowledge that his loans to Flash Ltd will be paid before any other debts and as the security is against Flash's most valuable asset, its land, it is likely that he will receive the full amount of the loan of £5,000.

10 This question requires candidates to consider the authority of company directors and other company officers to enter into binding contracts on behalf of their companies.

Article 70 of Table A model articles of association provides that the directors of a company may exercise all the powers of the company. It is important to note that this power is given to the board as a whole and not to individual directors and consequently individual directors cannot bind the company without their being authorised in some way so to do. There are three ways in which the power of the board of directors may be extended to individual directors.

(a) The individual director may be given *express authority* to enter into a particular transaction on the company's behalf. To this end, Article 72 allows for the delegation of the board's powers to one or more directors. Where such express delegation has been made, then the company is bound by any contract entered into by the person to whom the power was delegated. However, in the present situation it does not appear that Len has been expressly given the power to enter into the contract with Mo, and so the company cannot be made liable on this basis.

(b) A second type of authority that may empower an individual director to bind his company is *implied authority*. In this situation, the person's authority flows from their position. Article 84 provides for the board of directors to appoint a managing director and Article 72 also allows the board of directors to delegate to any managing director such powers as they consider desirable to be exercised by that person. Thus the board of directors may expressly confer any of their powers on the managing director as they see fit. The mere fact of appointment, however, will mean that the person so appointed will have the implied authority to bind the company in the same way as the board, whose delegate he or she is. Outsiders, therefore, can safely assume that a person appointed as managing director has all the powers usually exercised by a person acting as a managing director.

Implied actual authority to bind a company may also arise as a consequence of the appointment of an individual to a position other than that of managing director. In *Hely-Hutchinson* v *Brayhead Ltd* (1968), although the chairman and chief executive of a company acted as its *de facto* managing director, he had never been formally appointed to that position. Nevertheless, he purported to bind the company to a particular transaction. When the other party to the agreement sought to enforce it, the company claimed that the chairman had no authority to bind it. It was held that, although the director derived no authority from his position as chairman of the board, he did acquire such authority from his position as chief executive and thus the company was bound by the contract he had entered into on its behalf.

Once again, however, it would appear that Mo cannot make use of this method of fixing Katch Ltd with liability for his contract as Len has not been appointed to any executive office in the company.

(c) The third way in which an individual director may possess the power to bind his company is through the operation of ostensible authority, which is alternatively described as apparent authority or agency by estoppel.

This arises where an individual director has neither express nor implied authority. Nonetheless, the director is held out by the other members of the board of directors as having the authority to bind the company. If a third party acts on such a representation, then the company will be estopped from denying its truth.

In *Freeman and Lockyer* v *Buckhurst Park Properties (Mangal) Ltd* (1964), although a particular director had never been appointed as managing director, he acted as such with the clear knowledge of the other directors and entered into a contract with the plaintiffs on behalf of the company. When the plaintiffs sought to recover fees due to them under that contract, it was held that the company was liable: a properly appointed managing director would have been able to enter into such a contract and the third party was entitled to rely on the representation of the other directors that the person in question had been properly appointed to that position.

The situation in the problem is very similar to that in *Freeman and Lockyer* v *Buckhurst Park Properties (Mangal) Ltd*. The board of Katch Ltd has permitted Len to act as its managing director, and he has even used that title. The board has therefore acquiesced in his representation of himself as their managing director and consequently they and Katch Ltd are bound by any contracts he might make within the scope of a managing director's implied authority. As entering into a contract to draw up plans would clearly come within that authority, Katch Ltd will be liable to pay Mo or face an action for breach of contract.

1 This question is divided into two parts, the first of which requires a consideration of the difference between criminal and civil law, with the second part requiring an explanation of the various courts which deal with these categories of law.

(a) 3–5 A thorough to comprehensive explanation of the difference between the two types of law.
0–2 Ranging from some but little knowledge down to no understanding at all of the differences.

(b) 4–5 Full explanation of both court systems.
2–3 Some explanation of the courts in both systems.
0–1 Little or no knowledge of either court system or, at the higher end of this grade, some knowledge of one of the systems.

2 This question is divided into two parts, part (a) carries 6 marks and part (b) carries 4 marks.

8–10 A thorough understanding of both topics demonstrated by references to cases or examples.
5–7 A clear understanding of both topics but perhaps lacking in detail.
Alternatively, an unbalanced answer showing good understanding of one part but less in the other.
2–4 Some, but limited, understanding of both topics, or clear understanding of only one of the topics.
0–1 Little or no knowledge of either of the topics.

3 This question refers to the issue of remoteness of damage in the law of negligence.

8–10 A thorough understanding of the issues involved. It is likely that the best answers will focus on the cases, although examples might be used.
5–7 A clear understanding of the topics but perhaps lacking in detail.
2–4 Some, but limited, understanding of the issue, perhaps not referring to any cases to support the explanation.
0–1 Little or no knowledge of the topic.

4 This question requires candidates to explain three of the clauses in a company's memorandum of association.

8–10 A thorough understanding of all three clauses. It is likely that the best answers will provide examples or cite appropriate cases, although this is not necessary to acquire full marks.
5–7 A clear understanding of the clause but perhaps lacking in detail or unbalanced in only dealing with two of them.
2–4 Some, but limited, understanding of the clauses.
0–1 Little or no knowledge of the clauses.

5 This question requires candidates to explain the rules relating to the lawful distribution of company dividends and further requires the candidates to focus on the different rules that apply to public and private companies. Although divided into three parts, candidates may provide a global answer.

8–10 A thorough understanding of law relating to dividends as it applies to both public and private companies. Cases may well be cited and will be credited.
5–7 A clear understanding of the general law but perhaps lacking in detail or unbalanced in only dealing with one of the types of company.
2–4 Some, but limited, understanding of the law.
0–1 Little or no knowledge of the clauses.

6 This question, relating to issues in employment law, is divided into two parts and the marks will be allocated equally.

(a) Requires candidates to explain what is meant by constructive dismissal.
4–5 A clear concise explanation perhaps citing cases or examples.
2–3 A clear understanding, but perhaps lacking authority or examples.
0–1 Unbalanced, or may not deal with all of the required aspects of the topic. Alternatively the answer will demonstrate very little understanding of what is actually meant by constructive dismissal.

(b) 4–5 Thorough to complete answers, showing a detailed understanding of all or certainly most of the remedies available.
2–3 A clear understanding of the remedies, but perhaps lacking in detail.
0–1 Little or no knowledge of the topic.

7 This question requires candidates to consider the role of the auditor in relation to companies and the precise way in which this relationship is regulated by company law.

8–10 A thorough understanding of the role of the auditor explaining their rights and duties. Mention will also be made of their qualifications for office and the manner in which they are appointed and may be removed.
5–7 A clear understanding of the general law but perhaps lacking in detail or unbalanced in only dealing with some issues.
2–4 Some knowledge of the role of auditors but lacking in detail or unbalanced in the detail provided.
0–1 Little or no knowledge of the topic.

8 This question requires candidates to analyse a problem scenario from the perspective of the law of contract and to apply that law appropriately. Given the fact that there are only 10 marks available candidates will gain no marks for irrelevant material.

8–10 A thorough analysis of the scenario focusing on the appropriate rules of law and applying them accurately. It is extremely likely that cases will be cited in support of the analysis and/or application.
5–7 A clear understanding of the general law but perhaps lacking in detail or unbalanced in only dealing with some issues.
2–4 Some, but limited, understanding of the law or completely lacking in application.
0–1 Little or no knowledge of the relevant law.

9 This question, divided into three parts, essentially requires candidates to consider the difference between various company creditors on the winding up of a company.

(a) 2–3 A good to thorough explanation of the situation of employees as preferred creditors.
0–1 Little or no knowledge of the relevant law.

(b) 2–3 A good general knowledge of the liability of holders of unpaid shares.
0–1 Little or no knowledge of the relevant law.

(c) 2–4 A good explanation of fixed charges together with accurate application of the law.
0–1 Some knowledge, but lacking in detail or application.

10 This question focuses on the authority of individual directors and how companies may be fixed with liability for contracts entered into by them. As with the other questions in this section, it requires candidates to analyse the problem scenario and to apply that law appropriately.

8–10 A thorough analysis of the scenario focusing on the appropriate rules of law and applying them accurately. It is extremely likely that cases will be cited in support of the analysis and/or application.
5–7 A clear understanding of the general law but perhaps lacking in detail or unbalanced in only dealing with some issues.
2–4 Some, but limited, understanding of the law or completely lacking in application.
0–1 Little or no knowledge of the relevant law.