Fundamentals Pilot Paper – Skills module

Corporate and Business Law (Global)

Time allowed
Reading and planning: 15 minutes
Writing: 3 hours

ALL TEN questions are compulsory and MUST be attempted.

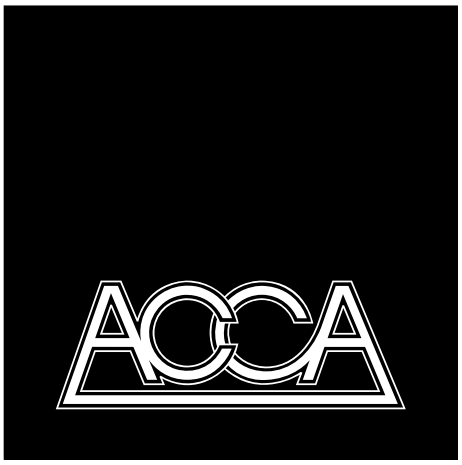
Do NOT open this paper until instructed by the supervisor.

During reading and planning time only the question paper may be annotated. You must NOT write in your answer booklet until instructed by the supervisor.

This question paper must not be removed from the examination hall.

The Association of Chartered Certified Accountants

Paper F4 (GLO)



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The question paper starts on page 3

ALL TEN questions are compulsory and MUST be attempted

1 Explain the role and activities of the following organisations:

(a) UNCITRAL; (6 marks)

(b) WTO. (4 marks)

(10 marks)

2 Within the context of the UNCITRAL Model Law on International Commercial Arbitration, explain the grounds and procedure for challenging a decision of an arbitration panel.

(10 marks)

3 Within the context of the UN Convention on Contracts for the International Sale of Goods, explain the meaning of, and the rules relating to, the concept of 'acceptance'.

(10 marks)

4 Within the context of the UN Convention on Contracts for the International Sale of Goods, explain the obligations placed on the contractual parties to preserve goods, in their possession, belonging to the other contractual party.

(10 marks)

5 In relation to company directors explain how the following types of authority may arise and explain the extent of the authority arising under each category:

(a) express authority; (3 marks)

(b) implied authority; (3 marks)

(c) apparent/ostensible authority. (4 marks)

(10 marks)

6 In relation to company law explain and distinguish between the following:

(a) annual general meeting; (5 marks)

(b) extraordinary general meeting; (2 marks)

(c) class meeting. (3 marks)

(10 marks)

7 (a) Explain briefly what is meant by 'corporate governance'. (4 marks)

(b) Within the context of corporate governance examine the role of, and relationship between, executive directors and non-executive directors. (6 marks)

(10 marks)

8 Art, a Dutch wholesaler entered into a contract with Carl, a Belgian chocolate manufacturer for the delivery of one tonne of chocolates per week at a specified price to an English retailer. The contract stated that the deliveries were to be made for a period of eight weeks, from May until the end of June.

During May the contract worked well, Art paid the weekly instalments and Carl delivered the chocolates to the retailer. However, in the first week in June, Art paid the usual instalment but Carl did not supply any chocolates to England, informing Art that he was uncertain as to whether he would ever be able to supply the full one tonne of chocolates as required under the contract.

Required:

Advise Art as to what action he can take under the UN Convention on Contracts for the International Sale of Goods, paying particular attention to the effect of Article 73 of the Convention.

(10 Marks)

9 Flop Ltd was in financial difficulties. In January, in order to raise capital it issued 10,000 $1 shares to Gus, but only asked him to pay 75 cents per share at the time of issue. The directors of Flop Ltd intended asking Gus for the other 25 cents per share at a later date. However, in June it realised that it needed even more than the $2,500 it could raise from Gus's existing shareholding. So in order to persuade Gus to provide the needed money Flop Ltd told him that if he bought a further 10,000 shares he would only have to pay a total of 50 cents for each $1 share, and it would write off the money owed on the original share purchase.

Gus agreed to this, but the injection of cash did not save Flop and in December it went into insolvent liquidation, owing a considerable amount of money.

Required:

Explain any potential liability that Gus might have on the shares he holds in Flop Ltd.

(10 marks)

10 In January the board of directors of Huge plc decided to make a take over bid for Large plc. After the decision was taken, but before it is announced the following chain of events occurs:

(i) Slye a director of Huge plc buys shares in Large plc;

(ii) Slye tells his friend Mate about the likelihood of the take-over and Mate buys shares in Large plc;

(iii) at a dinner party Slye, without actually telling him about the take-over proposal, advises his brother Tim to buy shares in Large plc and Tim does so.

Required:

Consider the legal position of Slye, Mate and Tim under the law relating to insider dealing.

(10 marks)

End of Question Paper

Answers

1 (a) The United Nations Commission on International Trade Law (UNCITRAL) is the core legal body within the United Nations system in the field of international trade law. It was established by the General Assembly in 1966 (Resolution 2205(XXI)). In establishing the Commission, the General Assembly recognized that disparities in national laws governing international trade created obstacles to the flow of trade, and UNCITRAL was given the task of furthering the progressive harmonization and unification of the law of international trade. This was to be achieved by:

- Co-ordinating the work of organisations active in this field and encouraging co-operation among them;
- Promoting wider participation in existing international conventions and wider acceptance of existing model and uniform laws;
- Preparing or promoting the adoption of new international conventions, model laws and uniform laws and promoting the codification and wider acceptance of international trade terms, provisions, customs and practices, in collaboration, where appropriate, with the organisations operating in this field;
- Promoting ways and means of ensuring a uniform interpretation and application of international conventions and uniform laws in the field of the law of international trade;
- Collecting and disseminating information on national legislation and modern legal developments, including case law, in the field of the law of international trade;
- Establishing and maintaining a close collaboration with the United Nations Conference on Trade and Development;
- Maintaining liaison with other United Nations organs and specialised agencies concerned with international trade;
- Taking any other action it may deem useful to fulfil its functions.

The Commission is composed of 60 member States elected by the General Assembly and is structured so as to be representative of the world's various geographic regions, economic and legal systems. The Commission carries out its work at annual sessions, which are held in alternate years at United Nations Headquarters in New York and in Vienna. Members of the Commission are elected for terms of six years, the terms of half the members expiring every three years.

The Commission operates through six working groups, although these are composed of all member States of the Commission. The six working groups and their current topics are as follows:

- working group I – Privately-financed infrastructure projects
- working group II – International arbitration and conciliation
- working group III – Transport law
- working group IV – Electronic
- working group V – Insolvency
- working group VI – Security interests

Non-members of the Commission, as well as interested international organizations, are invited to attend sessions of the Commission and of its working groups as observers and can participate in any discussions to the same extent as members.

The following are some of the most important outcomes of the work conducted by UNCITRAL:

United Nations Convention on Contracts for the International Sale of Goods (Vienna, 1980). This Convention establishes a comprehensive code of legal rules governing the formation of contracts for the international sale of goods, the obligations of the buyer and seller, remedies for breach of contract and other aspects of the contract.

United Nations Convention on the Carriage of Goods by Sea, 1978 (the 'Hamburg Rules'). This Convention establishes a uniform legal regime governing the rights and obligations of shippers, carriers and consignees under a contract of carriage of goods by sea.

UNCITRAL Model Law on International Commercial Arbitration (1985). These provisions are designed to assist States in reforming and modernizing their laws on arbitral procedure so as to take into account the particular features and needs of international commercial arbitration.

United Nations Convention on International Bills of Exchange and International Promissory Notes (New York, 1988). This Convention provides a comprehensive code of legal rules governing new international instruments for optional use by parties to international commercial transactions.

UNCITRAL Model Law on Electronic Commerce. This Model Law, adopted in 1996, is intended to facilitate the use of modern means of communications and storage of information.

UNCITRAL Model Law on Cross-Border Insolvency. This Model Law seeks to promote fair legislation for cases where an insolvent debtor has assets in more than one State.

(b) The World Trade Organization (WTO) was created in 1995, as the re-embodiment of the General Agreement on Tariffs and Trade (GATT) had provided the rules for the system of international trade since 1948. GATT evolved through several rounds of negotiations, with the last one, the Uruguay Round which lasted from 1986 to 1994 leading to the agreement to the creation of the WTO. Whereas GATT had mainly dealt with trade in goods, the WTO and its agreements now cover trade in services, and in traded inventions, creations and intellectual property. The WTO has nearly 150 members, accounting for over 97% of world trade.

The WTO's overriding purpose is to assist the free flow of trade through the removal of obstacles to such trade. It also endeavours to ensure that individuals, companies and governments know what the trade rules are around the world, thus giving them the confidence that there will be no sudden changes of policy.

The WTO seeks to achieve these purposes by:

– Administering trade agreements
– Acting as a forum for trade negotiations
– Settling trade disputes
– Reviewing national trade policies
– Assisting developing countries in trade policy issues, through technical assistance and training programmes
– Cooperating with other international organizations.

The WTO Agreements, covering goods, services and intellectual property, spell out the principles of liberalization, and the limited permitted exceptions to that process are the result of negotiations between the members. The agreements include individual countries' commitments to lower customs tariffs and other trade barriers, and to open and keep open services markets. They set procedures for settling disputes. They prescribe special treatment for developing countries. They require governments to make their trade policies transparent by notifying the WTO about laws in force and measures adopted, and through regular reports by the secretariat on countries' trade policies. The current set of agreements is the outcome of the 1986–94 Uruguay Round negotiations which included a major revision of the original General Agreement on Tariffs and Trade (GATT). Through these agreements, WTO members engage to operate a non-discriminatory trading system that spells out their rights and their obligations. Each country receives guarantees that its exports will be treated fairly and consistently in other countries' markets. Each promises to do the same for imports into its own market. The system does, however, allow a degree of latitude to developing countries in implementing their commitments.

All WTO members must undergo periodic scrutiny, each review containing reports by the country concerned and the WTO Secretariat.

Decisions of the WTO are made by the entire membership, usually on the basis of consensus. However, a majority vote is possible but it has never actually been used in the WTO, although such decisions were taken under the WTO's predecessor, GATT.

The WTO's structure is as follows:

– the **Secretariat** is based in Geneva. It employs around 600 staff under the direction of a director-general. The Secretariat has no decision-making role and its duties are to supply technical support for the various councils and committees and the ministerial conferences, to provide technical assistance for developing countries, to analyze world trade, and to explain WTO affairs to the public and media. The Secretariat also provides some forms of legal assistance in the dispute settlement process and advises governments wishing to become members of the WTO.

– the **Ministerial Conference** is the WTO's top level decision-making body is which meets at least once every two years.

– the **General Council** (normally ambassadors and heads of delegation in Geneva, but sometimes officials sent from members' capitals) which meets several times a year in Geneva. The General Council also meets as the Trade Policy Review Body and the Dispute Settlement Body.

– Specific councils such as the **Goods Council, Services Council and Intellectual Property (TRIPS) Council** report to the General Council.

– numerous specialised committees, **working groups** and **working parties** deal with the individual agreements and other areas such as the environment, development, membership applications and regional trade agreements.

Under the Dispute Settlement Understanding the WTO operates a dispute settlement procedure for resolving trade quarrels when they arise between members countries. The dispute settlement procedure encourages countries to settle their differences through consultation. However, where this proves unsuccessful, the parties engage in a stage-by-stage procedure that may eventually result in a binding ruling by a panel of experts, subject to the further possibility of an appeal. The judgments of the panels are based on interpretations of the agreements and individual countries' commitments.

Settling disputes is the responsibility of the Dispute Settlement Body (the General Council in another guise), which consists of all WTO members.

The Dispute Settlement Body has the sole authority to establish 'panels' of experts to consider the case, and to accept or reject the panels' findings or the results of an appeal on a point of law only. It monitors the implementation of the rulings and recommendations, and has the power to authorize retaliation when a country does not comply with a ruling. Panellists are usually chosen in consultation with the countries in dispute. Only if the two sides cannot agree does the WTO director-general appoint them. Panels consist of three (possibly five) experts from different countries, who examine the evidence and decide who is right and who is wrong. The panel's report is passed to the Dispute Settlement Body, which can only reject the report by consensus. Panellists for each case can be chosen from a permanent list of well-qualified candidates, or from elsewhere. They serve in their individual capacities. They cannot receive instructions from any government.

Any appeal is heard by three members of a permanent seven-member Appellate Body set up by the Dispute Settlement Body and broadly representing the range of WTO membership. Members of the Appellate Body have to be individuals with recognized standing in the field of law and international trade, not affiliated with any government.

The appeal can uphold, modify or reverse the panel's legal findings and conclusions. The ultimate decision rests with the Dispute Settlement Body which has to accept or reject the appeals report within 30 days, however, and rejection is only possible by consensus.

2 In any case of arbitration it is essential that the parties involved can place utmost reliance on the person chosen to be the arbitrator. They must be able to rely on the fact that the arbitrator has the requisite skills to act in his arbitral capacity, but equally they must be able to trust that the person appointed is, and will remain, neutral and will deliver a fair and impartial decision. Impartiality and independence are therefore of crucial importance in the operation of international arbitration. Consequently, under Article 12 of the UNCITRAL Model Law of Commercial Arbitration, when a person is approached in connection with the possibility of their being appointed as an arbitrator, they are required to disclose any circumstances likely to give rise to justifiable doubts as to their impartiality or independence. They are also required to notify the parties of any circumstances that subsequently raise such doubts as to their impartiality.

The appointment of a person as an arbitrator may only be challenged on two grounds:
– where circumstances exist that give rise to justifiable doubts as to his impartiality or independence, or
– where the person appointed does not possess qualifications agreed to by the parties.

In addition a party can not challenge an arbitrator appointed by them, or in whose appointment they participated, for any reasons they were aware of before the arbitrator was appointed.

Under Article 13 the parties are free to agree on a procedure for challenging an arbitrator. Where no such agreement has been established, then any party who intends to challenge an arbitrator has 15 days, after becoming aware of the constitution of the arbitral tribunal or after becoming aware of any grounds for challenge, to send a written statement of the reasons for the challenge to the arbitral tribunal.

Unless the challenged arbitrator withdraws from his office or the other party agrees to the challenge, the arbitral tribunal shall decide on the challenge. If a challenge is not successful, the party issuing the challenge has a further 30 days to request the court or other specified authority to decide on the challenge. This level of decision is final, and cannot be further appealed against. Whilst any appeal is under way, the original arbitral tribunal, including the challenged arbitrator, may continue the arbitral proceedings and make an award.

3 A contract is concluded at the moment when an acceptance of an offer becomes effective in accordance with the provisions of the Convention (*Article 23*). Such a pronouncement, however, requires an explanation of what is to be taken as amounting to acceptance under the provisions of the Convention.

By virtue of *Article 18* acceptance of an offer may be made by means of a *statement* or other *conduct* of the offeree. The essential feature is that the action indicates agreement to the offer originally made by the offeror. Consequently it is possible for acceptance to be spoken or written, but it is equally possible for the acceptance to take place through the performance of an action such as the despatch of goods or payment of an agreed price. As with other forms of acceptance, any such act normally takes effect at the moment of performance. It is imperative to emphasise that, silence or inactivity cannot amount to acceptance, so the offeror cannot impose acceptance on the offeree on the basis of the latter's inaction.

As regards the time of acceptance, it becomes effective at the moment the indication of assent reaches the offeror. An acceptance is not effective if the indication of assent does not reach the offeror within the time he has fixed or, if no time is fixed, within a reasonable time, due account being taken of the circumstances of the transaction, including the rapidity of the means of communication employed by the offeror.

An oral offer must be accepted immediately unless the circumstances indicate otherwise.

However, if, by virtue of the offer, or as a result of practices which the parties have established between themselves, or of usage, the offeree may indicate assent by performing an act, such as one relating to the despatch of the goods or payment of the price, without notice to the offeror, the acceptance is effective at the moment the act is performed, provided that the act is performed within the period of time laid down in the preceding paragraph.

Under *Article 19* an acceptance which contains additions, limitations or other modifications constitutes a counteroffer and acts as a rejection of the original offer.

However, if the additional terms do not 'materially alter the terms of the offer' then the acceptance is valid unless the offeror, without undue delay, objects to the alterations to the original offer.

Article 20 deals with matters relating to the time period within which acceptance has to be made. Thus,

- where a period of time for acceptance is set by the offeror in a telegram then that period begins to run from the moment the telegram is handed in for dispatch.
- where the period of time for acceptance is set in a letter then the period begins to run from the date shown on the letter. If no such date is shown, then the period runs from the date shown on the envelope.
- a period of time for acceptance fixed by the offeror by telephone, telex or other means of instantaneous communication, begins to run from the moment that the offer reaches the offeree.
- if a letter or other writing containing a late acceptance shows that it has been sent in such circumstances that if its transmission had been normal it would have reached the offeror in due time, the late acceptance is effective as an acceptance unless, without delay, the offeror orally informs the offeree that he considers his offer as having lapsed or dispatches a notice to that effect (*Article 21*).
- Official holidays or non-business days occurring during the period for acceptance are included in calculating the period. However, if a notice of acceptance cannot be delivered at the address of the offeror on the last day of the period because that day falls on an official holiday or a non-business day at the place of business of the offeror, the period is extended until the first business day which follows.

Acceptance 'reaches' the addressee when it is made orally to him or delivered by any other means to him personally, to his place of business or mailing address or, if he does not have a place of business or mailing address, to his habitual residence (*Article 24*).

Late acceptance may, however, be effective if without delay the offeror orally so informs the offeree or dispatches a notice to that effect (*Article 21*).

An acceptance may be withdrawn if the withdrawal reaches the offeror before or at the same time as the acceptance would have become effective (*Article 22*).

4 The United Nations Convention on Contracts for the International Sale of Goods imposes a duty on both parties to any contract covered by its provisions to preserve any goods in their possession belonging to the other party. Such a duty is of particular importance in international sale of goods contracts where the other party is unlikely to have a physical presence, and may not even have agents to act for them, in the country where the goods are located.

Under certain circumstances the party in possession of the goods may sell them, or may even be required to sell them. In such a situation the party selling the goods has the right to retain reasonable expenses for preserving and selling the goods out of the proceeds of the sale. They must of course account for any deduction to the other party for the balance.

The detailed provision of the Convention is as follows;

Article 85 provides that if the buyer does not take delivery of the goods at the agreed time and the seller has the goods in their possession or control, then the seller must take such steps as are reasonable in the circumstances to preserve them. As a result of the failure on the part of the buyer, the seller is entitled to any additional expense entered into to preserve the goods. The seller is entitled to keep the goods until they have received reasonable expenses from the buyer.

Equally, where the goods are supposed to be paid for on delivery, failure by the buyer to pay the price gives rise to similar provisions and procedures.

Article 86 applies to situations where goods are rejected by the buyer for some reason, either under the specific terms of the contract, or the under the general provisions of the Convention and the seller, or their agent, is not present at the place of delivery. In such circumstances, the buyer must take such steps to preserve the goods as are reasonable in the circumstances. If the goods have been placed at the buyers' disposal at the agreed destination and the buyers exercise the right to reject them, they must nonetheless take possession of the goods on behalf of the seller, provided that this can be done without payment of the price and without unreasonable inconvenience or unreasonable expense.

Once again, as with *Article 85*, they are entitled to retain the goods until they have been compensated for any reasonable expenses incurred. In respect of this latter point, *Article 87* expressly provides that any party, who is bound to take steps to preserve goods under the provisions of the Convention, may deposit them in a warehouse of a third person at the expense of the other party to the contract, provided that the expense incurred is not unreasonable.

Article 88

If the goods are subject to rapid deterioration, or their preservation would involve unreasonable expense, the party who is bound to preserve the goods in accordance with the Convention must take reasonable measures to sell them.

Also, where there has been an unreasonable delay by the other party in taking possession of the goods, or in taking them back, or in paying the price or the cost of preservation, then the party who was bound by the Convention to preserve the goods *may* sell them.

In the first situation the party selling the goods must give notice to the other party of his intention to sell to the extent that such notice is reasonably possible. In the second situation reasonable notice of the intention to sell must be given to the other party.

In any case the party selling the goods has the right to retain reasonable expenses for preserving and selling the goods out of the proceeds of the sale. They must, of course, account to the other party for any balance due on the sale.

5 An agent is a person who is empowered to represent another legal party, called the principal, and to bring the principal into a legal relationship with a third party. Any contract entered into is between the principal and the third party each of whom may enforce it. In the normal course of events the agent has no personal rights or liabilities in relation to the contract.

The principal/agent relationship can be created in a number of ways. It may arise as the outcome of a distinct contract, which may be made either orally or in writing, or it may be established purely gratuitously, where some person simply agrees to act for another.

In establishing a relationship of principal/agent, however the principal does not give the agent unlimited power to enter into any contract whatsoever but is likely to place strict limits on the nature of the contracts that the agent can enter into on his behalf. In other words the authority of the agent is limited and in order to bind a principal any contract entered into must be within the limits of the authority extended to the agent. The authority of an agent can take a number of distinct forms.

(a) **Express authority**

In this instance, when the principal/agency relationship is established, the agent is instructed as to what particular tasks are required to be performed and is informed of the precise powers given in order to fulfil those tasks. If the agent subsequently contracts outside of the ambit of their express authority then they will be liable to the principal and to the third party for breach of warrant of authority (see below). The consequences for the relationship between the principal and third party depends on whether the third party knew that the agent was acting outside the scope of their authority.

For example, an individual director of a company may be given the express power by the board of directors to enter into a specific contract on behalf of the company. In such circumstances the company would be bound by the subsequent contract but the director would have no power to bind the company in other contracts.

(b) **Implied authority**

This refers to the way in which the scope of express authority may be increased. Third parties are entitled to assume that agents holding a particular position have all the powers that are usually provided to such an agent. Without actual knowledge to the contrary they may safely assume that the agent has the usual authority that goes with their position.

In *Watteau* v *Fenwick* (1893) the new owners of a hotel continued to employ the previous owner as its manager. They expressly forbade him to buy certain articles including cigars. The manager, however, bought cigars from a third party, who later sued the owners for payment as the manager's principal. It was held that the purchase of cigars was within the usual authority of a manager of such an establishment and that for a limitation on such usual authority to be effective it must be communicated to any third party.

Directors of companies can also bind their companies on the basis of implied authority. 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 as it was within the implied authority of a person holding such a position.

(c) **Apparent/ostensible authority**

This type of authority, which is an aspect of agency by estoppel, can arise in two distinct ways:

(i) Where a person makes a representation to third parties that a particular person has the authority to act as their agent without actually appointing them as their agent. In such a case the person making the representation is bound by the actions of the ostensible/apparent agent. The principal is also liable for the actions of the agent where they are aware that the agent claims to be their agent and yet does nothing to correct that impression.

In *Freeman & 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.

(ii) Where a principal has previously represented to a third party that an agent has the authority to act on their behalf. Even if the principal has subsequently revoked the agent's authority they may still be liable for the actions of the former agent unless they have informed third parties who had previously dealt with the agent about the new situation (*Willis Faber & Co Ltd* v *Joyce* (1911)). Thus companies should inform their previous clients where a director has had his authority, either express or implied, removed or reduced.

6 In theory, the ultimate control over a company's business lies with the members in a general meeting. One would obviously conclude that a meeting involved more than one person; and indeed there is authority to that effect in *Sharp* v *Dawes* (1876) in which a meeting between a lone member and the company secretary was held not to be validly constituted. It is possible, however, for a meeting of only one person to take place in the following circumstances:

(i) in the case of a meeting of a particular class of shareholders and all the shares of that class are owned by the one member.

(ii) by virtue of s.371 of the Companies Act 1985 (CA) the court may order the holding of a general meeting at which the quorum is to be one member.

Types of meetings

There are three types of meeting:

(a) **the annual general meeting**. By virtue of s.366 of CA 1985, every company is required to hold an annual general meeting (AGM) every calendar year; subject to a maximum period of 15 months. This means that if a company held its AGM on 1 January 2000, then it must hold its next AGM by 31 March 2001 at the latest.

If a company fails to hold an AGM then any member may apply to the Secretary of State to call a meeting in default (CA s 367). The business conducted at AGMs tends to be routine such as the re-election of directors, consideration of accounts and approval of dividends. In line with the recognised distinction between public and private companies the CA 1989 introduced a provision, in the form of a new CA s.366 A, which permitted private companies, subject to approval by a unanimous vote, to dispense with the holding of annual general meetings. Under s.381 A of the CA 1985 it is no longer necessary for a private company to convene a general meeting where the members have unanimously signed a written resolution setting out a particular course of action.

(b) **the extraordinary general meeting**. An extraordinary general meeting (EGM) is any meeting other than an AGM. EGMs are usually called by the directors, although members holding 10% of the voting shares may requisition such a meeting by virtue of s.368 (CA 1985).

(c) **the class meeting**. This refers to the meeting of a particular class of shareholder; ie those who hold a type of share providing particular rights, such as preference shares. Where it is proposed to alter the rights attached to particular shares then it is necessary to acquire the approval of the holders of those particular shares to any such alteration. In order to achieve this approval, a meeting of those holding such shares has to be called to seek their approval of any proposed alteration (CA ss.125 –127).

Meetings may be convened in a number of ways by various people:

(i) by the directors of the company under Article 37 of Table A. Under s.142 CA 1985, to call meetings where there has been a serious loss of capital, defined as the assets falling to half or less than the nominal value of the called up share capital.

(ii) by the members using the power to requisition a meeting under s.368 CA 1985.

(iii) by the auditor of a company under s.392A, which provides for a resigning auditor to require the directors to convene a meeting in order to explain the reason for the auditor's resignation.

(iv) the Secretary of State may under s.367, on the application of any member, call a meeting of a company where it has failed to hold an AGM as required under s.366.

(v) the court may order a meeting under s.371, where it is impracticable otherwise to call a meeting.

7 **(a)** Corporate governance refers to the way in which companies are run and operated. According to the Organisation for Economic Co-operation and Development:

Corporate governance is the system by which business corporations are directed and controlled. 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. By doing this, it also provides the structure through which the company objectives are set, and the means of attaining those objectives and monitoring performance.

Although these interrelated issues have always been of concern in the way companies function, it cannot but be recognised that the increase in the attention placed on matters of corporate governance has been a result of the perceived weakness in company regulation which has been apparent in some of the recent scandals involving such large companies as Enron and Worldcom in America and Marconi and Parmalat in Europe.

In order to ensure an effective corporate governance framework it has been deemed necessary to set out defined rules and regulations, including voluntary codes. In the United Kingdom one such code is the Combined Code On Corporate Governance, which is the result of the review of the role and effectiveness of non-executive directors conducted by Derek Higgs and a review of audit committees conducted by Sir Robert Smith. This new combined code has applied to listed companies since November 2003. Companies have either to confirm that they comply with the Code's provisions or, where it does not, to provide an explanation of their non-compliance. Whilst listed companies are expected to comply with the Code's provisions most of the time, it is recognised that departure from its provisions may be justified in particular circumstances. Every company must review each provision carefully and give a considered explanation if it departs from the Code provisions.

(b) As regards the structure pf the board of directors the Combined Code requires that the board should include a balance of executive and non-executive directors (and in particular independent non-executive directors) such that no individual or small group of individuals can dominate the board's decision taking.

Executive directors usually work on a full time basis for the company and may be employees of the company with specific contracts of employment. Section 318 Companies Act (CA) 1985 requires that the terms of any such contract must be made available for inspection by the members. Section 319 renders void any such contract, which purports to be effective for a period of more than five years, unless it has been approved by a resolution of the company in a general meeting. In fact the Combined Code on Corporate Governance recommends that the maximum period for directors employment contracts should be one year.

Non-executive directors do not usually have a full-time relationship with the company, they are not employees and only receive directors' fees. The role of the non-executive directors, at least in theory, is to bring outside experience and expertise to the board of directors. They are also expected to exert a measure of control over the executive directos to ensure that the latter do not run in the company in their, rather than the company's, best interests. As the Combined Code puts it:

> 'As part of their role as members of a unitary board, non-executive directors should constructively challenge and help develop proposals on strategy. Non-executive directors should scrutinise the performance of management in meeting agreed goals and objectives and monitor the reporting of performance. They should satisfy themselves on the integrity of financial information and that financial controls and systems of risk management are robust and defensible. They are responsible for determining appropriate levels of remuneration of executive directors and have a prime role in appointing, and where necessary removing, executive directors, and in succession planning.'

It is important to note that there is no distinction in law between executive and non-executive directors and the latter are subject to the same controls and potential liabilities as are the former.

8 Art and Carl entered into a binding instalment contract in which the latter was obliged to supply the agreed quantity of chocolate at the agreed price. Article 73 of the UN Convention on Contracts for the International Sale of Goods specifically deals with instalment contracts. Article 73(1) provides that, in the case of a contract for delivery of goods by instalments, if the failure of one party to perform any of his obligations in respect of any instalment constitutes a fundamental breach of contract with respect to that instalment, the other party may declare the contract avoided with respect to that instalment. It is clear that Carl's failure to supply any chocolate is a fundamental breach of the contract and consequently, under Article 73(1) Art can avoid that instalment of the contract and claim for damages to the extent of his lost profit on the sale of the chocolate. However, Art clearly wants to bring the contract to an end completely and Article 73(2) allows for just that possibility. Under that article, where one party's failure to perform any of his obligations in respect of any instalment gives the other party good grounds to conclude that a fundamental breach of contract will occur with respect to future instalments, he may declare the contract avoided for the future, provided that he does so within a reasonable time. It is clear that Carl's failure to deliver and his statement about his uncertainty in relation to the future supply of chocolate provides Art with sufficient grounds for suspecting that future instalments will not be met as required in the original agreement. Consequently Art can avoid the contract for the future, as long as he gives Carl notice of the fact within a reasonable time.

Article 73(3) further states that a buyer, who declares the contract avoided in respect of any delivery may, at the same time, declare it avoided in respect of deliveries already made or of future deliveries if, by reason of their interdependence, those deliveries could not be used for the purpose contemplated by the parties at the time of the conclusion of the contract. This provision, however, does not apply to the facts of this situation so Art cannot avoid his liabilities in relation to the chocolates already received.

9 This question requires candidates to consider various issues relating to the issuing of shares by companies, the requirement for those shares to be paid for by shareholders and shareholders' potential liabilities for the debts of their companies.

The first issue relates to the shares taken by Gus in January. United Kingdom law requires that the capital of any company having share capital must be divided into shares of a designated and fixed amount (s.2(5)). The nominal value of the shares represents the extent of a shareholder's potential liability (*Borlands Trustees* v *Steel* (1901)).

There is, however, no requirement that companies issue shares to the full extent of their authorised capital, nor indeed is there any requirement that the company require its shareholders to immediately pay the full value of the shares.

The proportion of the nominal value of the issued capital actually paid by the shareholder is called the paid up capital. It may be the full nominal value, in which case it fulfils the shareholders responsibility to outsiders; or it can be a mere part payment, in which case the company has an outstanding claim against the shareholder. It is possible for a company to pass a resolution that it will not make a call on any unpaid capital. However, even in that situation, the unpaid element can be called upon if the company cannot pay its debts from existing assets in the event of its liquidation.

Consequently, there was nothing unlawful in the issue of the shares as partly paid up, but the remaining, unpaid, part, can always be called upon if the company requires it to pay off its debts.

The foregoing point is further strengthened by rules preventing companies from issuing shares at a discount. It is a long established rule that companies are not permitted to issue shares for a consideration that is less than the nominal value of the shares together with any premium due. The strictness of this rule may be seen in *Ooregum Gold Mining Co of India* v *Roper* (1892). In that case the shares in the company, although nominally £1, were trading at 12.5p. In an honest attempt to refinance the company, new £1 preference shares were issued and credited with 75p already paid (note the purchasers of the shares were actually paying twice the market value of the ordinary shares). When, however, the company subsequently went into insolvent liquidation the holders of the new shares were required to pay a further 75p.

The common law rule is now given statutory effect in s.100 Companies Act 1985 (CA) and is supported by s. 99 which states that shares are only treated as paid up to the extent that the company has received money or money's worth. If a company does enter into a contract to issue shares at a discount it will not be able to enforce this against the proposed allottee. However, anyone who takes shares without paying the full value, plus any premium due, is liable to pay the amount of the discount as unpaid share capital, together with interest at 5% (s.100(2)/CA 1985). Also any subsequent holder of such a share who was aware of the original underpayment will liable to make good the shortfall (s.112 CA 1985).

Applying the foregoing to Gus's situation in relation to his shareholdings in Flop Ltd he cannot avoid liability to pay up to the full value of the shares he has taken in it. Thus in relation to the first lot of shares he will be liable to pay a maximum of $2,500 (25 cents x 10,000) shares and in relation to the second lot he will be liable to pay a maximum of $5,000 (50 cents x 10,000 shares). The extent of his liability will depend on the actual debts owed but cannot exceed the nominal value of the shares.

10 Dealing in shares, on the basis of access to unpublished price sensitive information, provides the basis for what is referred to as 'insider dealing' and is governed by part V of the Criminal Justice Act 1993 (CJA).

Section 52 of the CJA sets out the three distinct offences of insider dealing:

(i) an individual is guilty of insider dealing if they have information as an insider and deal in price-affected securities on the basis of that information.

(ii) an individual who has information as an insider will also be guilty of insider dealing if they encourage another person to deal in price-affected securities in relation to that information.

(iii) an individual who has information as an insider will also be guilty of insider dealing if they disclose it to anyone other than in the proper performance of their employment, office or profession.

The CJA goes on to explain the meaning of some of the above terms as follows.

(i) Dealing is defined in s.55 CJA, amongst other things, as acquiring or disposing of securities, whether as a principal or agent, or agreeing to acquire securities. Section 52 makes it clear that only such activity in a regulated market is covered by the Act.

(ii) Inside information is defined in section 56 as:

– relating to particular securities,
– being specific or precise,
– not having been made public and
– being likely to have a significant effect on the price of the securities.

(iii) Section 57 states that a person has information as an insider only if they know it is inside information and they have it from an inside source. The section then goes on to consider what might be described as primary and secondary insiders. The first category of primary insiders covers those who get the inside information directly through either:
– being a director, employee or shareholder of an issuer of securities; or
– having access to the information by virtue of their employment, office or profession.

The second category of insiders includes those whose source, either directly or indirectly, is a primary insider, as defined above.

Applying the general law to the problem scenario, one can conclude as follows:

(i) Slye is an 'insider' as he receives inside information from his position as a director of Huge plc. The information fulfils the requirements for 'inside information' as it relates to: particular securities, the shares in Large plc; is specific, in that it relates to the takeover; has not been made public; and is likely to have a significant effect on the price of the securities. On that basis Slye is clearly guilty of an offence under s.52 when he buys the shares in Large plc.

(ii) When Slye tells his friend Mate about the likelihood of the take-over he commits the second offence of disclosing information he has as an insider. Mate then becomes an insider himself and is guilty of dealing when he buys shares in Large plc.

(iii) When Slye advises his brother Tim to buy shares in Large plc, he commits the third offence under s.52 of encouraging another person to deal in price-affected securities in relation to inside information. Tim on the other hand has committed no offence for the reason that, although he has bought shares in Large plc, he has not received any specific information and therefore cannot be guilty of dealing on the basis of such information.

1 8–10 Good explanation of the two organisations.

5–7 Sound explanation but lacking in detail or perhaps slightly unbalanced.

0–4 Weak explanation or very unbalanced in that the answer only deals with one type.

2 8–10 Good explanation of the grounds and procedure for challenging an arbitrator's appointment. Reference to the provisions of the Model Law will be expected.

5–7 Fair understanding perhaps lacking in detail or reference to the Model Law.

0–4 Very unbalanced answer or lacking any detailed explanation.

3 This question requires candidates to explain the rules relating to the concept of acceptance under the UN Convention on Contracts for the International Sale of Goods.

8–10 Good explanation of the meaning acceptance with reference to the appropriate Articles.

5–7 Fair explanation of the meaning but perhaps lacking in detail or examples.

0–4 Very unbalanced answer or lacking any detailed explanation.

4 This question requires candidates to explain the rules relating to the preservation of goods under the UN Convention on Contracts for the International Sale of Goods.

8–10 Good explanation of rules with reference to the appropriate Articles.

5–7 Fair explanation of the obligations but perhaps lacking in detail or examples.

0–4 Very unbalanced answer or lacking any detailed explanation.

5 8–10 Good to complete answer which shows a knowledge of the meaning and effect of the two types of authority. It is likely that case authority will be provided, and they will be rewarded accordingly.

5–7 Fair explanation of the two types of authority but perhaps lacking in detail, or only dealing with two types.

0–4 Some basic knowledge of what is meant by the terms, but no real depth of understanding. Perhaps an unbalanced answer that only deals with one part of the question.

6 8–10 A good treatment of all three types of meeting, probably, although not necessarily, with reference to statutory provisions.

5–7 A sound understanding of the area, although perhaps lacking in detail.

2–4 Some understanding of the area, but lacking in detail, perhaps failing to deal with one type of meeting.

0–1 Little or no knowledge of the area.

7 8–10 A good explanation of the meaning of corporate governance generally and the roles of the two types of directors in particular. Reference might well be made to the OECD or the Combined Code.

5–7 A sound understanding of the area, although perhaps lacking in detail.

2–4 Some understanding of the area, but lacking in detail, perhaps failing to deal the relationship of the two group of directors.

0–1 Little or no knowledge of the area.

8 8–10 A good analysis of the scenario with a understanding and application of the law, with detailed reference to the convention.

5–7 Some understanding of the situation but perhaps lacking in detail or reference to the convention.

0–4 Weak answer lacking in knowledge or application, with little or no reference to the convention.

9 8–10 A complete answer, highlighting and dealing with all of the issues presented in the problem scenario. It is most likely that cases and statutory provisions will be referred to, and they will be credited.

5–7 An accurate recognition of the problems inherent in the question, together with an attempt to apply the appropriate legal rules to the situation.

2–4 An ability to recognise some, although not all, of the key issues and suggest appropriate legal responses to them. A recognition of the area of law but no attempt to apply that law.

0–1 Very weak answer showing no, or very little, understanding of the question.

10 8–10 A good analysis of the scenario with a clear explanation of the law relating to the insider dealing, with detailed reference to statutory provisions.

5–7 Some understanding of the situation but perhaps lacking in detail or reference to the statutes.

0–4 Weak answer lacking in knowledge or application, with little or no reference to the statute.