

C05

Fundamentals of Ethics,
Corporate Governance and
Business Law

Syllabus outline

Ethics and Business	15%
Ethical Conflict	10%
Corporate Governance	10%
Comparison of English Law with Alternative Legal Systems	10%
The Law of Contract	20%
The Law of Employment	10%
Company Administration and Finance	25%

Exam Format & Strategy

- ▶ Where to take the exam
At an accredited CIMA CBA Centre
- ▶ When to take the exam
This will depend on the type of course
- ▶ Type of exam
Random Computer based assessment of 2 Hours duration. 75 compulsory questions, each with one or more parts.
All questions to be attempted, pass mark 50%
- ▶ How does the CBA work?
Questions are displayed on a monitor, students enter answers onto the computer. At the end of the exam the computer marks the answers automatically.

English Law and Alternative Legal Systems

Chapter 1

Criminal Law and Civil Law

- ▶ A crime is an offence against the State.

The State prosecutes a person who is accused of a crime. The object is to prove guilt, if proven beyond a reasonable doubt the accused is convicted and sentenced, if not guilty they are acquitted.

- ▶ Civil law sets out the rights and duties of persons as between themselves.

An action is brought by one person (the claimant) against another (the defendant). The object is to show liability, the burden of proof is less, a balance of probabilities.

Sources of English Law

- ▶ CASE LAW

 - custom/common law

 - Equity

- ▶ LEGISLATION:

 - ▶ Acts of Parliament

 - ▶ Delegated legislation

- ▶ EUROPEAN UNION LAW

- ▶ OTHER SOURCES:

 - ▶ Other legal jurisdictions eg USA, Australia etc

 - ▶ Academic opinion

Case law

- ▶ Based on the system of Judicial precedent
- ▶ Common law applies automatically
- ▶ Equity developed to give a fair system of law granted at the discretion of the court

Acts of Parliament

Parliament consists of:

- ▶ the House of Commons,
 - ▶ the House of Lords and
 - ▶ The Monarch.
- ▶ For a Bill to become an Act, it must pass the three readings procedure and receive Royal Assent.
 - ▶ Parliament is sovereign, in theory it can pass any law it likes.

Statutory interpretation

- ▶ Judges cannot question the validity of statutes but they can interpret the meaning of that statute.
- ▶ Judges use Aids to interpretation, rules of interpretation and presumptions to assist them in their interpretation.

Delegated Legislation

Delegated legislation is made on behalf of Parliament and consists of:

- ▶ Statutory instruments - Made by the Government Ministers using powers delegated by Parliament
- ▶ Bye-laws - Made by local authorities
- ▶ Orders in Council - made by Crown and privy Council in times of national emergency or when Parliament not sitting
- ▶ Scottish Parliament and Welsh Assembly law-making powers

European Union Law

There are several sources of EU law:

- ▶ ***The Treaties.*** The primary source: the Treaties of Paris and Rome which created the first EU bodies, and all subsequent Treaties.
- ▶ ***Regulations.*** Regulations by the Commission and Council are directly applicable, with no need for further legislation by member states.
- ▶ ***Directives.*** Directives by the Commission and Council are addressed to the member states, and require that they change their own law to comply.
- ▶ ***Decisions.*** Addressed to individuals or companies or member states but only binding on them

European Union Law

- ▶ **Recommendations.** These have no formal legal effect, but have considerable persuasive force.
- ▶ **The European Court of Justice.** It gives decisions and rulings in disputes involving EU law, and its decisions are binding on the parties themselves in the United Kingdom. They also form precedents and are influential in building up EU law.
- ▶ **The European Parliament** provides supervision and advice only to the Commission and Council of Ministers

Judicial Precedent

The system, adopted by the judges, of following previous decisions is called the doctrine of judicial precedent:

- ▶ Some precedents are binding and must be followed
- ▶ Some precedents are persuasive and may be followed

EU and Member States

- ▶ Founding treaties
- ▶ Regulations and directives
- ▶ Principal institutions:
 - European Parliament
 - Council of Ministers
 - European Commission
 - European Court of Justice

Status and Power of EU

- ▶ EU to have primacy over member states
- ▶ EU shall have legal personality to act as a single person or body
- ▶ Subsidiarity applies where member state needs EU to act to achieve an objective
- ▶ Proportionality applies where EU does no more than to achieve an objective

Judicial Precedent

- ▶ Court judgments normally comprise two elements:
 - ▶ Ratio decidendi - the legal principle for the decision based on the facts of the case; it is binding precedent
 - ▶ Obiter dicta - statements which are not part of the ratio; they are persuasive precedent only
- ▶ Binding precedents require:
 - ▶ Hierarchy of the Courts
 - ▶ Ratio decidendi
 - ▶ Same material facts

The Hierarchy of the Civil Courts

- ▶ In general, precedents of the higher courts bind the lower ones - but not vice versa.
- ▶ The House of Lords is not bound by its own precedents in exceptional circumstances, it binds all inferior courts
- ▶ The ECJ binds all English courts
- ▶ The Court of Appeal binds all inferior courts and itself (subject to exceptions)
- ▶ The High Court binds all inferior courts
- ▶ The County Court binds no-one

The Tort of Negligence

- ▶ A tort is a civil wrong by one or more persons against another. Action is brought by the person affected by wrongful conduct (the 'claimant') against the wrongdoer (the 'defendant').
- ▶ The main remedy sought is damages (financial compensation).
- ▶ Examples of torts:
 - ▶ Negligence - relevant for this syllabus
 - ▶ Nuisance
 - ▶ Trespass
 - ▶ Slander and libel

Negligence

- ▶ This occurs when one person suffers harm or loss as a result of the failure of another to exercise reasonable care.
- ▶ Elements of a successful negligence claim:
 - ▶ a duty of care is owed by one party to the other,
 - ▶ there has been breach of that duty of care (e.g. negligent act or statement), and
 - ▶ that the breach of duty led to loss or damage (e.g. property damaged, physical injury and associated financial losses) being suffered by the claimant.

Duty of Care

- ▶ There is a duty of care to take reasonable care not to cause foreseeable harm to foreseeable victims - The Neighbour principle
- ▶ The duty was established in Donoghue v Stevenson .
- ▶ The duty was extended in later cases showing how the law develops from judicial precedent eg to include economic loss (Hedley Byrne v Heller)

Limits on the duty of care

- ▶ There must be sufficient proximity between the parties, the duty cannot be owed over a limitless area or a limitless number of people (Alcock v Chief Constable of South Yorkshire Police).
- ▶ There may be public policy reasons for not applying the neighbour principle (Mulcahy v Ministry of Defence)

The breach of duty

- ▶ The claimant must prove the duty was breached by the defendant
- ▶ He must show that the facts show a breach
- ▶ He must also show that the defendant failed to take the degree of care which a reasonable man would have taken.
- ▶ The facts can speak for themselves, this is known as Res Ipsa Loquitor

Resultant loss

- ▶ The claimant must show he has suffered loss or damage as a direct consequence of the breach.
- ▶ The claimant must show a causal link between the act or omission and the damage caused.
- ▶ If the loss is caused by someone or something other than the defendant there is no action against him.
- ▶ The damage must be of a type that is reasonably foreseeable

Defences to Negligence

- ▶ Contributory negligence arises when the plaintiff has partly contributed to their own misfortune - any damages award is likely to be reduced

A partial defence

- ▶ Sayers v Harlow D C (1958)

- ▶ Volenti non fit injuria

A complete defence

Negligent Misstatement

- ▶ If advice is given or statements are negligently made, there may be liability where a duty of care is owed, it is breached and financial loss is suffered as a result:
- ▶ Hedley Byrne v Heller & Partners (1963)
- ▶ Smith v Eric S Bush (1989)
- ▶ Caparo Industries plc v Dickman (1990)
- ▶ A D T Ltd v Binder Hamlyn (1995)

Civil Court Structure

- ▶ The House of Lords (now Supreme Court)
- ▶ Court of Appeal
- ▶ High Court
- ▶ County Court

Criminal Court Structure

- ▶ The House of Lords (now Supreme Court)
- ▶ Court of Appeal
- ▶ Crown Court
- ▶ Magistrates Court

Religious Legal Systems

Sharia law

- ▶ Sharia covers social, political, religious and economic issues
 - ▶ Some laws cannot be altered as they are divinely ordained
 - ▶ Some laws can be altered as they are created by judges and lawyers and are usually attempting to interpret divine principles

Sharia law

- ▶ Primary sources of Sharia law:
 - ▶ The Qur'an
 - ▶ The Sunnah "The Way"
 - ▶ For some Muslims, the unanimity of the disciples of Muhammad on certain issues
- ▶ Secondary sources of Sharia Law:
 - ▶ Reasoning and analogy of new situations
 - ▶ Consensus of the community

Sharia law

- ▶ Different interpretation and application of Sharia law in different countries.
- ▶ Some Muslim countries have a combination of religious and secular courts
- ▶ Sharia law must be comprehensive to provide fully for spiritual and physical well-being

Sharia law

- ▶ The Five Pillars of Islam
- ▶ Obligatory
- ▶ Meritorious
- ▶ Permissible
- ▶ Reprehensible
- ▶ Forbidden

EU and Member States

- ▶ Founding treaties
- ▶ Regulations and directives
- ▶ Principal institutions:
 - ▶ European Parliament
 - ▶ Council of Ministers
 - ▶ European Commission
 - ▶ European Court of Justice

Status and Power of EU

- ▶ EU to have primacy over member states
- ▶ EU shall have legal personality to act as a single person or body
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International Legal Relations

- ▶ Public international law
- ▶ Private international law
- ▶ Vienna Convention of the law of Treaties

International Legal Relations

- ▶ Individual countries and states may be parties to international agreements
- ▶ Individual organisations may be parties to international agreements
- ▶ Uniformity of dealings helps commercial organisations and business practice

Revision questions

Define / explain:

- ▶ Injunction
- ▶ Specific performance order
- ▶ The Literal Rule
- ▶ The Golden Rule
- ▶ The Mischief Rule
- ▶ The Purposive Rule
- ▶ The Rule of Language
- ▶ Judicial precedent
- ▶ The Neighbour Principle
- ▶ Breach of duty

Revision questions

Define / explain:

- ▶ Contributory negligence

The Law of Contract

Chapter 2

Contract - Essential Elements

- ▶ Form of the contract
- ▶ The agreement
 - offer
 - acceptance
- ▶ Consideration provided by both parties
- ▶ Intention to create legal relations
- ▶ Reality of the consent (freely)
- ▶ Capacity to contract
- ▶ Legality

The Form of the Contract

- ▶ **Simple contracts** require no specific formalities to be complied with, i.e. can be oral, in writing or even by conduct
- ▶ Contracts which must be in writing (else they are void):
 - ▶ For the sale of land
 - ▶ Bills of exchange, cheques and promissory notes
 - ▶ Contracts for marine insurance
- ▶ Contracts which must be evidenced in writing:
 - ▶ Hire purchase and consumer credit agreements - unenforceable
- ▶ Contracts which must be made by deed:
 - ▶ Transfer of title to land

The Agreement - Offer

An offer is a statement of willingness to be bound on specified terms without further negotiations.

It may be made to an individual, a group or to the world at large.

- ▶ The following are not a valid offer:
 - ▶ An invitation to treat
 - ▶ Advertising jargon
 - ▶ Shop window display
 - ▶ Goods on shop shelves
 - ▶ Statement of selling price
 - ▶ Statement of future intention

Termination (End) of the Offer

An Offer ends in 3 ways:

- ▶ It is revoked before acceptance - may be express or implied revocation and must be communicated
- ▶ By rejection - may be express as in:

Routledge v Grant , Dickinson v Dodds

- may be implied by a counter offer as in:

Hyde v Wrench

- ▶ It lapses:

after a specified period of time

after a reasonable period of time if none specified

Ramsgate Victoria Hotel Co v. Montefiore (1866)

usually as a result of death of either party before acceptance

if the contract was conditional and condition not met

Validity of Acceptance

- ▶ Acceptance may be in any form
 - ▶ implied by conduct, verbal, written etc
 - ▶ Carlill v Carbolic Smoke Ball Co (1893)
- ▶ If a specified form of acceptance is required, this must be complied with.
- ▶ Acceptance must be unconditional and unqualified.
- ▶ Silence is not valid acceptance
 - ▶ Felthouse v. Bindley (1863)

Communication of Acceptance

- ▶ General rule - Acceptance must be communicated to offeror to be effective
- ▶ Exceptions -

The postal rule, acceptance is complete as soon as the letter is properly posted as long as use of the post is reasonable

The offeror may dispense with the need for communication of acceptance as in Carlill v Carbolic Smoke Ball Co

Consideration

The basic rule:

- ▶ Every simple contract must be supported by consideration from both parties.
- ▶ Contracts made by deed (specialty contracts) do not require consideration unless the terms of the agreement require it.

Consideration

- ▶ ‘Consideration is an act or forbearance (or the promise of it) on the part of one party to a contract as the price of the promise made to him by the other party to the contract’: Dunlop v Selfridge (1915) , it is the price of obtaining the other person’s promise
- ▶ It may be executed or executory
- ▶ It need not be adequate
- ▶ Consideration must be sufficient: the following are not sufficient and so not valid consideration
 - ▶ Vague promises with no monetary value - White v Bluett
 - ▶ Past consideration - Re McArdle
 - ▶ Promises to meet existing contractual or statutory obligations
 - ▶ Illegal or immoral actions

The Part Payment problem

- ▶ General Rule - Payment of a smaller sum will not discharge a debt of a greater amount - The rule in Pinnel's case
- ▶ Exceptions
 - Payment by a third party
 - Composition with creditors
 - Accord and satisfaction - D & C Builders v Rees
 - Promissory Estoppel - Central London property v High Trees House

Privity of Contract

- ▶ Normally only the two parties to a contract can enforce that contract
 - ▶ Tweddle v Atkinson (1861)
 - ▶ Dunlop Pneumatic Tyre Co v Selfridge (1915)
- ▶ Exceptions:
 - ▶ Where promise is in the form of a deed
 - ▶ The Contracts (Rights of Third parties) Act 1999
 - ▶ Third party must be identified and intention of contracting parties must be clear
 - ▶ Nissin Shipping Co Ltd v Cleaves & Co Ltd (2003)

Intention to be Legally Binding

- ▶ Commercial contracts normally presumed to be legally binding
 - ▶ Jones v Vernon's Pools (1938)
 - ▶ Rose & Frank v Crompton Bros (1925)
- ▶ Social and domestic arrangements not normally presumed to be legally binding
 - ▶ Balfour v Balfour (1919)
 - ▶ Merritt v Merritt (1970)

Misrepresentation

- ▶ Definition - a false statement of fact which has induced the other party to enter into the contract - i.e. it has been relied upon
- ▶ It may be innocent, negligent or fraudulent
- ▶ Excludes:
 - ▶ Statement of opinion
 - ▶ Statement of future conduct or intent
 - ▶ Statement of law
 - ▶ Silence - unless
 - ▶ half-truth - R v Kyslant
 - ▶ facts have changed - With v O'Flanagan (1936)
 - ▶ contracts of utmost good faith “(*uberrimae fidei*)”

Misrepresentation- Remedies

- ▶ Voidable at option of party deceived - i.e. both parties restored to their original position
- ▶ Otherwise - remedy can depend on the type of misrepresentation, innocent, fraudulent or negligent.
- ▶ Rescission is always available provided the right to rescission is not lost i.e. by a third party acquiring title
- ▶ A misrepresentation can become a term of the contract, for breach of a term the injured party has further and better remedies.

Incorporation of Terms into Contracts

EXPRESS TERMS

- ▶ Actual notice or express agreement
- ▶ Signature on a document
 - ▶ L'estrage v Graucob (1934)
- ▶ Reasonable notice
 - ▶ Olley v Marlborough Court Hotel (1949)
- ▶ Previous consistent business dealings
 - ▶ Spurling v Bradshaw (1956)

Incorporation of Terms into Contracts

IMPLIED TERMS

► Implied by statute

► Sale of Goods Act 1979

- that the seller has (or will have) the right to sell
- that the goods shall correspond with any description;
- that the bulk will correspond with any sample; and
- where the sale is made in the course of business, that the goods shall be both, of satisfactory (formerly 'merchantable') quality and reasonably fit for the required purpose if the seller has been made aware of this.

Beale v Taylor (1967)

Frost v Aylesbury Dairy Co Ltd (1905)

Incorporation of Terms into Contracts

- ▶ Unfair Contract Terms Act (1977)
- ▶ Unfair Terms in Consumer Contract Regulations (1999)
- ▶ Supply of Goods and Services Act (1982)
 - ▶ Work performed with reasonable care and skill
- ▶ Implied by court - what may reasonably have been agreed between parties

Contract Terms

- ▶ Conditions - A condition is an important term going to the root of the contract
- ▶ Warranties - A warranty is a less important term, which is incidental to the main purpose of the contract
- ▶ Innominate terms - An innominate or indeterminate term is neither a condition nor a warranty; court will need to determine by the effect of the breach

Exemption or Exclusion Clauses

- ▶ Definition - an attempt by one party to limit or exclude liability to the other under the terms of a contract
- ▶ The law provides protection to the weaker party by ;
 - Common law rules of incorporation and interpretation
 - Statutory protection - The Unfair Contract Terms Act 1977

Exemption or Exclusion Clauses

- The Misrepresentation Act 1967
- Consumer Credit Act 1974 - cannot stop debtor paying off amount due at any time and there is a prescribed procedure if in default
- Consumer Credit Act 2006 - borrowers can challenge agreements on the basis that they are unfair.

Exemption or Exclusion Clauses

-Unfair Terms in Consumer Contracts Regulations 1999

- ▶ applies to standard form contracts between businesses and consumers
- ▶ requirement to be in good faith and to be written in plain language, or will not be binding on the consumer
- ▶ does not apply to all contracts (e.g. employment contracts)

Discharge of the contract

- ▶ There are 4 ways to discharge or terminate the contract
 - Performance
 - Agreement
 - Frustration
 - Breach

Contract Performance

- ▶ Must be complete to discharge liability
 - ▶ Cutter v Powell (1795)
- ▶ Divisible or severable contracts - still only one contract, even though payment at agreed points of performance
- ▶ Substantial performance
 - ▶ Hoenig v Isaacs (1952)
 - ▶ Bolton v Mahadeva (1972)
- ▶ Prevention of performance
 - ▶ Planche v Colburn (1831)

Frustration of Contract

- ▶ Definition - occurs when a contract becomes impossible to complete due to factors outside of the control of the two parties
 - ▶ Taylor v Caldwell (1886)
 - ▶ Krell v Henry (1903) and Herne Bay Steamboat Co v Hutton (1903)
 - ▶ Avery v Bowden (1855)
- ▶ Contract is ended and sums paid recoverable subject to recovery of expenses incurred
- ▶ The Law Reform (Frustrated Contracts) Act 1943

Breach of Contract

- ▶ Definition - one party fails to fully perform their contractual obligations in the manner required by the contract:
 - ▶ Actual breach - the breach occurs on the due date for performance
 - ▶ anticipatory or repudiatory breach - may be express or implied by conduct
 - ▶ breach of condition - repudiate or damages
 - ▶ breach of warranty - damages only

Breach of Contract - Non-financial Remedies

- ▶ Rescission where the other party has repudiated the contract (for misrepresentation)
- ▶ Specific performance - court order to perform contractual obligations
- ▶ Injunction - court order not to break contractual obligations

Breach of Contract - Financial remedies

- ▶ Remedies in sale of goods contracts

- ▶ Action for the price

- ▶ Damages

- Definition - financial compensation for the loss or damage suffered as a result of the breach - not designed to be punitive

- Factors to consider:

- ▶ remoteness and causation

- ▶ measure - extra expenses incurred or foreseeable profit lost

- ▶ mitigation by claimant - unmitigated losses cannot be recovered

- ▶ contributory negligence where there is a duty of care

- ▶ liquidated damages may be allowed

The Law of Employment

Chapter 3

The Employment Relationship

- ▶ Definition - a contractual relationship to supply skill and labour to another
- ▶ Applicable law
 - ▶ The law of contract
 - ▶ Equal opportunities, anti-discrimination and health and safety legislation
 - ▶ Employment Rights Act 1996 - employee to receive written particulars of key terms as evidence of contract agreed within two months

Employees and Contractors

Tests to determine employment status:

- ▶ the control test - is employer able to control and direct the employee?
- ▶ the integration test - is the employee's work integrated into business?
- ▶ the economic reality test (or multiple test) - what is the economic reality of the relationship between employee and employer?

Employees and Contractors

- ▶ Why is the distinction important?
 - ▶ Income tax and national insurance law
 - ▶ Vicarious liability of employers
 - ▶ Statutory benefits and protection to employees only
 - ▶ Minimum wage
 - ▶ Redundancy
 - ▶ Unfair dismissal
 - ▶ Statutory Sick Pay

The Employment contract

► Sources of the employment contract

Terms expressly negotiated and agreed

Terms included by custom or collective agreement

Terms implied by the common law

Terms implied by statute

EU influence e.g. on discrimination , equal pay etc

► The E.R.A statement of particulars

Written notice of particulars to be given within 2 months of commencement

Changes to be notified within one month

Includes pay, holiday entitlement, job title etc

Implied Duties of Employers

- ▶ To pay reasonable remuneration
- ▶ Provide work, where remuneration or skill/expertise depends upon this
- ▶ Provide a reasonably safe system of work
- ▶ Reimburse employees for expenses incurred
- ▶ Behave reasonably and responsibly towards employees
- ▶ Check that employees are entitled to work and remain in the UK

There is no implied duty to provide a reference nor to provide work unless the above exceptions apply

Statutory Rights of Employees

- ▶ Sex Discrimination Acts 1975-1986
- ▶ Equal pay Act 1970
- ▶ Employment Rights Act 1996
- ▶ Employment Act 2002
- ▶ Race Relations Act 1976
- ▶ Employee has right to join/not join an independent trade union and take part in its activities

Statutory Rights of Employees

- ▶ Disability Discrimination Act 1995
- ▶ Employment Equality (Age) Regs 2006
- ▶ Time off for trade union activities
- ▶ Training as a safety representative
- ▶ Look for new work upon redundancy
- ▶ Time to perform public duties

Implied Duties of Employees

- ▶ Obey lawful and reasonable orders - not if illegal, unreasonable or dangerous
- ▶ Mutual co-operation, i.e. perform work in a reasonable manner
- ▶ Exercise reasonable care and skill
- ▶ Perform duties personally
- ▶ Act in good faith
- ▶ Loyal and faithful service
- ▶ Confidentiality - may apply after leaving

Implied Duties of Employees

- ▶ Comply with restraint of trade clauses
 - ▶ usually void, unless reasonable
 - ▶ Countrywide Assured Financial Services v Pollard (2004)
- ▶ Patent rights normally belong to the employee, but employer may claim ownership
- ▶ Copyright of written work normally belongs to the employer

Notice and Dismissal

- ▶ Employment Act 2002 contains minimum criteria of dismissal, disciplinary and grievance procedures
 - ▶ identify in writing the conduct
 - ▶ meeting between parties to identify decision
 - ▶ right of appeal, further meeting and communication

Termination by Notice

- ▶ May be until expiry of fixed term, or
- ▶ Expressly agreed in contract, or
- ▶ Reasonable notice to employee - but minimum:
 - ▶ work 1 month = 1 week notice
 - ▶ else 1 week per year = 12 weeks max
- ▶ Reasonable notice to employer - minimum of 1 week after 1 month
- ▶ Either party can waive right to notice and employee can accept payment in lieu

Summary Dismissal

- ▶ Definition - dismissal without notice for serious breach of contract
- ▶ If the breach is sufficiently serious it will not be wrongful dismissal since it will be the employee who is in breach
- ▶ Examples of such breaches might be theft from the employer or violence towards another employee

Wrongful Dismissal

- ▶ Dismissal without proper notice or justification - i.e. breach of contract
- ▶ Sue for unliquidated damages in county or high court - in lieu of wages for notice period, subject to employee mitigating losses
- ▶ Can apply to all workers
- ▶ Possible to bring action for both wrongful and unfair dismissal

Unfair Dismissal

- ▶ To claim compensation worker must qualify:
 - ▶ Must be an employee
 - ▶ Must have been employed for 1 year continuous service
 - ▶ Must apply to Tribunal within 3 months
 - ▶ Employee must show has been dismissed
- ▶ Dismissal:
 - ▶ Actual dismissal from wording used by employer
 - ▶ Constructive dismissal
 - ▶ Expiry of a fixed term contract

Unfair Dismissal

- ▶ Once employee shows he has been dismissed the law presumes the dismissal to be unfair
- ▶ The employer must show the dismissal was for one of the statutory fair reasons
 - ▶ Lack of competence and/or qualification
 - ▶ Misconduct;
 - ▶ Redundancy;
 - ▶ Contravention of a statute
 - ▶ Some other substantial reason

Unfair Dismissal

- ▶ The tribunal must decide whether, having regard to all the circumstances the employer acted reasonably in dismissing the employee:
- ▶ Must comply with statutory dismissal procedure, otherwise automatically unfair
- ▶ Some reasons are automatically unfair (Inadmissible reasons)
 - Joining/refusing to join Trade Union
 - Pregnancy or child birth or related matters
 - Unfair selection for redundancy i.e. not LIFO
 - Considerations of health and safety
 - Enforcing a statutory right or whistleblowing

Unfair Dismissal Remedies

- ▶ Basic award - depends upon age and years of service (up to a current max of £464 pw) up to max 20 years
- ▶ Compensatory award - max £76,574
- ▶ Re-instatement - same employer on same terms
- ▶ Re-engagement - same employer, but not on same terms
- ▶ Special or additional award - if employer refuses to comply with reinstatement or re-engagement or if for automatically unfair reason

Occupational Safety

- ▶ Health & Safety at Work Act 1974
 - ▶ duty on employers and employees to take all steps reasonably practicable to ensure safety of anyone/everyone on work premises
 - ▶ breach leads to criminal offence

Occupational Safety Regulations

- ▶ Employer has duty to do risk assessment of matters affecting health and safety
- ▶ Provision and use of work equipment
- ▶ Personal protective equipment
- ▶ Manual handling operations
- ▶ Display screen equipment,
- ▶ The workplace

Other Occupational Safety Duties

- ▶ Maintain records of equipment testing
- ▶ Maintain records of accidents - if serious, notify H&SE
- ▶ Set up safety committee if required to do so by union
- ▶ Take more care of vulnerable employees

Occupational Injuries

- Civil Liability

- ▶ Breach of statutory duty
- ▶ Breach of employment contract
- ▶ Negligence - duty of care owed:
 - ▶ selection, training and conduct of staff
 - ▶ Hudson v Ridge manufacturing (1957)
 - ▶ maintenance of materials, equipment etc
 - ▶ Bradford v Robinson Rentals (1967)
 - ▶ operation of a safe system of working
 - ▶ Paris v Stepney Borough Council (1951)

Company Administration

Chapter 4

Learning Objectives

- ▶ Describe the characteristics of different forms of business organisations and the implications of corporate personality;
- ▶ Explain the purpose and legal status of the articles of association;
- ▶ Explain the ability of a company to contract;
- ▶ Explain the use and procedure of board meetings and general meetings of shareholders;
- ▶ Identify the various types of shareholder resolutions.

Types of business

- ▶ Sole Trader
- ▶ Partnerships
 - ▶ The general or ordinary partnership
 - ▶ Limited partnerships
 - ▶ Limited Liability Partnerships
- ▶ Companies

Sole Trader

- ▶ Responsibility and liability
- ▶ Advantages and disadvantages
- ▶ Business name vs name of owner

The ordinary or general partnership

- ▶ Definition - an unincorporated association defined in The Partnership Act 1890 as 2 or more **persons** carrying on business **in common** with view **to profit**
 - ▶ Characteristics
 - ▶ The Partnership Agreement
 - ▶ Partnership name
 - ▶ Limited partnerships (next slide)

Limited Partnership Act 1907

- ▶ Requires one at least unlimited partner
- ▶ Must be registered at Companies House
- ▶ Limited partners have no right of management
- ▶ No power to bind the firm to contracts

The ordinary or general partnership

Authority of partners

- ▶ Agency relationship of partners
- ▶ Apparent authority
- ▶ Trading partnerships

Liability of partners

- ▶ Liability in contract?
- ▶ Holding out
- ▶ Liability in tort
- ▶ Misapplication of money or property

Which partners are liable?

The ordinary or general partnership

Dissolution of a partnership

- ▶ Without court order - automatically
- ▶ By court order
- ▶ Distribution of assets - assets pay for liabilities

The Veil of incorporation

- ▶ Separate legal entity from its owners and/or managers - veil of incorporation
 - ▶ Macaura v Northern Assurance Co Ltd (1925)
- ▶ Members have limited liability
 - ▶ Salomon v Salomon & Co Ltd (1897)
- ▶ Can sue and be sued
- ▶ Perpetual succession
- ▶ Company owns assets and incurs liabilities in own name
- ▶ Ultra vires rule (not so important since CA 06)

Lifting the Corporate Veil

BY STATUTE

- ▶ Accounts by group of related companies
- ▶ Wrongful and fraudulent trading
- ▶ Public company trading certificates
- ▶ Phoenix companies

BY THE COURTS

- ▶ To overcome fraud or sham companies
- ▶ Nationality during war
- ▶ To recognise agency relationships within corporate groups
- ▶ By EU law to apply competition controls

Limited Liability Partnership Act 2000

- ▶ Hybrid between 1890 partnership and limited liability company
- ▶ Members (i.e. partners) have limited liability
- ▶ LLP owns assets and incurs liabilities
- ▶ LLP has perpetual succession
- ▶ Formal incorporation and registration procedure with Companies House

Limited Liability Partnership Act 2000

- ▶ Annual return and audited accounts filed
- ▶ Members decide their own internal regulation and decision-making
- ▶ Members assessed for personal income tax

Types of Company

- ▶ Classification by limitation
- ▶ Public and private companies
- ▶ Holding companies
- ▶ Quoted companies
- ▶ CICs
- ▶ European companies
- ▶ Small companies
- ▶ Multinational companies

Public & Private Companies

- ▶ Name ends with plc or ltd
- ▶ Minimum issued capital of £50,000 for plc - no minimum for ltd
- ▶ Minimum paid up capital of 25% of nominal value, plus 100% of premium for plc - no minimum for ltd
- ▶ Trading certificate required by plc - not applicable for ltd

Public & Private Companies

- ▶ Minimum of 2 directors for plc - 1 for ltd
- ▶ Appropriately qualified company secretary required by plc, no secretary required for ltd
- ▶ PLC can have shares “listed” or “quoted” on a recognised exchange and offer shares to public
- ▶ More onerous regulation of plc and deregulation of ltd

Company Registration - Promoters

- ▶ Definition - as anyone taking the necessary steps to register a company and obtaining the Certificate of Incorporation
- ▶ Excludes professional advisors acting on behalf of clients
- ▶ Owe fiduciary duties (honesty, good faith etc) to the company
- ▶ If making profit, must disclose to company and members
- ▶ May be liable on pre-incorporation contracts
- ▶ Avoiding liability on pre-incorporation contracts

Company Registration

▶ Documentation

▶ The application must contain:

- proposed name
- whether members have limited liability and whether the liability is by guarantee (rare) or by shares (usual)
- whether company is private/public
- details of registered office

The Company Name

- ▶ Name must end with public limited company or plc or limited or ltd
- ▶ Cannot be the same as another registered company
- ▶ Cannot use certain names
- ▶ Certain names need consent of Secretary of State
- ▶ Passing off

The Registered Office

- ▶ Every company must have one
- ▶ It determines the company's domicile
- ▶ The postal address can be changed by notifying the Registrar
- ▶ The registered office cannot be changed

Application sent with:

- ▶ The Memorandum
- ▶ The Articles (not necessary if company adopts model articles)
- ▶ Statement of capital and initial shareholding
- ▶ Statement of proposed officers
- ▶ Statement of compliance
- ▶ Registration fee

The Memorandum of Association

- ▶ Just simple document signed by the subscribers
- ▶ Subscribers confirm they wish to form a company and if company is limited by shares that they will take at least one share each

Certificate of Incorporation

- ▶ Signed and issued by Registrar if incorporation formalities complied with
- ▶ Company exists from date on certificate which contains name, registration number and location of registered office and if public/private company
- ▶ Ltd can commence trade
- ▶ If incorporating a plc - it must also obtain a trading certificate before commencing trade (s761 CA 06)

Articles of Association

- ▶ The company's constitution consists of the Articles of Association and any resolutions or agreements that affect the constitution
- ▶ Set out way in which company is governed and regulates relationship between shareholders and company
- ▶ Can adopt model articles or prepare tailored set
- ▶ Must be printed and divided into numbered paragraphs

Alteration of the Articles

- ▶ Usually by special resolution
- ▶ Can have entrenched provisions
- ▶ Cannot be altered so as to increase members' liability to the company
- ▶ Any alteration must be bona fide for benefit of company
- ▶ Cannot conflict with CA 06
- ▶ Court can order cannot be changed if unfairly prejudicial to member
- ▶ If alteration varies class rights company must follow procedure

Effect of Articles of Association

- ▶ CA 06 s33 - bind current and future members and company in contractual relationship - in membership matters only
 - ▶ Rayfield v Hands (1958)
 - ▶ Eley v Positive Life Assurance Co (1876)
 - ▶ Pender v Lushington (1877)
 - ▶ Re New British Iron Co Limited ex parte Beckwith (1898)

Statutory Books of the Company

- ▶ Registers e.g. Register of Members
- ▶ Annual return
- ▶ Accounting records
- ▶ Annual financial statements

Corporate Capacity to Contract

- ▶ Pre-incorporation
- ▶ Possible solutions:
 - ▶ use “off-the-shelf” company
 - ▶ novation - company enter into contract after incorporation
 - ▶ assign contracts to company after incorporation
- ▶ Ultra vires
 - ▶ not so important since CA 06
 - ▶ effect of s39 CA 06) with third
 - ▶ effect of s40 CA 06) parties
 - ▶ effect of s41 CA 06 - with directors

see
Promoter

Advantages of Limited Liability Companies

- ▶ Limited liability of members
- ▶ Perpetual succession
- ▶ Right to transfer shares, subject to articles constraints
- ▶ No limit to number of members
- ▶ Company owns assets
- ▶ Grant fixed and/or floating charge as security for borrowings
- ▶ Can keep management and ownership of the company separate

Disadvantages of Limited Liability Companies

- ▶ Formal incorporation process
- ▶ Publicity and filing requirements - accounts and returns
- ▶ Administrative burden - audit requirement; statutory books and registers maintained
- ▶ Formal dissolution process
- ▶ Company must maintain capital once raised

Meetings

- ▶ Board meetings
- ▶ Members meetings

General meetings

Annual general meetings

Class meetings

Directors Board Meetings

- ▶ Board meeting - a meeting of the board of directors to decide company policy and transact business
- ▶ Decision-making normally by majority decision: Chairman may have casting vote
- ▶ May appoint MD or CE
- ▶ Can be called by any director or company secretary at reasonable notice
- ▶ If held, must record minutes
- ▶ Confidential proceedings

Annual General Meeting

- ▶ Only required to be held by public companies
- ▶ Must hold within 6 months of end of accounting reference date
- ▶ No more than 15 months between meetings
- ▶ Notice must be in writing and in accordance with Articles
- ▶ At least 21 days notice should be given

General Meeting of Members

- ▶ Any meeting other than an AGM
- ▶ Members vote upon resolutions put before the meeting, having previously received notice of agenda
- ▶ Those entitled to receive notice and attend:
 - ▶ members
 - ▶ company directors
 - ▶ company secretary
 - ▶ Auditor
- ▶ 14 days notice required

Resolutions at General Meetings

▶ Ordinary:

- ▶ simple majority of those who attend and vote in person or by proxy on show of hands, or by poll if called
- ▶ special notice to company required for:
 - ▶ removal of auditor
 - ▶ removal of director
- ▶ used for most business, the default resolution
- ▶ 14 days notice

Resolutions at General Meetings

▶ Special:

- ▶ require 14 days notice to members; exclude day of sending and day of receipt
- ▶ 75% majority of those who attend and vote, in person or by proxy, on show of hands or by poll if called
- ▶ used for major changes in the company business

Written Resolutions

- ▶ Only available for private companies
- ▶ Can be used for all general meeting resolutions except for removal of director or auditor
- ▶ Either simple or 75% majority required depending on type of business
- ▶ Members have 28 days (usually) to vote
- ▶ Copies of written resolutions should be sent to auditors

Calling a General Meeting

- ▶ Directors decide timing and location
- ▶ Identify whether AGM or GM
- ▶ Should include agenda and identify any special resolutions
- ▶ Members holding 5% of voting rights, or 100 members holding on average £100 paid-up capital, can requisition resolution for inclusion on AGM agenda
- ▶ Include right of member to appoint a proxy
- ▶ Notice can be by electronic means

Conduct at General Meeting

- ▶ Vote initially by show of hands
- ▶ Poll may be demanded by not less than 5 members, or member(s) holding 10% of paid-up capital or voting rights
- ▶ Minutes to record conduct of business and results of votes on resolutions
- ▶ Minutes to be kept and if signed by Chairman - usually prima facie evidence, unless articles state otherwise, that they are correct
- ▶ Must be a quorum present
- ▶ Proxies may be appointed

Company Finance and Management

Chapter 5

Shares and Share Capital Terminology

- ▶ The nature of shares - a bundle of rights and obligations set out in articles
- ▶ Share capital - set out in statement of capital and initial shareholding in application for registration
- ▶ Issued and allotted share capital - the type, class and number of shares held by the shareholder
- ▶ Called up - the amount the company require members to pay on shares
- ▶ Paid up - amount shareholders have paid on shares issued

Types of Shares

- ▶ Ordinary or equity shares)
) Most usual
- ▶ Preference shares)
- ▶ Deferred or founders shares - rare
- ▶ Redeemable shares
- ▶ Treasury shares - limited to public companies

Types of Shares

▶ Classes of shares

- ▶ Each class or type of shares in issue will have their own contractual rights and entitlements - they are known as class rights
- ▶ Variation of rights changes the rights attaching to a class of shares - this requires prior consent of that class of members
- ▶ Dilution of rights is the issue of additional shares of that class, thus watering down the proportionate dividend and voting rights per share, members cannot object to this

Issuing Shares

Public companies

- ▶ Need authority for directors to issue
 - ▶ by articles
 - ▶ by resolution of members

Private companies

- ▶ Directors have authority to issue unless restricted by articles
- ▶ Cannot sell shares to public

Pre-emption Rights

- ▶ CA 06 gives limited pre-emption rights to existing shareholders if ordinary shares are **issued** for cash
- ▶ Offered in proportion to existing shareholding
- ▶ Aim - to retain control of company
- ▶ Private companies have restrictions on **transfer** of shares

Methods of Issuing Shares

- ▶ Private companies cannot invite public to purchase shares
- ▶ Listing
- ▶ Prospectus
- ▶ Public offer
- ▶ Placing
- ▶ Rights issues
- ▶ Bonus issues

Payment for Shares

- ▶ Company must receive undertaking to receive at least the nominal value of a share upon issue
- ▶ Shares cannot be issued at a discount and be regarded as fully paid
- ▶ Shares may be issued at a premium to their nominal value
- ▶ Must be in money or moneys worth - cash, assets or undertaking to perform work or services
- ▶ PLC - additional rules apply

Shares Issued for Improper Purpose

- ▶ Shares must be issued to raise capital for the company, not some other collateral purpose, such as to change proportionate voting power or avert a takeover
 - ▶ Bamford v Bamford (1969)
 - ▶ Hogg v Cramphorn Ltd (1967)

Maintenance of Capital

- ▶ There are rules on maintenance of capital to prevent a company reducing its 'buffer fund' for creditors
- ▶ Shares cannot be issued at a discount
- ▶ Rules on reduction of capital
- ▶ Company cannot purchase its own shares
- ▶ Public company cannot give financial assistance for purchase of own shares
- ▶ Companies cannot hold its own shares
- ▶ Companies can only make distributions (dividends) out of profits

Rules on Reduction of Capital

- ▶ CA 06 sets out rules on reduction (s641)
- ▶ Different procedure for private/public companies
- ▶ Public
 - ▶ Special resolution
 - ▶ Application to court
 - ▶ Filing of documents
- ▶ Private
 - ▶ Special resolution
 - ▶ Solvency statement
 - ▶ Filing of documents

Acquisition of Own Shares

- ▶ Can purchase by order of Court
- ▶ Company may redeem shares subject to several criteria - see later
- ▶ Shares can be forfeited or surrendered
- ▶ Company can receive a gift of shares
- ▶ Can purchase under s690 CA 06

Redemption of Shares

- ▶ Some non-redeemable shares must remain in issue
- ▶ Redemption must be authorised by the articles and specify terms or amount for redemption plus time period
- ▶ Private company
 - ▶ Can use capital by way of pcip
 - ▶ Directors have authority to allow redemption unless articles prevent
- ▶ Public company
 - ▶ Articles must give authority
 - ▶ Can only use distributable profits or proceeds of fresh issue

Redemption of Shares

- ▶ Redemption must be for cash paid immediately and may be at a premium in excess of the nominal value
- ▶ Shares redeemed must be cancelled
- ▶ If redemption from distributable profits, then restore creditor buffer by creating Capital Redemption Reserve:
 - ▶ Dr Retained profits
 - ▶ Cr Capital Redemption Reserve
- ▶ Return must be made to Registrar within 28 days

Purchase of Own Shares

- ▶ The General rule
- ▶ CA 06 allows companies to purchase their own shares if the requisite procedure is followed
- ▶ Similar requirements as for redeeming own shares
- ▶ Finance for the purchase

How a company purchases their own Shares

- ▶ Ltd may make ‘off-market’ purchase only:
 - ▶ Off-market purchase requires special resolution with details of contract to be given to members; no time limit is required: file resolution with Registrar
- ▶ Court may order company to purchase shares under certain circumstances
- ▶ Public company may make market purchase
 - ▶ Ordinary resolution with maximum number of shares and max/min price
 - ▶ Max time limit 18 months

Financial Assistance for Purchase of Own Shares

- ▶ A private company is not restricted from giving financial assistance for purchase of own shares
- ▶ General rule - Public company may not give assistance to a third party
- ▶ Exceptions to rule
 - ▶ Principal purpose not to give financial assistance
 - ▶ Principal purpose was a larger purpose
 - ▶ Payment of dividends
 - ▶ Allotment of bonus shares
 - ▶ Loans made in the ordinary course of business
 - ▶ Loans under employee share schemes

Companies holding their own shares

- ▶ A company cannot be a member of itself so in almost all case where a company acquires its own shares it must cancel them.
- ▶ Treasury shares
- ▶ Subsidiary companies

Distributions (Dividends)

- ▶ Companies can only make dividends out of distributable profits
- ▶ Public companies must also satisfy net asset requirements
- ▶ Company should use latest audited accounts

Loan Capital

- ▶ Characteristics of loans and borrowings:
 - ▶ Loan is a contractual obligation and must be repaid, irrespective of profit/loss made by company
 - ▶ Lender may require a fixed and/or floating charge as security
 - ▶ Tax relief available on interest payments
 - ▶ Classified as a liability on the balance sheet

Debentures

- ▶ Definition - document which evidences a loan to the company; loans may be either unsecured or secured
- ▶ Fixed charge:
 - ▶ On specific, identifiable asset(s)
 - ▶ Restriction on company to deal or amend the assets without prior consent of lender
 - ▶ Charge holder has right to take possession in event of default on loan

Floating Charge

- ▶ Characteristics of a floating charge:
 - ▶ it is a charge over a class of assets of a company, present and future
 - ▶ that class is one which, in the ordinary course of the company's business, changes from time to time
 - ▶ the company may deal freely with the assets the ordinary course of its business until default when the charge crystallises on the available assets

Floating Charge

- ▶ A floating charge will crystallise on:
 - ▶ liquidation of company
 - ▶ company ceases business
 - ▶ any other circumstances which under terms of loan will cause it to crystallise
- ▶ Advantages and disadvantages of floating charges

Registration of Charges

▶ Registration of charges

- Company must maintain a register of charges as part of statutory books

- Registration of charges must be done < 21 days with Registrar, or company and officers responsible commit offence, but usually done by lender

- Charges not registered are void, but the loan remains valid as unsecured liability, charges registered late become valid from that date and subject to other claims being registered ahead

- Charges over land must also be registered with H M land registry

▶ Priority of charges

▶ Rights of debenture holders

Shares v Debentures

Shareholders

Part owner

Voting rights

Dividends only paid out of profits

Paid after assessment of tax

May vary in value

Directors usually need authority to issue

Capital paid after creditors

Debenture holders

Creditor

No voting rights

Interest must be paid even if no profits

Interest deducted before profits assessed for tax

Value is certain and fixed

No need for authority to create loan

Capital repaid first on winding up

Preferences/Transactions at an undervalue

- ▶ Companies give preferences to a creditor if that creditor is put into a better position than he should have been in a winding up
- ▶ A transaction at an undervalue is a gift or transaction in the 2 years before liquidation where the company has given greater consideration than it received

Directors

- ▶ Ltd company must have at least 1 director; plc must have minimum of 2
- ▶ Non-executive directors have no involvement in day-to-day decision-making
- ▶ Executive directors manage the company on day-to-day basis.
- ▶ Managing director (or chief executive) may be appointed by the Board to be head of day-to-day decision-making
- ▶ Shadow directors (s251 CA 06)

Appointment of Directors

- ▶ In statement of proposed officers
- ▶ Articles provide for appointment in GM with ordinary or written resolution
- ▶ By directors to appoint on a casual basis, until the next AGM when members can ratify appointment
- ▶ May be subject to eligibility criteria per articles of association
- ▶ Directors must give their signed consent and Registrar notified <14 days
- ▶ Company to update their register of directors
- ▶ Directors must be over 16 and at least one must be a natural person

Retirement of Directors

- ▶ All directors must retire at first AGM; thereafter 1/2 must retire annually
- ▶ Retiring directors may offer themselves for re-appointment
- ▶ If also a member, can use voting rights
 - ▶ Bushell v Faith (1970)
- ▶ Director may give written notice to company of retirement - either specified time period, or reasonable notice

Disqualification of Directors

- ▶ Company Directors Disqualification Act 1986 - criminal offence if continue
- ▶ Articles of association:
 - ▶ Mental patient
 - ▶ Eligibility criteria no longer complied with - shareholding/criminal conviction etc
 - ▶ Bankrupt
 - ▶ Notice of resignation or retirement
- ▶ Director may incur personal liability if continuing to hold office
- ▶ Company may still be liable if director has apparent authority

Removal of Director s168 CA 06

- ▶ Requires ordinary resolution with min 28 days special notice to company prior to meeting
- ▶ Company must notify director concerned
- ▶ Director rights:
 - ▶ Make written representations and circulate to members
 - ▶ Representations read at GM if not circulated
 - ▶ Attend and speak at GM at which vote taken
 - ▶ If also a member, can vote on resolution

Powers of Directors

- ▶ Powers are set out in the articles
- ▶ Directors are authorised to exercise all the powers of the company for any business of the company
- ▶ Directors act as a board
- ▶ The board may elect a chairman who can exercise a deciding vote
- ▶ Usually majority decisions by board

Limits and Controls over Powers of Directors

- ▶ s177 CA 06 duty of director of a company interested in a contract with the company to declare nature and extent of interest
- ▶ ss190-196 CA 06 substantial property transaction
- ▶ Long term service contracts (over 2 years)
- ▶ Loans to directors
- ▶ Other restrictions (e.g. 75% majority needed to change company name)

Authority of Directors

- ▶ The board of directors have authority as a whole
- ▶ Individual directors do not have authority unless it is given:
 - ▶ expressly
 - ▶ impliedly
 - ▶ by virtue of holding out

Duties of Directors

- ▶ To whom are duties owed?
- ▶ The Statutory Duties
 - ▶ s171 Duty to act within powers
 - ▶ s172 Duty to promote success of company
 - ▶ s173 Duty to exercise independent judgement
 - ▶ s174 Duty to exercise reasonable care, skill and diligence
 - ▶ s175 Duty to avoid conflict of interest
 - ▶ s176 Duty not to accept benefits from third parties
 - ▶ s177 Duty to declare interest in transactions
- ▶ Consequences of a breach of duty

Liability of Directors

TO SHAREHOLDERS

TO CREDITORS

- ▶ s213 IA 1985 - fraudulent trading
- ▶ s214 IA 1986 - wrongful trading

Division of Powers Between Directors and members

- ▶ Company powers exercised:
 - ▶ By members in GM by voting on resolution proposed, or by written resolution if private company
 - ▶ Members in GM may give instruction to the directors by special resolution
 - ▶ By directors in board meetings, exercising powers to run the company on a day-to-day basis
 - ▶ Some transactions taken by the board are required to be approved by members in GM

Duty of Board to Report to General Meeting

- ▶ Duty for public company to hold AGM and report annually to members with 21 days notice to members
 - ▶ Ltd to file accounts with reg < 9 months
 - ▶ Plc to file accounts with reg < 6 months
- ▶ Private companies no longer need to hold AGMs
- ▶ Quoted companies must include a “business review” in the directors’ report
- ▶ Exemption clauses for directors

Majority Rule and Minority Protection

- ▶ COMMON LAW
- ▶ The rule of the majority
- ▶ If a wrong is done to the company, it is the company who should bring the legal action - the rule in Foss v Harbottle
- ▶ The wrongful act may be ratified by the members in *GM*
- ▶ Exceptions to the rule in Foss v Harbottle

Statutory Protection for Minorities

- ▶ STATUTE
- ▶ Derivative actions ss260-269 CA 06
- ▶ Unfairly prejudicial conduct s994 CA 06
- ▶ s122 Insolvency Act, just and equitable ground
- ▶ Other statutory provisions e.g. right for 1/10 of registered members to require directors to call a GM

Personal rights of members

- ▶ s33 CA 06 - the articles are evidence of a contact between the company and members in membership-related matters
- ▶ Member can seek remedy with representative action where rights have been ignored
 - ▶ Pender v Lushington (1877)

The Company Secretary

- ▶ Definition - the senior administrative officer of the company - does not normally have executive authority
- ▶ All public limited companies are required to appoint a company secretary
- ▶ Company secretary must be qualified
 - ▶ Employed as plc secretary for 3 out of 5 previous years
 - ▶ Member of qualifying body of CIMA
 - ▶ Qualified lawyer
 - ▶ Employment in a body that appears to directors to qualify that person to act

The Company Secretary

- ▶ Appointed in statement of proposed officers
- ▶ Thereafter appointed and removed by the directors
- ▶ Must give signed consent to take position, consent deemed given if in statement of officers
- ▶ Maintain register of company secretaries

The Company Secretary

- ▶ Function and status:
 - ▶ Call board and GM at request of directors
 - ▶ Attend board and GM to take minutes of meetings
 - ▶ Maintain statutory books and registers
 - ▶ Make appropriate returns to reg
 - ▶ Has little or no executive authority, unless delegated by the directors
 - ▶ Has apparent authority to enter administrative contracts e.g. Panorama Developments Ltd v Fidelis Furnishing fabrics Ltd (1971)

Ethics and Business

Chapter 6

Why Ethics Are Important

- ▶ The nature of ethics and why Accountants should perform their work properly - it is a matter of:
 - ▶ competence; having the skills and expertise to do what is required
 - ▶ integrity; behaving in an honest manner
 - ▶ objectivity; reporting the results of any work done in an unbiased manner without any conflicts of interest

Why Ethics are important

- ▶ Legal and disciplinary frameworks:
 - ▶ Criminal law proceedings
 - ▶ Civil law
 - ▶ Employer disciplinary action
 - ▶ Professional institute disciplinary action
- ▶ Problems with legal frameworks

set the threshold for unacceptable accounting practices at too high a level so it is difficult to monitor effectively

Often only set minimum standards to achieve, not necessarily what is best or most appropriate

Why Ethics Are Important

- ▶ Consider examples where judgement and estimation may be used in the preparation of financial statements
- ▶ Selection of accounting policies such as:
 - ▶ Accruals and prepayments
 - ▶ Provisions
 - ▶ Depreciation methods
 - ▶ Inventory counting and valuation

Why Ethics Are Important

- ▶ CIMA Code of Ethics developed to assist management accountants to identify potential ethical pressures, manage those pressures and take appropriate courses of action to deal with those pressures
- ▶ As CIMA students, you should be able to identify, explain, resolve or address ethical problems

Why Ethics Are Important

- ▶ Distinguishing between morals and ethics:
 - ▶ Both are concerned with “doing the right thing”
 - ▶ Morals usually based upon personal beliefs, which could be religion-based
 - ▶ In many cases, moral and ethical codes may be identical or similar, but may also differ significantly to create a personal conflict

Why Ethics Are Important

- ▶ Moral v ethical dilemma: consider an organisation making employees redundant, whilst the directors remain in office, having received large salaries and bonus payments and other benefits
- ▶ You may consider it morally unacceptable that this is happening, but can you breach confidentiality to publicise this situation?

Why Ethics Are Important

- ▶ What can I do for the best?
 - ▶ About individual responsibility
 - ▶ About practical courses of action
 - ▶ About making choices between different courses of action
- ▶ Major ethical issues do not arise very often therefore need awareness to recognise signs at an early stage so that they can be properly considered and appropriate courses of action taken.
- ▶ CIMA's code sets out the essential attributes of the accountant, the fundamental principles of integrity, objectivity, professional competence and due care, confidentiality and professional behaviour

Control of Ethical Behaviour

▶ Criminal law

- ▶ Serious threat or offence against the public or society at law
- ▶ Regulated by Parliament and courts
- ▶ Defined by Parliament and courts
- ▶ Enforced by police and regulators
- ▶ Punishment where offence proven beyond reasonable doubt

Control of Ethical Behaviour

▶ Civil law:

- ▶ Damage or loss suffered by other(s) as a result of obligations taken on e.g. negligence or breach of contract
- ▶ Regulated by Parliament and courts
- ▶ Defined by Parliament and courts
- ▶ Enforced by claimant bringing legal action
- ▶ Compensation or court order where loss proven on balance of probabilities

Control of Ethical Behaviour

▶ Regulations:

- ▶ Provide additional details of how to operate in practice
- ▶ Regulated by Parliament, regulatory bodies and courts
- ▶ Defined by Parliament, regulatory and professional bodies and courts
- ▶ Enforced by regulatory or professional body bringing action
- ▶ Warning or admonishment, fine, suspension and expulsion where fallen short of established standards

Control of Ethical Behaviour

▶ Code of practice:

- ▶ Guidance on how to undertake tasks as a practitioner
- ▶ Regulated by regulatory and professional bodies
- ▶ Defined by regulatory and professional bodies
- ▶ Enforced by regulatory or professional body bringing action, or self-enforced
- ▶ Warning or admonishment, fine, suspension and expulsion where fallen short of established standards

Ethics in the UK Accounting Profession

- ▶ Financial Reporting Council - independent regulator for corporate reporting and governance, which includes:
 - ▶ Professional Oversight Board for Accountancy to review the regulatory activity of the professional accountancy bodies
 - ▶ Auditing Practices Board for establishing auditing and ethical standards and issue of guidance to those who do audit and assurance work

Ethics in the UK Accounting Profession

- ▶ International Federation of Accountants issued a Code of Ethics in June 2005
- ▶ The IFAC believes the following personal qualities are required to meet public and CIMA expectations
 - ▶ Reliability
 - ▶ Responsibility
 - ▶ Timeliness
 - ▶ Courtesy
 - ▶ Respect
- ▶ Ethical codes in the UK accountancy profession are ‘framework-based’ or ‘principles-based’ to provide guidance which can then be applied to the specific situation encountered

Ethics in the UK Accounting Profession

- ▶ Many employers develop their own rules or code to apply professional and ethical standards
 - ▶ often they may exceed established standards to demonstrate their application or enforcement of established standards
- ▶ Ethical codes in the UK accountancy profession are ‘frame-work based’ or ‘principles-based’ Contrast this with the ‘statute-based’ or ‘rules-based’ system in the USA (Sarbanes-Oxley Act)

Ethics and Knowing the Rules

- ▶ Could be regarded as complying with the spirit of the regulation, to achieve its purpose, rather than simply following the letter of the law to achieve formal compliance
- ▶ There is a cultural change from trust and deference to public standards and accountability, along with transparency of decisions and actions

Seven Principles of Public Life

- ▶ Applies to all publicly qualified accountants:
 - ▶ Selflessness
 - ▶ Integrity
 - ▶ Objectivity
 - ▶ Accountability
 - ▶ Openness
 - ▶ Honesty
 - ▶ Leadership

Rules-Based Approach

- ▶ Either comply with, or break rules - it can provide certainty and clarity
- ▶ What are you trying to achieve with rules - enforcement or application?
- ▶ Rules require objective enforcement, rather than interpretation and application

Framework-Based Approach

- ▶ Frameworks typically identify potential threats and safeguards to compliance
- ▶ Provides flexibility
- ▶ Enables professional to be self-policing or self-regulating, rather than being monitored by external enforcement agency
- ▶ Self-regulation requires trust, honesty and effectiveness of application
- ▶ If ineffective, the government may introduce a rules-based approach

Framework-Based Approach

- ▶ Ethical values set the cultural tone of an organisation
- ▶ Management should set the standards and adhere to them, thus setting a good example to others
- ▶ Work to reinforce cultural and behavioural expectations of how people will behave in carrying out their role

CIMA and IFAC Codes of Ethics

- ▶ IFAC Code of Ethics for Professional Accountants 2005
 - ▶ High quality ethical standards...for professional accountants around the world
- ▶ CIMA Code of Ethics for Professional Accountants 2006
 - ▶ Reflects IFAC Code
 - ▶ Applies to members and students

The Code

- ▶ Part A - general applications of the code
 - ▶ Introduction and fundamental principles
- ▶ Part B - professional accountants in public practice
 - ▶ Conflicts of interest, appointment, fees, hospitality and gifts, objectivity and independence
- ▶ Part C - professional accountants in business
 - ▶ Preparation and reporting of information, expertise and financial interests
- The code is set out in full in Appendix 1

CIMA Code of Ethics - Fundamental Principles

- ▶ Integrity
- ▶ Objectivity
- ▶ Professional competence and due care
- ▶ Confidentiality
- ▶ Professional behaviour

Personal Development and Life-long Training

- ▶ Duty to keep up to date professionally - in both technical developments and personal competencies
- ▶ One of the fundamental principles of the CIMA Code to maintain professional knowledge and skill to ensure competent service
- ▶ CIMA CPD requirement

Independence of mind and appearance

▶ Independence:

- ▶ of mind: professional judgement should not be compromised
- ▶ in appearance: identify, evaluate and address threats to independence with safeguards, rather than trying to deal with problems retrospectively

Threats and Safeguards

- ▶ Accountants should evaluate any threats to compliance with the 5 fundamental principles
 - Self interest threats
 - Self review threats
 - Advocacy threat
 - Familiarity threat
 - Intimidation threat

Safeguards

- ▶ Once a threat has been identified an accountant should consider whether any safeguards can be used to eliminate or minimise the threat.
- ▶ 2 types
 - Safeguards created by the profession
 - Safeguards in the work environment

Accountability

▶ Accountability:

- ▶ being able to explain to others actions and decisions, whether a client or employer
- ▶ CIMA is accountable in performing a public interest duty

Responsibility

▶ Social responsibility:

- ▶ this deals with the role of the accountant in the community or society
- ▶ corporate responsibility policies state the nature of the interaction between the company and its stakeholders
- ▶ companies may now prepare social or corporate responsibility reports and will contain a mix of quantitative, qualitative and narrative disclosures

Ethical Conflict

Chapter 7

Ethics, Governance, Law and Social Responsibility

- ▶ Ethical codes v legislation
 - ▶ in many cases, they will be similar or identical
 - ▶ if there is a conflict, legislation prevails
- ▶ Ethical codes v contract
 - ▶ contracts with employers, customers, suppliers etc are voluntary arrangements
 - ▶ ethical principles should be adhered to at all times
 - ▶ if conflict, should apply professional ethics, rather than comply with contract of employment, although easier said than done

Ethics, Governance, Law and Social Responsibility

- ▶ Corporate governance and responsibility
 - ▶ organisations and consumers are more aware of an ethical approach to decision-making and doing business
 - ▶ many organisations have their own values-based code of operating - they set standards and help employees understand what is required of them
 - ▶ consistency of behaviour and decision-making helps individuals and organisations

Ethics, Governance, Law and Social Responsibility

- ▶ Corporate governance and responsibility
 - ▶ Cadbury Report (1992) regards it as good practice that companies draw up codes of ethics....and to publish them internally and externally
 - ▶ governance is generally regarded as the way in which an organisation is run, with emphasis on accountability, integrity and risk management

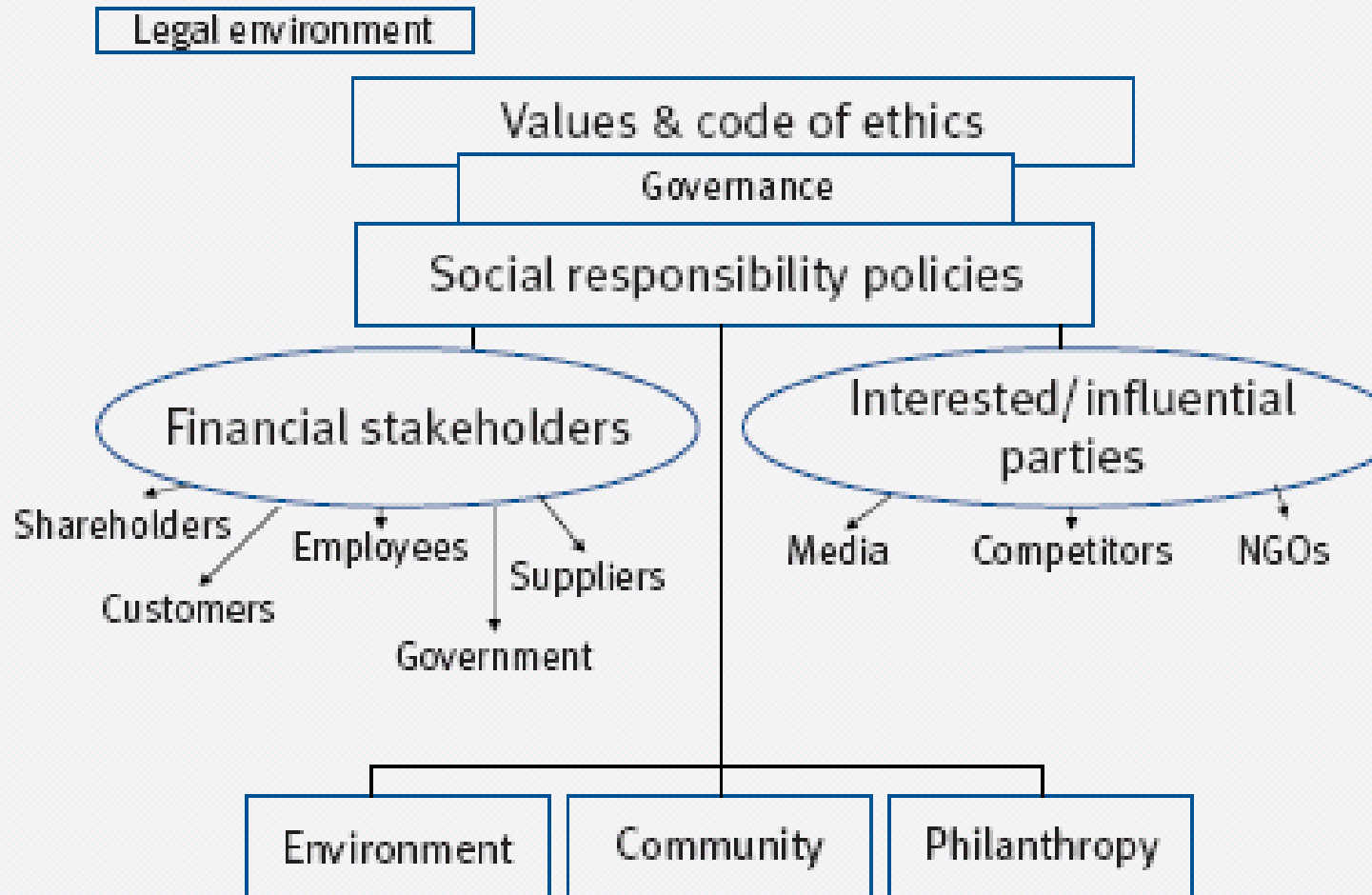
Ethics, Governance, Law and Social Responsibility

- ▶ Social responsibility - how an organisation manages its relationships in the wider community
- ▶ Typically will include:
 - ▶ potential stakeholders
 - ▶ groups to whom responsibilities may be owed
 - ▶ environmentally friendly policies
 - ▶ socially aware and responsible policies

Ethics, Governance, Law and Social Responsibility

- ▶ Types of stakeholder:
 - ▶ those with a financial-based relationship, e.g. employees, shareholders
 - ▶ those interested in the way an organisation behaves - e.g. media, activists and regulators - interest stakeholders
- ▶ All governance policies should be rooted in organisational values and code of ethics

Ethics, Governance, law and Social Responsibility



Development of an Ethics Programme

- ▶ Leadership from the top of the organisation
- ▶ Policy of consultation, information and transparency in decision-making
- ▶ Programme of training to ensure awareness and understanding of code

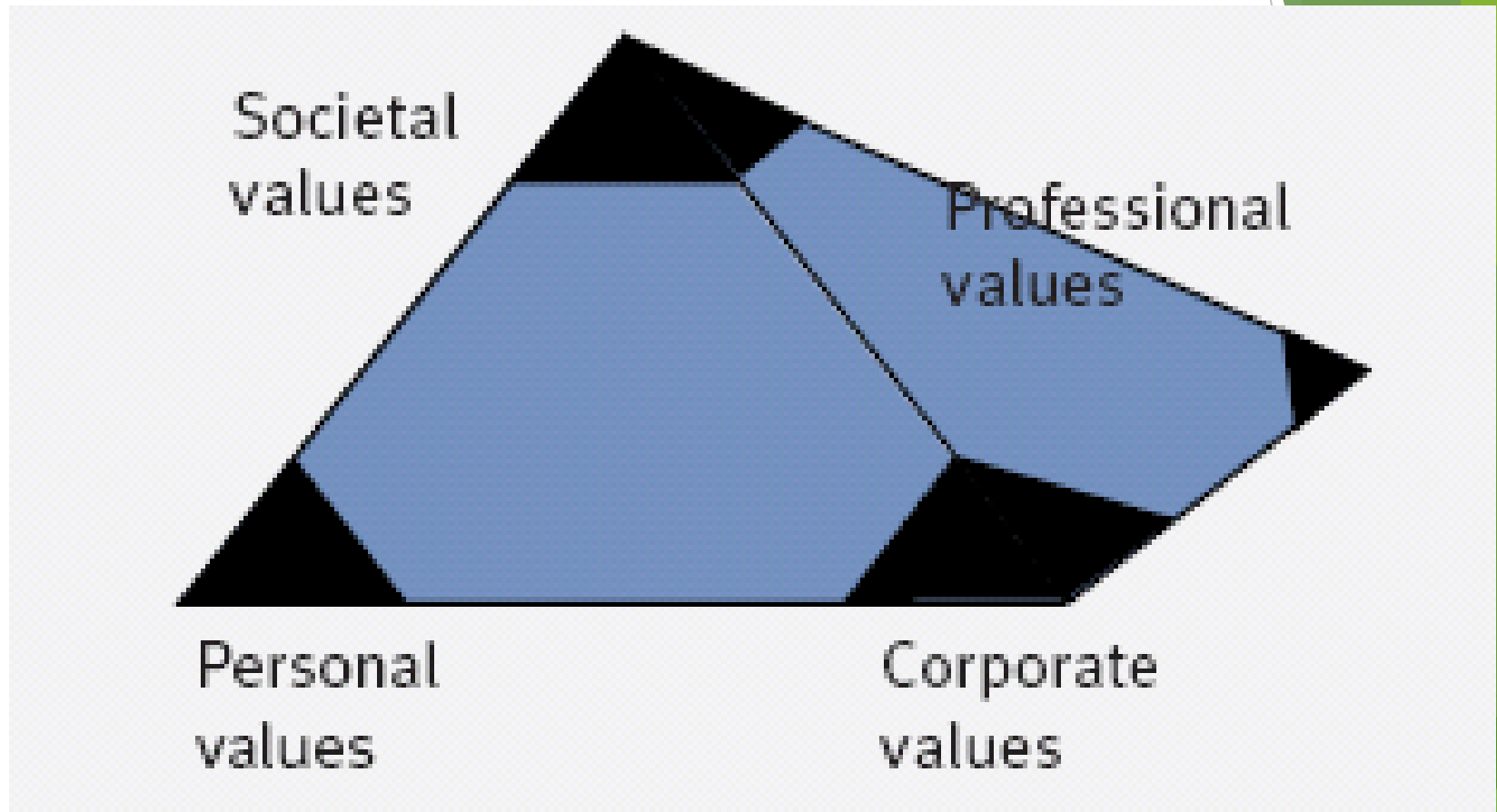
Unethical Behaviour

- ▶ Compliance with ethical codes or guides is likely to be greater when ethical behaviour is encouraged and/or when unethical behaviour is punished in some way:
 - ▶ financial penalties or consequences
 - ▶ loss of reputation and status
 - ▶ loss of personal or organisation credibility
 - ▶ trust and confidence is undermined

Ethical Dilemmas and Conflicts of Interest

- ▶ Individuals need to be able to identify ethical dilemmas and to then behave in an appropriate manner
- ▶ This requires training and awareness so that individuals act, and can be seen to act, with integrity

Identifying Ethical Dilemmas



How to Identify an Ethical Dilemma

- ▶ Individuals will have a choice over which course of action to adopt
- ▶ Compromise may be required in:
 - ▶ personal friendships and relationships
 - ▶ loyalties and affiliations to organisations
 - ▶ political beliefs
 - ▶ religious beliefs
- ▶ Use CIMA Code to gain guidance and seek solutions to ethical dilemmas

How to Identify an Ethical Dilemma

- ▶ To resolve a dilemma, a professional should always:
 - ▶ think objectively by ignoring personal preferences or choices
 - ▶ seek appropriate guidance from Code of Ethics and CIMA
 - ▶ reflect upon the situation, together with the range of possible outcomes and consequences

Managing Conflicts of Interest

- ▶ What is the ethics issue?
 - ▶ What are the options available?
 - ▶ What would you do?
-
- ▶ Ideally declare the conflict of interest for others to take over and act with integrity and objectively on behalf of the organisation

Ethical Conflict Resolution CIMA Code of Ethics

- ▶ Relevant facts
- ▶ Ethical issues involved
- ▶ Fundamental principles related to the situation
- ▶ Established internal procedures
- ▶ Alternative courses of action

Ethical Conflict Resolution CIMA Code of Ethics

▶ Possible outcomes:

- ▶ Do nothing
- ▶ Avoidance
- ▶ Change behaviour
- ▶ Arbitration, including discipline and grievance procedures

Ethical Conflict Resolution CIMA Code of Ethics

Transparency:

Do I mind who knows about my decision? Can I openly defend my stance?

Effect:

Have I identified whom the decision affects or hurts? Have I taken everything into account, including mitigating circumstances?

Fairness:

Will my decisions be judged by others to be fair?

Corporate Governance

Chapter 8

Introduction to Corporate Governance

- ▶ Focus upon public companies and corporate mismanagement, excesses and financial collapse
- ▶ Try to maintain public confidence in public companies
- ▶ Corporate governance is a dynamic, rather than static, concept

What is Corporate Governance?

- ▶ Not defined in legislation or by courts
- ▶ Cadbury Committee definition - the system by which companies are directed and controlled
- ▶ It concerns control and accountability of organisations to all stakeholders

Governance, Ethics and Company Law

- ▶ Company law includes both ethical principles and rules of behaviour for directors
- ▶ Need further ethical guidance where the law has been inadequate to modify behaviour completely:
 - ▶ may be difficult in practice to remove directors or restrict their remuneration
 - ▶ directors may be able to circumvent, without breaking, the law

Governance, Ethics and Company Law

- ▶ Increased activism by both individual and institutional shareholders in the way a company is run
- ▶ Criminal law covers some aspects of morality and ethical behaviour
- ▶ UK listed companies now subject to The Combined Code 2003

History of Corporate Governance - USA

- ▶ Separation of ownership and control of companies as they grew
- ▶ Growth of institutional shareholders who did not actively use their voting power or influence provided they received adequate returns
- ▶ Institutional funds now have legal obligation to actively manage investments on behalf of clients

History of Corporate Governance - USA

▶ Enron:

- ▶ corporate restructuring to hide borrowings off-balance sheet
- ▶ criminal convictions and civil liability for those responsible
- ▶ directors, senior executives and auditors primarily responsible - many, if not all, qualified accountants

History of Corporate Governance - USA

- ▶ Sarbanes-Oxley Act 2002
 - ▶ improved accuracy in corporate disclosure and reporting
 - ▶ extended measures to preserve auditor independence
 - ▶ personal accountability of chief executive and finance director for annual financial statements
 - ▶ Public Company Accounting Oversight Board to police audit of public companies in US

History of Corporate Governance - Europe

- ▶ EU wants to develop a common approach to fundamental governance issues by introduction and enforcement of EU Directives over time
- ▶ EU Corporate Governance Forum 2004 comprising range of stakeholders with objective to coordinate corporate governance efforts in the EU

History of Corporate Governance - UK

Piecemeal development of corporate governance UK:

- ▶ Cadbury Committee Report 1992
- ▶ Greenbury Committee Report 1995
- ▶ Hampel Committee Report 1998
- ▶ Turnbull Report 1999
- ▶ Higgs Report followed Enron corporate collapse

Directors' Behaviour and Duty of Care and Skill

- ▶ Directors' duties are now statutory
- ▶ Directors must only exercise their powers for a proper purpose
- ▶ Directors hold a fiduciary position i.e. a position of trust and confidence
- ▶ Duties are applied and interpreted using common law and equitable principles

Board Structures - UK

- ▶ Operate as a single ‘unitary’ board:
 - ▶ wholly executive - in private companies
 - ▶ majority executive - with some representation of non-executive directors
 - ▶ majority non-executive who operate a monitoring and supervisory function

- ▶ USA board structure is broadly in line with the UK

Board Structures - Europe

▶ France

- ▶ unitary board with combined role for chairman/chief executive
- ▶ unitary board with separate functions for chairman and chief executive
- ▶ two-tier board, with supervisory board containing chairman and management committee with separate chief executive
- ▶ board numbers 3-18, with 2/3 non-executive in listed companies

Board Structures - Europe

- ▶ Germany adopts a two-tier system:
 - ▶ supervisory board of min 20 members elected by partly shareholders and partly by employees
 - ▶ management board normally appointed for 5 year terms and membership controlled by the supervisory board; accountable to supervisory board for policy and strategy, profitability and compliance with law and regulation

The Role of the Board of Directors

- ▶ Combined Code states that it is to provide entrepreneurial leadership to the company within environment which assesses and manages risk
- ▶ Corporate governance includes aspects of social and environmental issues
- ▶ Compare extra costs of compliance and adherence with long term benefits of increased performance, confidence and accountability in a company

The Combined Code

- ▶ Two main principles of the Combined Code:
 - To encourage shareholders, non-executive directors and auditors to accept their legal responsibilities and scrutinise the stewardship of the company
 - To impose adequate checks and balances on executives without compromising entrepreneurship

The Combined Code

- ▶ The Combined Code is a set of principles not a set of rules
- ▶ The Combined Code applies to all companies incorporated in the UK and listed on the main market of the London Stock Exchange.
- ▶ It is divided into 4 sections:
Directors/Directors remuneration/
Accountability and audit/ Relations with
shareholders.

The key requirements of the Combined Code

- ▶ Separation of office of chairman and Chief Executive Officer.
- ▶ Recruitment of independent non-executive officers
- ▶ Effective, balanced board of directors and company secretary.
- ▶ Meaningful dialogue with shareholders
- ▶ Effective and meaningful reporting to external parties
- ▶ Creation of remuneration, nomination and audit committees.