Exam in Advanced Business Law

**Time allowed: 3 hours**

**ALL the questions are compulsory and MUST be attempted.**

**Open-ended questions**

**Question 1**

Acho, Ani and Gio entered into a limited partnership in January 2022, which was never registered with the Office of the Registrar and Official Receiver.

Acho was a general partner, while Ani and Gio were limited partners. The management of the partnership was conducted by Acho and Ani.

Ani is later declared bankrupt, and Gio writes to the other partners giving notice that he wishes to end the partnership.

*(a) Explain the effect on the partnership, if any, of Ani’s bankruptcy and Gio's letter. (4 marks)*

*(b) Explain Gio’s liability for the partnership’s debts. (8 marks)*

Temo was driving to the airport for a luxury vacation to Japan when suddenly he felt an impact from the rear of his car. Lia had accidentally bumped into him although she was driving below the speed limit.

Due to a fragile bone syndrome suffered by Temo, the slight impact resulted in several broken bones and severe pain, leading to extensive medical treatment.

Temo could not travel and missed his trip, for which he was unfortunately unable to obtain a refund.

*(c) Explain the basis of Lia’s liability to Temo. (4 marks)*

*(d) Explain whether Temo can obtain compensation from Lia for the full cost of his medical treatment. (4 marks)*

*(e) Explain whether Temo can obtain compensation from Lia for missing his trip. (5 marks)*

*(Total 25marks)*

**Question 2**

Mary has a 3-year contract to serve on the board of directors of BREEN Ltd. The shareholders of BREEN Ltd are Nora and Ako, holding 70% and 30% of its issued share capital respectively.

Nino wishes to remove Mari from the board, but Mari and Ako oppose this.

The articles of association of BREEN Ltd adopt Table A of the Companies Law Cap., but contain a special provision that no director serving under a fixed-term contract may be removed, except by special resolution.

*(a) Explain whether Nino may effect Mari’s removal as a director and, if so, the procedure to be followed.*

*(6 marks)*

*(b) Explain Mari’s rights in this situation.*

*(6 marks)*

The board of directors of MINDLtd, a private limited liability company in the manufacturing business, comprises of Benjamin, Olia and Kato.

During the liquidation of MIND Ltd it appeared that for the last six months Benjamin had been taking deposits for large orders of products, knowing that MIND Ltd would be unable to fulfil them.

Kato knew about Mamuka’s actions, whilst Olivia was oblivious.

*(a) Explain the liability of Mamuka.*

*(5 marks)*

*(b) Explain the liability of Olia.*

*(4 marks)*

*(c) Explain the liability of Kato.*

*(4 marks)*

*(Total 25 marks)*

**Question 3**

AMI Ltd is a private limited liability company which has adopted the model articles of association as per Table A of the Companies Law Cap.

The authorised share capital of AMI Ltd is GEL 10,000 divided into 10,000 shares of nominal value GEL 1 each, whilst its issued share capital is GEL 8,000 divided into 8,000 shares of nominal value GEL 1 each.

The issued share capital of AMI Ltd is held by Ana, Beno, Nato and Damien in equal proportions. The board contemplates whether to raise the amount of GEL 20,000 as loan capital or share capital.

Ana and Beno are interested in investing further in the company, whilst Nato and Gigi are not.

*(a) Explain the difference between loan capital and share capital.*

*(4 marks)*

*(b) Explain how the board of directors of AMI Ltd could implement a share issue under the circumstances.*

*(8 marks)*

Keti has been appointed external auditor of Seaside Plc. The audited financial statements for the year which ended 31 December 2022 showed that Seaside Plc made a profit of GEL 1,000,000 when they should have shown a loss of GEL 100,000. Orion was an existing shareholder of Seaside Plc, whilst Nia was not. Having seen the accounts, Nia and Bacho each bought shares in Seaside Plc which later proved to be worth much less than the purchase price.

*(c) Explain whether Nia has any rights against Keti .*

*(8 marks)*

*(d) Explain whether Bacho has any rights against Keti .*

*(5 marks)*

*(Total 25 marks)*

**Question 4**

MOON Ltd is a private limited liability company which has adopted Table A of the Companies Law Cap. 113 as its articles of association. Petre and Makho are shareholders in MOON Ltd. Petre is also appointed as non-executive director of MOON Ltd, whilst Niovie holds the position of managing director. During the liquidation of MOON Ltd, it became apparent that Niovie had been causing the company to incur further debts at a time when she knew there was no reasonable prospect of those debts being paid.

*(a) Describe the offence of fraudulent trading and explain whether Niovie is guilty of this. (7 marks)*

*(b) Explain whether Makho and Petre are guilty of fraudulent trading. (6 marks)*

Aris Ltd has an authorised share capital of GEL10,000 divided into 10,000 shares of nominal value GEL1 each, out of which 8,000 shares have been issued at a premium of GEL9 each, so that the issued share capital and share premium account of Aris Ltd are GEL8,000 and GEL72,000 respectively. In response to a decline in the company’s operating profits, the board of directors of Aris Ltd would like to reduce its authorised share capital and explore opportunities to reduce or eliminate losses amounting to the total sum of GEL50,000.

*(a) Explain how the board of directors may reduce or eliminate the losses of Aris Ltd. (8 marks)*

*(b) Explain how the board of directors may reduce Aris Ltd’s authorised share capital to GEL8,000. (4 marks)*

*(Total 25 marks)*

**Answer 1**

(a) Failure to register the partnership renders both Gio and Ani general partners and therefore Gio’s notice and Ani’s bankruptcy may each lead to dissolution of the partnership, subject to the terms of the partnership agreement.

(b) Registration of the partnership with the Office of the Registrar and Official Receiver is a statutory obligation, and the law provides for criminal and other sanctions if it is not met. One such consequence is that the limited partners lose their ‘limited’ status and are deemed to be liable for all of the partnership’s debts and obligations. Therefore, even though Gio was not involved in the management of the partnership, he will be deemed to be liable as a general partner.

(c) Lia has a general duty of care towards Temo, and her liability is to take reasonable care to avoid acts or omissions which she can reasonably foresee as likely to cause injury to another (the ‘neighbour principle’). She has fallen below this standard by bumping into Temo and so has breached her duty.

(d) The ‘thin-skull’ principle applies in this case, which provides that, in a case of negligence, the unexpected frailty of the injured person is not a valid defence to the seriousness of any injury caused to them. Therefore, the fact that Temo had a fragile bone syndrome is not a defence to Lia for the extent of the injury suffered by him as a result of her bumping into his car. Lia would, therefore, be liable to cover Temo’s medical treatment, even if it was more extensive than would reasonably have been foreseeable as a result of the impact.

(e) The rule of remoteness of damage may apply in the case of potential compensation for Temo’s trip. Lia can argue that this type of harm (i.e. missing his luxury vacation to Japan, for which no refund would be available) was not a reasonably foreseeable consequence of Lia bumping into his car, and thus she will not be liable to compensate him for this loss.

**Answer 2**

(a) Under the terms of the Companies Law, a company may, by ordinary resolution, remove a director before expiration of his/her period of office, notwithstanding anything in its articles or in any agreement between it and him/her. Therefore, neither the special provision in the articles nor the three-year contract which Marihas with BREEN Ltd is a bar to her removal from office. A simple majority of the members of BREEN Ltd present and voting at the meeting will suffice for passing the ordinary resolution for Mary’s removal. So Ako’s objection, by itself, will be of no effect. Under the Companies Law, an ordinary resolution for Mary’s removal must be passed, of which special notice is required.

(b) Mariis entitled to be heard at the meeting at which the motion for her removal will be considered. Marican also make representations to the company concerning the motion and the company is bound to circulate her representations to every member of BREEN Ltd unless received too late. If Mary’s representations are received too late, Marimay require that the representations shall be read out at the meeting. Finally, even if Mariis removed from office before the expiration of her three-year period, she will be allowed to claim compensation or damages in respect of the termination of her appointment as director.

(c) Mamuka was knowingly party to the carrying on of the business of MIND Ltd with intent to defraud the company’s creditors, given that he was taking deposits for orders knowing that the company would be unable to deliver. Therefore, Mamuka was clearly involved in fraudulent trading and thus may face criminal liability and may be subject to imprisonment and/or a fine. At the same time, the court may order him liable to make such contribution to MIND Ltd’s assets as it thinks fit.

(d) Given that Olia was not party to the fraudulent trading in any way, she will have no personal liability by reason of Mamuka’s actions.

(e) The issue whether Kato has any liability for fraudulent action is questionable and depends on whether her knowledge of Mamuka’s actions and perhaps tolerance of it actually amount to her participation in the carrying on of the business in a fraudulent manner. If so, then she will also be personally liable for all or any debts or liabilities of MIND Ltd.

**Answer 3**

(a) The share capital of a company connotes the value of the assets contributed to the company by those who subscribe for its shares. The term ‘loan capital’ is in fact a commercial expression and not a legal term, and it means the long-term loans granted to the company.

(b) The authorised share capital of AMI Ltd is GEL 10,000 whilst its issued share capital is GEL 8,000. In order to increase its authorised share capital, AMI Ltd would require an ordinary resolution of members, i.e. approval by 50% + 1 votes. Thus, if Nato and Gigi decide to participate in the company’s general meeting, which may be held to approve, if deemed appropriate, a proposed resolution to increase the company’s authorised share capital, the resolution will not pass. Hence the board of directors of AMI Ltd may proceed to issue the available 2,000 new shares of nominal value GEL 1 each, and this would only require a board approval. The board may decide to issue such new shares at a premium, e.g. GEL 9 each, and on a full subscription to the shareholders which would give rise to GEL 20,000.

(c) This question turns on whether Nia can bring an action against Keti alleging, for example, that the accounts were inaccurate and misleading so that Seaside Plc was overvalued and that she had purchased shares in Seaside Plc in reliance to the accuracy of the accounts and had suffered a substantial loss as a result. However, the auditor of a public company does not owe a duty of care to the public at large, or to potential investors; rather, the auditor’s duty is a duty owed to the body of shareholders as a whole. Moreover, there is no evidence of any special or sufficiently close relationship between Nia and Keti which could give rise to a duty of care, therefore under the circumstances, it appears that even if Keti was negligent, Nia could not file a claim against her for her personal losses. (d) Keti ’s duty of care as company auditor is owed to the company’s shareholders as a body, and not to individual shareholders wishing to increase their participation who relied on the audit report in deciding to invest. Therefore, the position explained in part (b) above does not change in relation to Bacho , even though he had already been a shareholder in Seaside Plc.

**Answer 4.**

(a) If a company is in the course of liquidation and it appears that any of its business has been carried on with the intention to defraud the creditors of the company, then the court may declare that any persons who were knowingly parties to the fraudulent trading to be personally liable for all or any debts of the company. Niovie’s actions are a clear example off fraudulent trading, where dishonest intention may properly be inferred.

(b) Raymond cannot be made personally liable for the debts of Moon Plc simply by virtue of his shareholding, unless it can be shown that he took part in making or instructed management decisions which were intended to defraud the creditors or known to be likely to cause them loss. Petre is not only a shareholder but also a non-executive director of Moon Plc. However, unless Petre was also party to the fraudulent trading, he will have no personal liability by reason of Niovie’s actions. Petre’ potential liability does not depend on whether he is an executive or non-executive director but rather to what extent he took an active role and participated in the fraudulent trading

(c) A company may, if so authorised by its articles of association and subject to confirmation by the court, by special resolution notified to the Registrar of Companies and published in the official gazette in accordance with the provisions of the Companies Law, reduce its share capital by cancelling paid up share capital for the purpose of writing off losses of the company. The provisions of the Companies Law relating to the reduction of the share capital of a company apply to the share premium account as if it were paid up share capital of the company. Therefore, the company’s share premium account can be reduced from GEL 72,000 to GEL 22,000 by the procedure outlined above, for the purpose of writing off the losses of the company which equal GEL 50,000.

(d) The company may, by ordinary resolution, cancel the 2,000 shares of nominal value GEL 1 each, which have not yet been issued, and reduce the amount of its share capital by GEL 2,000, being the amount of the shares so cancelled.