

ICSA Qualifying Programme

Company Law

Sample mark scheme 2019

SAMPLE

Section A

Question number	Answer	Mark
1	B – Creation of a floating charge	
Total		(1)

Question number	Answer	Mark
2	<p>Yes – directors can decline to register a share transfer, but only where:</p> <ul style="list-style-type: none"> • they are granted this power in the articles (1); and • they provide reasons within 2 months (s.771). (1) <p>Reward correct responses even where s.771 is not cited.</p> <p>Accept “where the shares are certificated and a proper instrument of transfer is not received by the company”</p> <p>Accept “if the agreement to transfer shares is tainted by illegality”</p> <p>Accept “if the transferee does not have the capacity to hold shares”</p>	
Total		(2)

Question number	Answer	Mark
3	<p>A person has information as an insider if, and only if:</p> <ul style="list-style-type: none"> • they know that it is inside information (1) and • they know that they have it, from an inside source (1). <p>Reward other valid responses</p>	
Total		(2)

Question number	Answer	Mark
4	False – only quoted companies are required to prepare a directors’ remuneration report.	
Total		(1)

Question number	Answer	Mark
5	<p>The steps are:</p> <ul style="list-style-type: none"> • Pass a special resolution (1). • Deliver form RR01 (plus accompanying documents) to Companies House (1). • Comply with the minimum capital requirement (1). <p>Accept "Complete form RR01" Accept "File form RR01" Reward other valid responses.</p>	
Total		(3)

Question number	Answer	Mark
6	<p>Up to 5 marks from the following:</p> <p>Any member of the company may inspect the register free of charge (1) and anyone else may inspect it on payment of a fee (1).</p> <p>Inspection requests should state the reason for the inspection. If this is not included it should be sought by the company (1).</p> <p>The company must either comply with the request or seek permission from the Court to refuse it (1). Permission to refuse inspection will only be given where the request is not made for a proper purpose (1). If the Court agrees the request is not for a proper purpose it will make an order directing the company to refuse it (1).</p> <p>Reward other valid responses.</p>	
Total		(5)

Question number	Answer	Mark
7	<p>Award up to 5 marks from the following:</p> <ul style="list-style-type: none"> • The petition for winding up is a remedy of last resort (1). • It will generally not be approved where an alternative remedy is available (1). • The definition of "just and equitable" is very wide, giving the Court wide discretion (1). • Examples of situations where winding up has been deemed appropriate include where the company is set up for a fraudulent purpose (1), where the company is deadlocked (1) or where its objects become impossible (1). • The key importance of s.122(1)(g) is to companies which are quasi-partnerships (see e.g. Ebrahimi v Westbourne Galleries) (1). <p>Answers need not make reference to all the examples above. Reward other valid responses.</p>	
Total		(5)

Question number	Answer	Mark
8	<p>Award up to 6 marks from the following:</p> <p>A disqualification order is a court order (1) which provides that for a specified period (1) the disqualified person must not:</p> <ul style="list-style-type: none"> • be a director of a company (1) or be involved in any way with the formation, promotion or management of a company (1), unless they have the permission of the court (1) • act as a receiver of the company's property (1), unless they have the permission of the court • act as a company secretary (1) • act as an insolvency practitioner (1) <p>Reward other valid responses.</p>	
Total		(6)

Section B

Question number	Indicative content
<p>9 25 marks</p>	<p>Answers should evaluate the validity of Alina and Mary's actions and so should primarily focus on the validity of the issue and allotment of shares, the potential breaches by the directors' of their duties and the unlawful payment of the dividend.</p> <p>Answers could include the following content:</p> <p>Allotment of shares</p> <ul style="list-style-type: none"> • Swan is a private limited company with only one class of share so the directors will have the authority to allot shares, subject to any restriction in the articles (s.550 Companies Act 2006). • However, the issue of new shares will dilute the holdings of the existing members (in fact this is the reason for the issue), so any new shares should first be offered to the existing members in proportion to their existing shareholding in accordance with the rules on pre-emption rights set out in s.561. • It appears that the pre-emption provisions have been breached, so although the allotment is valid, Alina and Mary will be liable to compensate any shareholders who have lost out. <p>Directors' duties</p> <ul style="list-style-type: none"> • Alina and Mary have a duty to exercise their powers only for the purposes for which they were conferred (s.171(b)). • If they have exercised the power to allot shares for the purpose of diluting Shaun's shareholding and preventing him from voting them out of office, this amounts to a breach of the s.171(b) duty. • Where directors act for multiple purposes, the duty can still be breached if the dominant purpose was an improper one. • Mary may be in breach of the duties in s.173 (independent judgement) and s.174 (duty to exercise reasonable care, skill and diligence) by going along with the proposal to pay a dividend without question. • Alina and Mary are also likely in breach of the general duty in s.172. The duty requires directors to act in good faith to promote the success of the company for the benefit of its members as a whole. Answers may query whether the good faith duty has been discharged. If the allotment was made for a purpose other than to promote the success of the company, this may also amount to a breach. Section 172(1) also requires directors to have regard to the interests of various stakeholders, the long term consequences of decisions and the company's reputation for high standards of business conduct. Arguably these aspects of the duty have also been breached. <p>Payment of dividend</p> <ul style="list-style-type: none"> • The Model Articles permit dividends to be paid following a recommendation by the board and a declaration by the company made by an ordinary resolution. There is no evidence on the facts of a board meeting having taken place. Alina, Mary and Timothy have enough shares between them to pass an ordinary resolution declaring the dividend, but if the proper procedure has not been followed, the process for declaration does not comply with Model Articles.

	<ul style="list-style-type: none"> • The key issue is that dividends may only be paid out of profits available for the purpose (s.830), which are defined as are the company's accumulated, realised profits, less its accumulated realised losses. • As Swan has no distributable reserves, it appears that the dividend has been paid out of capital. • Because the distribution is unlawful, Alina and Mary will be personally liable to repay the money distributed to Swan Ltd (<i>Re Exchange Banking Co, Flitcroft's Case</i>). The members can also be liable if they knew, or had reasonable grounds for believing, that the dividend was made unlawfully (CA 2006, s 847).
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Level	Mark	Descriptor
	0	No rewardable material.
Level 1 (Fail)	1-12	<ul style="list-style-type: none"> • The answer may attempt to explain the definitions of key terms such as allotment of shares, directors' duties and dividends, but these are likely to be unclear and not explained in full. • The answer demonstrates limited understanding of the legal issues arising. This is communicated in a basic way with simple or generalised statements. • Points made are superficial and not directly linked to the scenario in the question. • There is little application of relevant knowledge and understanding to the scenario • The answer includes limited critical analysis of the facts • Any analysis is not used to make a judgement/draw conclusions and is not supported by examples or sources.
Level 2 (Pass)	13-16	<ul style="list-style-type: none"> • The answer includes the definitions of key terms such as allotment of shares, directors' duties and dividends. • The answer demonstrates understanding of the legal issues arising and expresses ideas with clarity. • Points made are relevant and linked to the scenario in the question. • There is application of relevant knowledge and understanding to the scenario • The answer includes analysis of the facts. • Analysis is used to make a good judgement/draw conclusions, supported by examples.
Level 3 (Merit/distinction)	17-25	<ul style="list-style-type: none"> • The answer includes a clear definition of key terms such as allotment of shares, directors' duties and dividends. • The answer demonstrates a deeper understanding of the legal issues arising and these are communicated in a logical writing structure. • A range of points made are relevant and linked to the scenario in the question. • There is a good application of relevant knowledge and understanding to the scenario • The answer includes good analysis of the facts. • Analysis is used to make a clear judgement/draw conclusions and supports this with examples.

Question number	Indicative content
10 (a) 10 marks	<p>The first part of the answer should briefly explain the meaning of corporate personality and then discuss when the veil of incorporation has been lifted at common law, with reference to relevant cases. Answers in both parts should not be penalised for being overly descriptive; an answer which is largely descriptive or narrative may still achieve a pass grade under the criteria below. In order to merit higher marks, there should be an attempt at evaluation, critique or analysis of the case law.</p> <p>Answers could include the following content:</p> <p>Corporate personality</p> <ul style="list-style-type: none"> • Corporate personality refers to the fact that in law, a company has a legal personality separate from that of its founders and members. As such it has many of the same rights and attributes as natural persons. A company can own property, enter into contracts, borrow money, employ staff, sue and be sued in its own right. • The significance of the company's separate legal personality is explored in <i>Salomon v Salomon [1897]</i>. The House of Lords judgment in that case strongly upholds the clear separation between the company and its personnel, re-stating that directors and members are not liable for the debts of the company beyond their original capital contribution. Thus, corporate personality (also called the corporate veil) can be used to shield the company's personnel from liabilities incurred by the company. • Trading via a corporation with a separate legal personality is appealing because it protects the company's directors from acquiring legal responsibility for the company's debts and other liabilities. However, it is also open to abuse. The courts therefore have the power to disregard corporate personality at common law (also called lifting the veil of corporate personality). Historically however they have been reluctant to dismantle corporations which have been properly set up in accordance with the law. <p>Development of the rules on piercing the veil</p> <p>Instances where the corporate veil has been pierced include the following.</p> <ul style="list-style-type: none"> • The company is being used as a vehicle to effect a fraud, or as a façade or sham as in <i>Gifford Motor Home Co v Horne [1933]</i>. • Where an agency relationship existed between a parent company and its subsidiary such as <i>Smith Stone and Knight Ltd v Birmingham Corporation [1939]</i>.

Level	Mark	Descriptor
	0	No rewardable material.
Level 1 (Fail)	1-4	<ul style="list-style-type: none"> • The answer may attempt to explain the definitions of corporate personality and disregarding corporate personality/piercing the veil, but these are likely to be unclear and not explained in full. • The answer demonstrates limited understanding of the legal issues arising. This is communicated in a basic way with simple or generalised statements. • There is little application of relevant knowledge and understanding which is

		<p>not supported by an evaluative statement</p> <ul style="list-style-type: none"> • The answer includes limited critical analysis of the issues surrounding corporate personality • Any analysis is not used to make a judgement/draw conclusions and is not supported by relevant examples or sources.
Level 2 (Pass)	5-6	<ul style="list-style-type: none"> • The answer includes the definitions of key terms such as corporate personality and disregarding corporate personality/piercing the veil. • The answer demonstrates understanding of the legal issues arising and expresses ideas with clarity. • There is application of relevant knowledge and understanding but supported by a limited evaluative statement • The answer includes critical analysis of the issues surrounding corporate personality • The analysis is used to make a judgement/draw conclusions.
Level 3 (Merit/distinction)	7-10	<ul style="list-style-type: none"> • The answer includes a clear and accurate definition of key terms such as corporate personality and disregarding corporate personality/piercing the veil. • The answer demonstrates a good understanding of the legal issues arising and these are communicated in a logical writing structure. • There is a good or excellent application of relevant knowledge and understanding supported by an evaluative statement. • The answer includes good or excellent analysis of the issues. • The analysis is used to make a clear judgement/draw conclusions and supports this with examples or primary sources.

Question number	Indicative content
10 (b) 15 marks	<p>A narrative/descriptive answer should receive a pass mark provided it is accurate and complete. Higher marks (Level 3) should be awarded where there is an attempt at analysis, critique or evaluation.</p> <p>Answers could include the following content:</p> <p>The judgment in <i>Prest</i></p> <ul style="list-style-type: none"> The leading current authority on piercing the veil is that of the Supreme Court in <i>Petrodel Resources Ltd v Prest</i> [2013]. The case concerns the distribution of assets in a divorce settlement and as the court found that the assets concerned were held on trust for the claimant spouse, there was no need for the court to pierce the corporate veil in this case. However the judgment does contain clear guidelines (albeit <i>obiter</i>) on when a company's corporate personality may be disregarded. The guidelines are very restrictive. Lord Sumption explains that the only instance when the courts can disregard a company's corporate personality is where the 'evasion principle' applies. This is where "a person is under an existing legal obligation or liability or subject to an existing legal restriction which he deliberately evades or whose enforcement he deliberately frustrates by interposing a company under his control". He also explains that piercing the veil is a remedy of last resort and should not be used unless no other means exists to reach the required outcome. Although the Justices in <i>Prest</i> were not unanimous in their views on disregarding corporate personality, subsequent decisions such as that in <i>Wood v Baker</i> [2015] indicate that the restrictive approach endorsed by Lord Sumption is likely to be followed in the future.

Level	Mark	Descriptor
	0	No rewardable material.
Level 1 (Fail)	1-7	<ul style="list-style-type: none"> The answer may attempt to explain the judgment, but this is likely to be unclear and inaccurate. The answer demonstrates limited understanding of the legal issues arising. This is communicated in a basic way with simple or generalised statements. There is little application of relevant knowledge and understanding and the answer is largely descriptive. The answer includes limited critical analysis of the issues surrounding corporate personality. Any analysis is not used to draw conclusions and is not supported by relevant examples or sources.
Level 2 (Pass)	8-9	<ul style="list-style-type: none"> The answer includes a sufficient explanation of the judgment. The answer demonstrates understanding of the legal issues arising and expresses ideas with clarity. There is application of relevant knowledge and understanding. The answer includes critical analysis of the issues surrounding corporate

		<p>personality.</p> <ul style="list-style-type: none"> • The analysis is used to draw conclusions and examples given.
Level 3 (Merit/Distinction)	10-15	<ul style="list-style-type: none"> • The answer includes a clear, accurate and comprehensive explanation of the judgment • The answer demonstrates a good understanding of the legal issues arising and these are communicated in a logical writing structure. • There is a good application of relevant knowledge and understanding supported by an evaluative statement. • The answer includes good critical analysis of the issues. • The analysis is used to draw conclusions and supports this with examples or primary sources.

Question number	Indicative content
11 (a) 17 marks	<p>In order to bring a successful claim, Mercy must first establish that James has breached one or more of his duties as a director. Directors owe their duties to the company, so she must then satisfy the statutory tests to gain permission to bring a derivative claim on the company's behalf. Answers should deal briefly with directors duties before turning to concentrate on the statutory process for bringing a claim.</p> <p>Answers could include the following content:</p> <p>Directors' duties</p> <p>There are several potential breaches of duty here.</p> <ul style="list-style-type: none"> • s.171 – James has breached this duty by acting outside his powers and/or using his powers for improper purposes. • s.175 – James has breached the duty to avoid conflicts of interest. This duty is applied very strictly. This is clear from the caselaw (e.g. <i>Bhullar v Bhullar</i>). • Conflicts of interest may be authorised, but on the facts, the other director was unaware of the transaction; if the conflict had been disclosed, the board would have the option of authorising it which would absolve James. • s.172 – James is not acting in good faith, and is in breach of the general duty to promote the success of the company for the benefit of the members as a whole. <p>The derivative claim</p> <ul style="list-style-type: none"> • The statutory derivative claim is available under the Companies Act 2006. The claim does not overrule the rule in <i>Foss v Harbottle</i> but it does allow shareholders to bring a claim on the company's behalf, subject to the strict criteria set out in s.260. • The grounds for a claim are set out in s.260(3). A claim may only be brought where there is negligence, default, breach of duty or breach of trust by a director. Applying this to the facts, there are several breaches here which could potentially justify a claim. • Under s.261(1), Mercy can apply for permission to bring a claim if she can demonstrate that there is a prima facie case. As she is a member and has prima facie evidence of breaches of duty by James, she is likely to satisfy this test. • The court must refuse permission to proceed with the claim if any of the conditions in s.263(2) are satisfied, namely if a hypothetical director acting in accordance with s.172 would not seek to continue it, or that the act complained of has been authorised by the company. On the facts the claim appears to be in the company's best interests. • Finally the court has discretion to refuse to allow the claim to continue under s.263(3) and (4). The Act directs the court to consider certain specific factors (e.g. cost and likelihood of recovering compensation) and also to have regard to the views of the members. Here, the views of Michael will be relevant – if he agrees the claim should go ahead, this will make the court more likely to grant permission. • In general, the courts have been reluctant to grant permission for derivative claims to proceed – see cases such as <i>Franbar Holdings v Patel</i> and <i>Mission Capita v Sinclair</i>.

Level	Mark	Descriptor
	0	No rewardable material.
Level 1 (Fail)	1-8	<ul style="list-style-type: none"> • The answer may attempt to define the derivative claim, but this may be unclear and not explained in full. • The answer demonstrates limited understanding of the relevant process. This is communicated in a basic way with simple or generalised statements. • There is little application of relevant knowledge and understanding.
Level 2 (Pass)	9-10	<ul style="list-style-type: none"> • The answer includes sufficient definition of the derivative claim. • The answer demonstrates understanding of the relevant process and expresses ideas with clarity. • There is application of relevant knowledge and understanding.
Level 3 (Merit/Distinction)	11-17	<ul style="list-style-type: none"> • The answer includes a clear definition of the derivative claim including reference to primary sources. • The answer demonstrates a good understanding of the relevant process and this is communicated in a logical writing structure. • There is a good application of relevant knowledge and understanding.

Question number	Indicative content
11(b) 8 marks	<p>The question requires discussion of what ratification is and whether it is applicable here, and if so, the likely consequences.</p> <p>Answers could include the following content:</p> <p>Ratification</p> <ul style="list-style-type: none"> • Ratification means approval or authorisation of an action taken by a director. Ratification takes place after the unauthorised act has been completed. • Members can usually ratify an act in breach of duty by a director via a resolution of the company. James owns 60% of the company's shares, which in theory means he could pass an ordinary resolution alone. However, see bullet point 5 below. • The effect of ratification is usually to absolve the director from a breach of duty in respect of the ratified act. • In respect of the derivative claim, the Court must refuse permission to continue a claim where the act or omission which is the basis of the claim has been authorised by the company (s.263(2)). If James's actions were to be ratified then the effect would be to bring the derivative claim to an end. • However, although many breaches of duty are capable of ratification, s.239 prevents shareholders voting on a resolution to ratify their own actions as directors, so James could not vote to ratify his own acts. Michael and Mercy own 30% and 10% of the company's shares, so if James cannot vote then Michael has more than 50% of the remaining voting shares. However, it is unlikely on the facts that Michael or Mercy would agree with James's actions. • In addition, dishonest acts can not generally be ratified (<i>Goldtrail Travel Ltd v Aydin</i>). The transfer to Avocado could also give rise to criminal liability. • Therefore, applying this to the facts, James's breaches of duty are not capable of ratification and the derivative claim will be unaffected.

Level	Mark	Descriptor
	0	No rewardable material.
Level 1 (Fail)	1-3	<ul style="list-style-type: none"> • The answer may attempt to define ratification, but this is likely to be unclear and not explained in full. • The answer demonstrates little or nounderstanding of the legal issues arising. This is communicated in a basic way with simple or generalised statements. • Points made are superficial and not directly linked to the scenario in the question. • There is little application of relevant knowledge and understanding.
Level 2 (Pass)	4-5	<ul style="list-style-type: none"> • The answer includes the definition of ratification. • The answer demonstrates understanding of the legal issues arising and expresses ideas with clarity. • Points made are relevant and linked to the scenario in the question. • There is application of relevant knowledge and understanding.

Level 3 (Merit/Distinction)	6-8	<ul style="list-style-type: none">• The answer includes a clear definition of ratification including reference to primary sources.• The answer demonstrates a good understanding of the legal issues arising and these are communicated in a logical writing structure.• A range of points made are relevant and linked to the scenario in the question.• There is a good application of relevant knowledge and understanding.
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Question number	Indicative content
12 25 marks	<p>The question requires candidates to discuss the course of action the liquidator will take. Answers should therefore begin by explaining the role of the liquidator, which is to collect the assets of the company, convert them into cash and use the resulting funds to pay the company's debts. Fenella must then distribute any remaining assets to those entitled to them in a statutorily prescribed order.</p> <p>Answers could include the following content:</p> <p>Fenella must consider how to ensure she has increased the pool of assets as far as possible, and then decide how to distribute them.</p> <p>Collecting assets</p> <ul style="list-style-type: none"> • Fenella will start by collecting all the company's cash and non-cash assets including plant and machinery, vehicles, stock etc. • She should also look to see whether she can increase the size of the asset pool by requiring anyone to make a contribution to the company's assets. • Directors may be required to repay any assets wrongly distributed prior to the liquidation. • In this case answers should consider wrongful trading and the creation of a preference. <p>Wrongful trading</p> <ul style="list-style-type: none"> • Wrongful trading occurs where the company has gone into insolvent liquidation, and at some time before the commencement of the winding up, a director knew or ought to have known that there was no reasonable prospect of avoiding insolvent liquidation (s.214 IA 1986). • The fact that the company continued to trade whilst technically insolvent does not automatically mean that wrongful trading has occurred; the question is whether the directors knew there was no reasonable prospect of avoiding insolvent liquidation. • On the facts, the auditor's advice in January 2018 appears to indicate that they ought to have known liquidation was inevitable. • If Desi and Ethan have engaged in wrongful trading, they can be required to make a contribution to the company's assets as the court thinks proper. <p>Creation of a preference</p> <ul style="list-style-type: none"> • A preference is created where a company does or allows something to be done which has the effect of putting a creditor, surety or guarantor in a better position which, in the event of an insolvent liquidation, they would otherwise have been in (s.239 IA 1986). • Where the creditor is a connected person (such as a director), preferences will be unlawful if created up to 2 years prior to the liquidation. • The repayment of the loan to Ethan therefore appears to be a preference. • Fenella can apply to the court for an order restoring the company to the position it would have been in had the preference not been made (e.g. compelling Ethan to repay the £10,000).

Distribution of assets

Answers should explain the order of distribution, as follows

- Liquidation expenses, £5,000, are repaid first.
- Preferential creditors are repaid next. The unpaid wages are preferential debts, but note that only the first £800 per employee will be classed as preferential. The remainder will rank as unsecured debt.
- Unsecured creditors are then repaid. This will include the balance of the £50,000 owed to the employees as well as any trading debts e.g. amounts owed to suppliers. Answers should note that the unpaid tax bill of £25,000 ranks as an unsecured debt. If there are not sufficient assets to pay all unsecured debtors in full then the pari passu rule applies which means the funds are shared so that all will receive an equal proportion of the money owed to them.
- Finally if there are any assets left, they may be distributed to the members. However, given that the company's assets were £70,000 and its debts exceed this (see below) amount, it is unlikely that the members will receive anything at all, even if the preference is repaid.
- £5000 in liquidation expenses
 £50,000 in wages (£800 per head ranking as preferential)
 £25,000 in tax
 = £80,000 in liabilities plus any additional trading debts not specifically mentioned
- Therefore even if the £10,000 preference is recovered there will be insufficient assets to return anything to the members.

Level	Mark	Descriptor
	0	No rewardable material.
Level 1 (Fail)	1-12	<ul style="list-style-type: none"> • A few legal issues are identified but are not directly linked to the scenario and are accompanied by little detail. • The answer demonstrates little or nounderstanding of the insolvency regime. This is communicated in a basic way with simple or generalised statements. • Points made are superficial and not directly linked to the scenario in the question • Any analysis is not used to make a judgement and is not supported by examples
Level 2 (Pass)	13-16	<ul style="list-style-type: none"> • Legal issues are identified which are relevant to the scenario and described in detail. • The answer demonstrates understanding of the insolvency regime and expresses ideas with clarity. • Points made are relevant and linked to the scenario in the question • The analysis is used to make a judgement and is supported by examples.
Level 3 (Merit/Distinction)	17-25	<ul style="list-style-type: none"> • A range of legal issues are clearly identified, the majority of which are linked to the scenario and described in some detail. • The answer demonstrates a good understanding of insolvency regime and is communicated in a logical writing structure with supporting examples. • A range of points made are relevant and linked to the scenario in the

		<p>question</p> <ul style="list-style-type: none">• The analysis is used to make a clear judgement and supports this with examples
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