

Coursework Assignment: Business Law

Your Grandmother discovers that you are taking a business law course and offers you £50,000 to set up a business of your choice

- a.) Before handing over the money she wants to know what form of business you would choose AND WHY.
 - b.) Having run her own business from her village for many years she wants to be sure that you understand the benefits and drawbacks of using agents.
 - c.) She started her first business whilst the Sale of Goods Act 1893 was in force but she wants an assurance that you are aware of the main conditions laid down in the Sale of Goods Act 1979. She needs you to show her BRIEF case examples of how some of these apply in practice.
- Draft a reply of 2000 words divided into THREE parts which could satisfy your grandmother that it would be reasonably safe to set you up in business..

Dear Grandma:

Thank you very much for offering to loan me 50,000 pounds to set up a business of my choice and I will certainly be pleased to answer the questions you have posed to me.

Firstly, you wish to know what kind of business I propose to set up. I have given a great deal of thought to this and my conclusions are that setting up a private limited Company, with a few shareholders to start off with would be the best option for me to choose. The Company could be incorporated in accordance with Articles in the Table A form, as allowed for under the Companies Act of 1985. This would provide an incentive for other shareholders to invest in the Company because the extent of their individual liabilities will be limited to the amounts left unpaid on their shares. This limited liability aspect has been deemed beneficial for the improved efficiency of the securities markets.¹ Later on, as the Company grows and expands, I could consider issuing shares in the public market and transforming the Company into a public limited Company.

¹ Ramsay IM and Noakes DB, 2001. Piercing the corporate veil in Australia 19 Company and Securities law Journal 250, at p 254 at pp 252-253

There are some advantages in setting up a private limited Company as opposed to a partnership. Berle and Means point out that with the growing size of corporations, ownership and management have been separated,² however in a partnership, the owners become fully liable for the Company's debts. The case of *Solomon v Salomon & Co Ltd*³ established the corporation as a distinct legal entity in common law, with an existence and personality separate from the people that comprise it. There is also the facility provided to a corporation for fundraising by selling shares to outside investors. The corporate body as an entity is impersonal and individuals may function in different capacities within an organization⁴, with their financial activities being shielded from the public eye, by virtue of the corporate veil. The corporate veil has been zealously guarded thus far, since the facility of limited liability available to a corporation has been deemed fundamental in the propagation of a capitalist economy.⁵ This has provided the facility for small agencies and businesses to assume a corporate form, directed towards raising capital for risky business purposes⁶. The corporation as a legal entity propagates itself and individuals associated with it are able to be exempted from liability for the debts of the Company; similarly, if one shareholder becomes bankrupt, Company assets cannot be used to pay those debts, since Company assets belong to the corporation as a separate legal person.

² See generally, Berle, Adolf A and Means, Gardiner C, 1968. The Modern Corporation and Private Property Harvest, USA, 1968 (Revised ed).

³ *Solomon v Salomon & Co Ltd* (1897) AC 22; also see *Hamilton v Whitehead* (1888) 14 ACLR 493

⁴ Watson, S, 2002. Who hides behind the corporate veil? Finding a way out of "the legal quagmire" 20 *Company and Law Securities Journal* 198 at p 202

⁵ Watson, S, *Ibid*, note 4, at p 201

⁶ Villalta G, "A Two-Edged Sword: Salomon and the Separate Legal Entity Doctrine" (2000) 7(3) *Murdoch University Electronic Journal of Law*, at p 5, [online] available at: http://www.murdoch.edu.au/elaw/issues/v7n3/puig73a_text.html

As you may note from the above, setting up a business as a private limited company in this manner will enable the company and its shareholders to enjoy all the benefits of a corporation, without liability for Company debts. Moreover, the facility of raising funds through public issue of shares will provide excellent grounds for I also propose to have a small Board of Directors with about three individuals on the Board. Justice Plowman in the case of *Parke v Daily News Ltd*⁷ held that the primary duty of the directors of a corporation is to their shareholders, superseding their duty to their employees.

The Directors are the principal agents of the Company but under the law, have been held to be subject to the same standards of loyalty and good faith in his duties as that expected from trustees,⁸ hence they owe a fiduciary duty to shareholders. In the case of *Re Dunham and Co*, the Court found that the director has been guilty of “considerable negligence” yet held that he had not breached his duty of diligence and care.⁹ However the duty of skill of a Director was best laid out by Romer J in the *Re City Equitable Fire Insurance Co Ltd*¹⁰ where he stated that while a Director was expected to exercise a certain level of skill and diligence that an ordinary reasonable man would apply under the circumstances, this did not mean that he was required to demonstrate a level of skill that was not commensurate with his experience. As you can imagine, this will enable our Company, as a new venture starting out with inexperienced directors, to have some leeway in operations without too stringent a degree of legal liability being imposed upon us. A director’s most important duties are therefore his fiduciary duties to the Company.

⁷ *Parke v Daily News Ltd* (1962) 1 Ch 927 at 962-3

⁸ For example, see *Re Lands Allotment Co* [1894] 1 Ch 616 at 631 and *Great Eastern Railway Co. v. Turner* (1872) 8 Ch App 149 at 152 per Lord Selborne.

⁹ *Re Dunham and Co* (1883) 25 Ch D 752 at 766

¹⁰ *Re City Equitable Fire Insurance Co Ltd* (1925) 1 Ch 407

But in view of changing community standards, the Courts have also moved to require more of directors, such as for example in the case of *Re Australian Venezolana Pty Ltd*¹¹ where it was held that directors were expected to make reasonable efforts to acquaint themselves with Company affairs. In the case of complicated situations where technical or expert knowledge is required, directors are now expected to seek and procure such expert advice in the interest of the shareholders of the Company, failing which they can be held guilty of a breach of duty of care and skill under the law¹². Farrar lays out three principal duties owed by the directors to the Company:

(a) Directors have a bona fide duty to act in the company's interest and must not exercise their powers for a collateral purpose.

(b) A director who profits as a result of his position as Director of a company is liable to account for such profits

(c) In a situation where the director's duty to the company conflicts with his personal interests, then any contract that arises in such a situation may be annulled by the Company.¹³ The duties of the director to the company are set out under in the Companies Act, which imposes a duty upon the directors to look out for the interests of the company and its employees as well as its shareholders.¹⁴ Therefore, I believe that we can gain the best legal advantage by starting off as a private limited company with myself being one of the Directors to maintain the required degree of control over Company activities.

You also wanted to be sure that I understand the benefits and drawbacks of using agents in performing duties for the company. According to Halsbury, the word agency is

¹¹ *Re Australian Venezolana Pty Ltd* (1962) 4 FLR 60 at 66.

¹² *In Re Duomatic Ltd* [1969] 2 Ch 365

¹³ Farrar, J.H, Hannigan, B.M, 1998. Farrar's Company Law, London Edinburgh and Dublin: Butterworths, pp 378

¹⁴ See Section 307 of the Companies Act of 1985

used to “connote the relation which exists when one person has an authority or capacity to create legal relations between a person occupying the position of principal and third parties.”¹⁵ If the acts of the agent are outside the express powers conferred by the principal, then the latter may not be held liable. For example in the case of *International Harvester Co v Carrigans*¹⁶ Carrigan purchased a faulty hay baler from agents of International Harvester Co. Since the agents went into liquidation, Carrigan tried to recover from the principal but it was held by the courts that no contractual relationship arose between the Company and Carrigan.

However, a different ruling was given by the courts in the case of *Freeman & Lockyear (A Firm) v Buckhurst Park Properties (Mangal) Ltd.*¹⁷ One of the directors of the defendant Company entered into a contract with the plaintiff architect company as an agent. But on the issue of non payment of fees, the architect Company sued the Buckhurst Company rather than the agent. The Court held that since the agent was authorized to act in relation to the Company’s business and appeared to be doing so with its full knowledge, therefore the Company was liable.

I fully understand the distinction between these two cases. Through the use of an agent, a corporation can often escape a legal, contractual relationship with a customer, as the agent assumes the responsibility for a product within a particular area¹⁸ and unless there is clear written consent given by the corporation with extent of responsibilities and authority clearly spelt out, the corporation may escape liability for an

¹⁵ Halsbury’s Laws of England, 4th edn, Vol I, para 701

¹⁶ *International Harvester Co v Carrigans* (1958) 100 CLR 644

¹⁷ *Freeman & Lockyear (A Firm) v Buckhurst Park Properties (Mangal) Ltd* (1964) 2 QB 480

¹⁸ *International Harvester Co v Carrigans* , Ibid note 16, at 653

agent's actions.¹⁹ Any breach of duty by an agent can also be held in favor of a principal corporation for recovery of damages²⁰ and non payment of commissions.²¹ Thus, a corporation has the facility of exerting full control over a subsidiary in its operations while escaping legal liability through the separate identify of a corporation from its members. Therefore, on this basis, we will judiciously use agents in marketing and promoting our Company's products; however we will be careful to negotiate agreements with them whereby they will be provided a degree of autonomy in their operations, so that our Company is not held liable for any damages that may arise out of their negligence or mishandling of goods and services, while at the same time, we can gain the benefit of using their services as independent contractors.

The third aspect you were concerned about is the Sale of Goods Act of 1982 and the changes that have been included within the scope of the Act. I am fully aware that some implied terms are included within every contractual agreement, even if they are not so spelt out. Section 14(2) of the Sale of Goods Act of 1979 includes an implicit provision about the quality of goods supplied. Section 14(3) implies that the seller is supplying goods that are reasonably fit for the purpose they are being supplied for²² and if not, the seller could be guilty of misrepresentation²³. According to Section 15, the material supplied is to be free from defects. Section 13 of the Sale of Goods Act also implies that where a supplier is carrying out a service it will be done with reasonable care and skill. Section 14 provides that where a specific time has not been agreed to by the

¹⁹ Alliance Acceptance Company Ltd v Oakley (1987) 48 SASR 337; also see Adams v Cape Industries plc (1990) – case report in Griffin, Stephen. Company law – Fundamental principles at p 12

²⁰ Christoforides v Terry (1924) All ER Rep 815

²¹ Christoforides, Ibid note 20 at 820

²² see the case of Keeley v Guy McDonald Ltd [1984] NLJ 134

²³ See the case of Oscar Chess v Williams [1957] 1 WLR 370, dealing with misrepresentation in description of product

parties and set out in the contract, then the service is to be carried out within a reasonable time frame.

The requirement for quality for example, would not be eschewed even in the case of a cheaper product. Dixon J proposed the “relevance of the price” test for a product as being one where a buyer “fully acquainted with the facts and therefore knowing what hidden defects exist...would buy them without abatement in the price....”²⁴ The terms of the contract must be adhered to strictly. For example, in the case of *Re Moore and Landauer*²⁵ there was an agreement of sale for 3000 tins of fruit packed in 30 tins. However the delivered consignment contained only 24 tins though the total number of fruit tins was still 3000 and the buyer was able to reject the entire consignment on grounds of breach of Section 13 of the SOGA, which states that delivered goods must correspond with their contractual description. In the case of *Reardon Smith v Hansen Tangen*²⁶, Lord Diplock clearly highlighted grounds that could exist for breach of contract through lack of identification of the goods being purchased:

“Ultimately the test is whether the buyer could fairly and reasonably refuse to accept the physical goods proffered to him on the ground that their failure to correspond with that part of what was said about them in the contract makes them goods of a different kind from those he had agreed to buy.”²⁷

Moreover, when selling products which could be dangerous, There is a reasonable duty of care that is expected from D-I-Y, based on the principle laid out in

²⁴ Dixon J in the case of *Henry Kendall & Sons v William Lillico & Sons Ltd* [1969] 2 AC 31, adopted from *Grant v Australian Knitting Mills* [1936] AC 100

²⁵ *Re Moore and Landauer* (1921) 2 KB 519

²⁶ *Reardon Smith v Hansen Tangen* (1976) 1 WLR 989 HL

²⁷ *Ibid*, n.26

*Donaghue v Stevenson*²⁸ that reasonable care must be taken to avoid injury to other persons. According to Lord Dunedin in the case of *Dominion Natural gas Co Ltd v Collins and Perkins*²⁹, when a dangerous product is involved, there is

“a peculiar duty to take precaution imposed upon those who send forth or install such articles when it is necessarily the case that other parties will come within their proximity.”³⁰ Otherwise, the product can be said to be defective – the kind of defect that could have been prevented with reasonable care by manufacturer of the product.

Manufacturers have been held liable for defective products when the defect arises due to the lack of care of the manufacturer³¹ or supplier of the product.

As a result, I believe that our Company must exercise care in manufacture and marketing of its products, taking into account all the terms that will be implied into contracts with customers under the statutory requirements of the Sale of Goods Act of 1982. I hope that the above will allay your concerns about the extent of my knowledge on the issues you have raised, Grandma and I look forward eagerly to your response and further action.

2055 words

²⁸ *Donaghue v Stevenson* [1932] AC 562

²⁹ *Dominion Natural gas Co Ltd v Collins and Perkins* (1909) 640

³⁰ *Dominion*, *Ibid*, n.29 at 646

³¹ *Kirby v Burke* (1944) IR 207

Bibliography

Books/Journal Articles:

- * Berle, Adolf A and Means, Gardiner C, 1968. The Modern Corporation and Private Property Harvest, USA, 1968 (Revised ed).
- * Farrar, J.H, Hannigan, B.M, 1998. Farrar's Company Law, London Edinburgh and Dublin: Butterworths, pp 378
- * Halsbury's Laws of England, 4th edn, Vol I, para 701
- * Ramsay IM and Noakes DB, 2001. Piercing the corporate veil in Australia 19 *Company and Securities law Journal* 250, at p 254 at pp 252-253
- * Villalta G, "A Two-Edged Sword: Salomon and the Separate Legal Entity Doctrine" (2000) 7(3) *Murdoch University Electronic Journal of Law*, at p 5, [online] available at: http://www.murdoch.edu.au/elaw/issues/v7n3/puig73a_text.html
- * Watson, S, 2002. Who hides behind the corporate veil? Finding a way out of "the legal quagmire" 20 *Company and Law Securities Journal* 198

Cases cited:

- * Alliance Acceptance Company Ltd v Oakley (1987) 48 SASR 337
- * Adams v Cape Industries plc (1990) – case report in Griffin, Stephen. "Company law – Fundamental principles" at p 12

- * *Christoforides v Terry* (1924) All ER Rep 815
- * *Donaghue v Stevenson* [1932] AC 562
- * *Freeman & Lockyear (A Firm) v Buckhurst Park Properties (Mangal) Ltd* (1964) 2 QB 480
- * *Great Eastern Railway Co. v. Turner* (1872) 8 Ch App 149
- * *Henry Kendall & Sons v William Lillico & Sons Ltd* [1969] 2 AC 31, adopted from *Grant v Australian Knitting Mills* [1936] AC 100
- * *International Harvester Co v Carrigans* (1958) 100 CLR 644
- * *Keeley v Guy McDonald Ltd* [1984] NLJ 134
- * *Kirby v Burke* (1944) IR 207
- * *Oscar Chess v Williams* [1957] 1 WLR 370
- * *Parke v Daily News Ltd* (1962) 1 Ch 927 at 962-3
- * *Reardon Smith v Hansen Tangen* (1976) 1 WLR 989 HL
- * *Re Australian Venezolana Pty Ltd* (1962) 4 FLR 60 at 66.
- * *Re City Equitable Fire Insurance Co Ltd* (1925) 1 Ch 407
- * *Re Duomatic Ltd* [1969] 2 Ch 365
- * *Re Dunham and Co* (1883) 25 Ch D 752 at 766
- * *Re Lands Allotment Co* [1894] 1 Ch 616 at
- * *Re Moore and Landauer* (1921) 2 KB 519
- * *Solomon v Salomon & Co Ltd* (1897) AC 22; also see *Hamilton v Whitehead* (1988) 14 ACLR 493

Legislation cited:

- * Companies Act of 1985
- * Sale of Goods Act of 1982

