

**PCLL Conversion Examination
January 2018
Examiner's Comments
Business Associations**

General comments

The standard of papers in this sitting of the Business Associations Conversion Examination was, overall, average, with many candidates incapable of providing coherent legal analysis.

As examiners, we expect candidates to be able to identify the legal issues in questions. Then they should identify the law that is relevant to the issues. They should also ask what the law means for their clients or advisees base on the facts as set out in the questions. The examination questions are designed to resemble as closely as possible what candidates may come across in practice.

Most Candidates finished the paper. I will now give some comments on how candidates answered each question. I will also describe where they did well and where they did less well.

Question 1

Almost everybody identified that the question was about directors' duties. Those candidates who did well for this question were able to subdivide the question into three separate legal issues relating to directors' duties. On the issue of delegation of director's duty, candidates who gave good answers not only pinpointed the relevant cases and statutory provisions, but were also able to point out that both Mark and Tom are professionals, they are therefore judged by a higher standard given their level of knowledge and they also discussed whether the delegation to Amy was reasonable given Amy's professional knowledge. Yet those who gave average or below average answers did not identify the relevant statutory provision (Section 465(2)) of the Companies Ordinance regarding the objective and subjective tests and nor did they discuss how or why the professions of the relevant parties are related to their level of liabilities.

On the issue of the no conflict rule, those candidates who did well were able to identify the relevant statutory provision relating to disclosure of material interests by the relevant director, and how this kind of contract becomes voidable merely by existence of such conflict based on case law. However, those who did relatively poorly simply mentioned that this was a conflict of interest but did not go on to elaborate their answers with reference to cases and statutory provision.

On the issue of using corporate information to make profit, candidates who did well were able to identify most of the relevant case laws and used those principles well to elaborate their analysis of the facts. A few even mentioned that if found liable, the company can hold the director accountable for the amount of profit made as a constructive trustee. Yet those who gave average answers did not provide coherent legal analysis with reference to relevant case laws. Some of those who answered poorly did not even identify or discuss this issue and jumped straight to the point that shareholders may resort derivative action.

Question 2

Most candidates identified that the question was about the articles of association and its enforceability. Those who did well for this question were able to differentiate members and outsiders of the company. Good answers pointed out that as an outsider, Tony Chan, cannot enforce the terms of the article of association just as the rule of privity applies by referring to the relevant cases. Yet those candidates who did relatively poorly did not discuss this issue adequately, with a few of them unable to even spot this issue.

On the issue regarding the enforceability of the articles amongst shareholders themselves, candidates with good answers cited the relevant statutory provision and case law to support their arguments and how this is related to the factual problem. Yet those who gave poor answer simply mentioned that Angel can enforce the term against Debbie and Olivia based on “fairness”, which has never been the legal test. Some candidates mentioned that the term is enforceable between shareholders but did not cite the relevant statutory provision and case law to support their arguments.

On the issue relating to the alteration of articles, some candidates failed to identify this in the answer and were not discussed at all. Those who gave average or below average answers did identify the issue but argued that shareholders could resort to unfair prejudicial remedy to challenge the validity of the alteration. Although this may be relevant yet not the gist of the answer. Those who answered well for this part were able to cite the relevant statutory provision and explained that a company may by special resolution alter or add to its articles, providing that the power to alter is exercised “bona fide for the benefit of the company as a whole” (Section 88(2) Companies Ordinance) and supported its argument with reference to case law (*Sidebottom v. Kershaw*).

Question 3

Almost everybody who attempted this question identified the principle of majority rule laid down in *Foss v. Harbottle* and how court is traditionally reluctant to interfere in the internal management affairs of the company.

Those candidates who gave good answers were able to cite the relevant statutory provisions of statutory derivative action and unfair prejudicial remedy and discussed thoroughly the conditions which the court would grant leave by making reference to the relevant case laws. Those who did exceptionally well for this question were able to distinguish the different approach the court treats public and private companies. Good answers mentioned that courts are more likely to intervene in the case of private companies with regards to oppression on minority shareholders based on the principle of “legitimate expectation” and that a private company is perceived to be a “de-facto partnership”. Some mentioned that courts could consider “just and equitable winding up” as a possible remedy.

Yet those candidates who gave relatively poor answers simply cited the relevant statutory provisions and cases without further elaborating on the legal analysis and what courts would consider in determining whether to intervene or grant leave for the action to proceed. For

example, is there a serious question to be tried or is there an arguable case? These are the type of questions a legal practitioner should be asking when advising its clients as to whether there is a legitimate claim.

A few exceptional candidates discussed the latest development in *Yuchuan & Others v. Shanshui Investment company*, where the CFI granted leave to the minority shareholders of Shanshui Investment to bring unfair prejudice proceedings in the name of the company by way of statutory derivative action pursuant to sections 732 and 733 of the Companies Ordinance.

Question 4

Most candidates who attempted the question were able to point out that the relevant statute is the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap 32). However, many of the answers failed to discuss the relevant statutory provisions and cases adequately.

In relation to the payment to TA by Daida, very few candidates cited the relevance of the validation order under section 182. Some candidates did mention the case of *Chevalier (HK) Ltd v Joint Liquidators of Right Time Construction Co Ltd* but failed to discuss its relevance to the factual problem.

On payment to Five Star, only a few candidates mentioned that the transaction could constitute unfair preference in the light of Cap 32 ss. 266 – 266D. Exceptional candidates mentioned that the new unfair preference provisions came into effect on 13 February 2017. Yet the overall legal analysis of this part was relatively weak by those who attempted this question.

Very few candidates discussed whether David could be considered as an “associate” by virtue of sections 265B or 256C.

Almost no candidate mentioned the relevance of *Re Gray's Inn* with regards to the dealing with the bank. Perhaps one or two candidates cited the Court of Appeal's judgment in *Super Speed Ltd (in liq) v Bank of Baroda* with regards to the issue of bank loan to support their arguments.

Overall, the majority of those who attempted this question did relatively poorly without referring to the relevant statutory provisions and case laws to support their answers.