

School of Accounting and Commercial Law

**COML 204 The Law of Organisations**

**Trimester Two, 2020**

**Take Home Test Instructions:**

* The test is comprised of **Three Questions**, which total 100 marks. All questions are compulsory. It is worth 30% of your final grade. The suggestion word limit for each question is stated at the end of the question, although the stated word limits are a guide only. It is recommended that Question One and Two be answered as a short essay and ILAC structure is used for Question Three.
* **Please answer the three questions in a word document (or similar),** with your name on the front page. You have 24-hours to complete this test from 6 pm on Monday 21st September. You must upload and submit your answer via the Turnitin link in Test/Quiz folder in Blackboard by 6 pm on Tuesday 22nd September 2020.
* A reminder that when you upload your assignment, you need to click to submit the document and then click to confirm submission. You will receive an automated email confirming submission (sent to your myvuw email address).
* Five percent of the total mark will automatically be deducted if this deadline is missed and a further five percent per day will be deducted for each subsequent day that the test is late. No marks will be awarded to any test submitted after the marking guide has been released or after ten days have elapsed, whichever occurs first.
* As this is a test, it is expected that you will complete it on your own. This means:

* + No collaboration or consultation with classmates or anyone else. All answers will be checked for similarity using Turnitin software.
  + The tutors and lecturer are not able to answer questions.
* Although this is a take home test rather than a full assignment, it is good to get into the habit of accurate and correct referencing. You may use either Law style footnotes or APA style references in your answer.
* **Guide to using Law style footnotes:**

Law references tend to be in footnotes. Cases and legislation are primary sources of law. This means your footnote should not state where you located the case/legislation (for example the textbook or a PowerPoint slide). You simply refer to the case/legislation itself.

If you quote directly from a book you should also footnote the reference to the book.

Here is a short (fictitious) example:

In *Black v Brown[[1]](#footnote-1)* the court ruled that all dogs must be kept on a leash when in public. Mary Smith, a well-known vet, cites the leading UK decision *Rusty v Lassie[[2]](#footnote-2)* as authority for her claim that poodles should not be included in the *Black v Brown* ruling. However, in *Key on Contracts* the author says “All dogs in New Zealand should be kept on a leash”.[[3]](#footnote-3) The Animal Control Act states all domestic animals should be kept under reasonable control in public.[[4]](#footnote-4)

Note: you only need to provide the full citation of a case the first time you mention it.

If necessary, you can refer to the “New Zealand Law Style Guide” <http://www.lawfoundation.org.nz/style-guide/> for further information. However, the Guide provides far more information than you will need for the test. Additional information is also available under the Readings & Library folder in the COML 310 blackboard site. This folder also contains further resources on the APA referencing system.

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**QUESTION ONE**

**Outline the approach taken by a Court when deciding if a business arrangement is a partnership governed by the Partnership Law Act 2019. Refer to all relevant provisions of that Act and any applicable case law/common law in your answer.**

**Suggested maximum word count: 400 words.**

**[25 MARKS]**

When analysing if a business arrangement is a partnership, a court will employ the Partnership Law Act 2019 (PLA 2019).

For a business arrangement to assessed as a partnership, it must first satisfy the three requirements outlined under Section 8.

Firstly, there must be a relationship of trust and mutual confidence between two or more people.

Secondly, they must carry on a business in common - this is an intention to operate a business together as observed in **Khan v Miah[[5]](#footnote-5).**

Thirdly, they must operate with a view to profit (hence a non-profit or charity cannot be considered a partnership).

As stated by Section 11, this analysis will require additional provable evidence of partnerships (outlined in Section 12-15) as other business entities (e.g companies, joint ventures etc.) can meet the conditions outlined in Section 8; as discussed in Section 9.

Once a business arrangement has met the three conditions of Section 8, the court will observe other provable evidence of partnership - this is outlined in Section 12 to 15.

Under Section 12 Co-ownership of land and Section 13 Sharing gross returns, does not in itself indicate a partnership as observed in **Cox v Coulson[[6]](#footnote-6)**.

However, if entities in the business arrangement are receiving shares of the net profit, under section 14 this may be considered provable evidence that a business arrangement - however this is subject to overall relationship and intention of the parties and Section 15 which outlined the circumstances where this evidence would be invalid.

In **Whywait PTY LTD V Davison[[7]](#footnote-7)** we observe this analysis.

On the grounds that the parties had delegated responsibilities necessary to complete the project - a relationship of trust and confidence was found.

On the grounds that the parties intended to complete and profit off the project together - a intention to carry on business was found.

On the grounds that the parties intended to earn a profit on the project - a view to profit was found.

Additionally, the parties equally shared the net profit on the project’s completion.

Thus, it was decided by the court that the arrangement in **Whywait PTY LTD V Davison[[8]](#footnote-8)** was a partnership as the business arrangement satisfied Section 8 and 14 of the PLA 2019.

In conclusion for a business arrangement to be determined as a partnership, it must satisfy the three conditions outline in Section 8 of the PLA 2019 and have valid provable evidence as outlined in Section 12 to 15.

**QUESTION TWO**

**Krill Adventures Limited is the registered company name of a successful business that markets high quality children’s clothes. Krill Adventures products have distinctive branding, featuring cartoons of Scratchy the Krill having fun adventures. (‘Krill’ is a small shrimp-like crustacean.)**

**Morris Spicer has on online business selling offensive t-shirts. The business is surprisingly successful, and Morris decides to incorporate a company, which he wishes to name Kill Adventures Limited. This is because his most successful product is a range of t-shirts showing people suffering various unexpected accidents and injuries.**

**Required:**

**Explain whether the Register is likely to register the name Kill Adventures Limited. Your answer should refer to relevant provisions of the Companies Act 1993, case law and any other authoritative source.**

**Suggested maximum word count: 400 words.**

**[25 MARKS]**

Names must be reserved in accordance to Companies Act 1993 (CA 1993) Section 20 before a business can apply to register a company. Does the name ‘Kill Adventures Limited’ meet the requirements of being approved by the name register?

Under Section 22, the Registrar must not reserve a name in which the use of would contravene an enactment, is identical or almost identical to the name of another company or in the opinion of the Registrar, is offensive.

The name ‘Kill Adventures Limited’ does not contravene an act as it does not breach Flags, Emblems and Names Protection Act 1981, Reserve Bank of New Zealand Act 1989, Co-operative Companies Act 1996 or Human Rights Act 1993.

It is unlikely that the name ‘Kill Adventures Limited’ would be considered identical or almost identical to ‘Krill Adventures Limited’. This is because the word ‘Krill’ and ‘Kill’ are likely to be dissimilar enough to grammatically to distinguish the two names. This assumption is made based on **Paint Factory Ltd v Registrar of Companies[[9]](#footnote-9),** where the Registrar refused to order company The Paint Factory (PN) Ltd to change its name because differences in names consisted of geographical, numerical or date markers. Additionally, there is no indication in the Companies Act 1993 or the Registrar’s practice that similar sounding company names should be considered identical or almost identical under Section 22.

The name ‘Kill Adventures Limited’ is unlikely to be considered offensive as it is not obscene, contrary to public policy or offensive to a particular section of the community/religion.

Therefore, the name ‘Kill Adventures Limited’ meets all 3 requirements of section 22 of the Companies Act 1993.

It is important to note that the Registrar’s function when making a decision under section 22 is only concerned with matters that arise out of the name. Due to the similarity in pronunciation Krill Adventures Limited may have grounds to prosecute Kill Adventures Limited for the tort of passing off or else for breaching the Fair-trading act 1986 Section 9 as observed in **Taylor Bros Ltd v Taylors Group Ltd[[10]](#footnote-10)**.

In conclusion, ’Kill Adventures Limited’ meets all 3 requirements of Section 22 of the Companies Act 1993, therefore it is likely to be approved by the name registered. However, the company should be wary of breaching the tort of passing off or the Fair-trading act 1986 Section 9.

**QUESTION THREE**

B**eta Builders Ltd (BBL) is a medium sized building company. BBL was incorporated by Charles Cook and Denise Downs, who were the original directors and shareholders. Five years ago, they decided to ‘grow’ the company by increasing the share capital of BBL and sold 60% of the shares in BBL to Alpha Holdings Ltd (Alpha).**

**Charles and Denise retain the balance of the shares and remain as directors. Alpha arrange for Eric Evans and Frank Foote to be appointed as directors of BBL. Both Eric and Frank are also directors of Alpha. The fifth director is Geraldine Green, who is a partner at a local law firm.**

**On the recommendation of Alpha, Eric and Frank suggest to the board of BBL that it should acquire a new building in Wellington. The purchase price for the building is $6.5 million. Geraldine also supports the purchase and therefore three of the five board members are in favour of the new acquisition and BBL proceeds with the purchase. It turns out that the building needed substantial strengthening work that appropriate pre-purchase due diligence checks would have uncovered. In addition, BBL borrowed funds from its bank to buy the building. However, the costs of servicing this loan and the costs of the unexpected strengthening work result in BBL not paying deducted PAYE and GST amounts to the IRD for 6 months in order to pay other creditors. The IRD eventually appoints a liquidator on the basis that the company is insolvent.**

**Required:**

**Explain what directors’ duties may been breached and who may have breached them.**

**Suggested maximum word count: 700 words**

**[50 MARKS]**

**Issue**

What director duties may have been breached by the directors of Beta Builders Ltd (BBL), who may have breached these duties.

**Law**

Companies act 1993:

-Section 126(1)b(i)and(ii), In this Act, **director**, in relation to a company, includes a person in accordance with whose directions or instructions an acting director may be required or is accustomed to act; Alpha Holdings Ltd (Alpha) would be deemed a shadow director as they control Eric and Frank.

-Section 135, A director must not— agree to the business of the company being carried on in a manner likely to create a substantial risk of serious loss to the company's creditors

-Section 136, A director must not agree to the company incurring an obligation unless the director believes at that time, on reasonable grounds, the company will be able to perform the obligation when it is required to

-Section 137, A director must exercise the care, diligence, and skill that a reasonable director would exercise in the same circumstances.

-Section 138, A director may rely on reports, statements and financial data etc. produced by a competent Employee Professional advisor or expert Specialist director or board committee, if the director Acts in good faith; and Makes proper inquiry where the inquiry is necessary in the circumstances; and Has no knowledge that such reliance is unwarranted

**Application**

By continuing to trade for 6 months after BBL was aware that they could not meet their financial obligations (deducted PAYE and GST amounts to the IRD), all the directors of BBL - Charles, Denise, Eric, Frank, Geraldine - are liable for breaching their duty of liquidity to BBL under Section 135 as they have engaged in reckless trading. By grounds of **Syntax Holdings (Auckland) Ltd (in liquidation) v Bishop[[11]](#footnote-11)**, when BBL began using money owed to the IRD to meet their financial obligations to other creditors, a reasonable director, taking a “sober assessment” would have liquidated the company to prevent creditors becoming exposed to illegitimate risk. As a result, the directors may be personally liable for the debts incurred during this period.

BBL directors Eric, Frank, Geraldine and Alpha (as a shadow director) engaged in the acquisition for the building to the value of $6.5 million using a bank loan. However, BBL did not have the financial capacity to finance the servicing of this loan. Eric, Frank, Geraldine and Alpha breached the duty of liquidity to BBL under Section 136 as they have incurred a major financial obligation without grounds to believe that BBL could meet that financial obligation. On the basis of **Re Wait Investments Ltd (in liq)[[12]](#footnote-12),** the decision would be considered unduly optimistic and without proper foundation as it was unreasonable to enter into this acquisition without organised financing. As a result, the directors may be personally liable for the debts of BBL.

By acting solely based off the recommendations of Alpha and without performing pre-purchase due diligence checks that a reasonable director would be expected to perform in that circumstance Eric, Frank and Geraldine breached their duty of competence to BBL under section 137.

Additionally, it could be argued on the basis of **Davidson v Registrar of Companies[[13]](#footnote-13)** Geraldine did not meet the requirements of a reasonable director as he is unlikely to have the necessary skills to understand crucial information in BBL (a building company) as he specialises in law - this may also extend to Eric and Frank depending on their comprehension of building and construction. This is also a breach to section 137 as they took no steps to understand the necessary components of acquiring a building.

Unless Alpha is considered an expert in buildings and construction, Eric, Frank and Geraldine would not have a defence for Section 137 under Section 138, as there was no reasonable steps taken by these directors to ensure that the trust in Alpha’s recommendation is warranted (especially if they did not have a strong understanding of building). This statement is made on the basis of **Goatland Ltd v Borrell[[14]](#footnote-14),** where unsubstantiated advice cannot provide a defence.

As a result, the directors may be personally liable for the debts of BBL.

**Conclusion**

Under the Companies act 1993 the director duties breached was liquidity under Section 135 and 136 by Charles, Denise, Eric, Frank, Geraldine and Alpha (as a shadow director) and the duty of competence under Section 137 by Eric, Frank, and Geraldine. As a result, the directors may be personally liable for the debts of BBL.

1. [2001] 3 NZLR 47. [↑](#footnote-ref-1)
2. (2006) 1 All ER 34 (HL). [↑](#footnote-ref-2)
3. J Key, Key on Contracts, (2006, LexisNexis) at 45. [↑](#footnote-ref-3)
4. Animal Control Act 1945, s21(a)(i). [↑](#footnote-ref-4)
5. [2001[ 1 All ER 20 (HL) [↑](#footnote-ref-5)
6. [1916] 2 KB 177 [↑](#footnote-ref-6)
7. [1997] 1 QD R 225 (QD CA) [↑](#footnote-ref-7)
8. [1997] 1 QD R 225 (QD CA) [↑](#footnote-ref-8)
9. [2000] 3 NZLR 220 [↑](#footnote-ref-9)
10. [1988] 2 NZLR 1 [↑](#footnote-ref-10)
11. [2013] NZHC 2171 [↑](#footnote-ref-11)
12. [1997] 3 NZLR 96 [↑](#footnote-ref-12)
13. [2011] 1 NZLR 542 [↑](#footnote-ref-13)
14. [2007] 23 NZTC 21,107 (HC) [↑](#footnote-ref-14)