

LPC BUDDY

Business Law & Practice
2021 / 22



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FOR THE LPC

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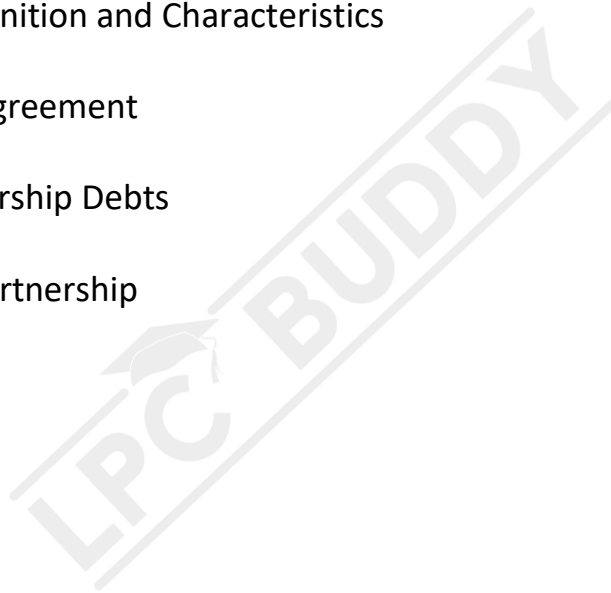
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1. Partnerships

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Partnerships - Introduction

❖ *Business Law & Practice, Chapter 13*

<p>What is a Partnership?</p> <p><i>Business Law & Practice, 13.2</i></p>	<ul style="list-style-type: none"> ❖ A partnership is where two or more people run and own a business together. ❖ It is created when the definition in s1 of the Partnership Act 1890 is satisfied. There are no further formalities required. ❖ This means that: <ul style="list-style-type: none"> ➢ There is no <i>requirement</i> for a written agreement (although it may be advisable to have one). ➢ If the component elements are satisfied, a partnership will exist even when the individuals involved are unaware of what they have created legally. 						
<p>Definition</p>	<ul style="list-style-type: none"> ❖ s1 Partnership Act 1890: “Partnership is the relation which subsists: <ul style="list-style-type: none"> ➢ <i>Between persons</i> ➢ <i>Carrying on a business in common.</i> ➢ <i>With a view of profit”</i> <table border="1" data-bbox="321 716 1529 1770"> <tr> <td data-bbox="321 716 527 793"> <p><i>“Between Persons”</i></p> </td> <td data-bbox="527 716 1529 793"> <ul style="list-style-type: none"> ❖ Partners can be individuals <u>or</u> companies. </td> </tr> <tr> <td data-bbox="321 793 527 1692"> <p><i>“Carrying on a Business in Common”</i></p> </td> <td data-bbox="527 793 1529 1692"> <ul style="list-style-type: none"> ❖ “Business” “includes every trade, occupation or profession” (s45 PA 1890) <ul style="list-style-type: none"> ➢ Virtually any activity of a <i>commercial nature</i> is capable of giving rise to a partnership (but not a charity; see below). ❖ The business must be “carried on”. This means that: <ul style="list-style-type: none"> ➢ There must be more than “mere agreement” (<i>Illot v Williams & Others [2013] EWCA Civ 645</i>) ➢ However, there is no requirement that the parties need to have actually commenced trading for a partnership to be formed: <ul style="list-style-type: none"> ▪ <i>Khan v Miah [2000] 1 WLR 2123: “There is no rule of law that the parties to a joint venture do not become partners until actual trading commences. The rule is that persons who agree to carry on a business activity as a joint venture do not become partners until they actually embark on the activity in question”.</i> ▪ In <i>Khan</i>, a partnership was held to exist where the parties had agreed to open a restaurant together. Whilst they had not traded, they had taken steps to pursue the venture, including opening a joint bank account, obtaining a bank loan, and acquiring premises, furniture and equipment. </td> </tr> <tr> <td data-bbox="321 1692 527 1770"> <p><i>“With a view of profit”</i></p> </td> <td data-bbox="527 1692 1529 1770"> <ul style="list-style-type: none"> ❖ The purpose of the business must be to make money. ❖ Charitable motives are unable to constitute partnerships. </td> </tr> </table>	<p><i>“Between Persons”</i></p>	<ul style="list-style-type: none"> ❖ Partners can be individuals <u>or</u> companies. 	<p><i>“Carrying on a Business in Common”</i></p>	<ul style="list-style-type: none"> ❖ “Business” “includes every trade, occupation or profession” (s45 PA 1890) <ul style="list-style-type: none"> ➢ Virtually any activity of a <i>commercial nature</i> is capable of giving rise to a partnership (but not a charity; see below). ❖ The business must be “carried on”. This means that: <ul style="list-style-type: none"> ➢ There must be more than “mere agreement” (<i>Illot v Williams & Others [2013] EWCA Civ 645</i>) ➢ However, there is no requirement that the parties need to have actually commenced trading for a partnership to be formed: <ul style="list-style-type: none"> ▪ <i>Khan v Miah [2000] 1 WLR 2123: “There is no rule of law that the parties to a joint venture do not become partners until actual trading commences. The rule is that persons who agree to carry on a business activity as a joint venture do not become partners until they actually embark on the activity in question”.</i> ▪ In <i>Khan</i>, a partnership was held to exist where the parties had agreed to open a restaurant together. Whilst they had not traded, they had taken steps to pursue the venture, including opening a joint bank account, obtaining a bank loan, and acquiring premises, furniture and equipment. 	<p><i>“With a view of profit”</i></p>	<ul style="list-style-type: none"> ❖ The purpose of the business must be to make money. ❖ Charitable motives are unable to constitute partnerships.
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<p>Effect of Creation - No Separate Legal Personality</p>	<ul style="list-style-type: none"> ❖ A partnership is unincorporated; it has no separate legal personality. ❖ This means that: <ul style="list-style-type: none"> ➢ “Partnership assets” are not owned by the partnership itself (because it is not a legal entity); they are owned by the partners. 						

	<ul style="list-style-type: none"> ➤ Partners will be personally liable for any debts, and their personal assets are at risk. ❖ As compared with a company, the benefits of a partnership are: <ul style="list-style-type: none"> ➤ Lack of formality; partners do not have to go through any of the extensive administrative and accounting requirements of a company. Partners are able to focus on the business itself. ➤ There is no requirement to make as much information public.
<p>Fundamental Characteristics of a Partnership</p> <p><i>Business Law & Practice, 13.2.2</i></p>	<p>Partners will tend to have the following rights and responsibilities:</p> <ol style="list-style-type: none"> 1. To be involved in making decisions which affect the business (s24(5)). 2. To share in the profits of the business; (s2(3) provides that this will be <i>prima facie</i> evidence that an individual is a partner (s24(1)). 3. To examine the accounts of the business; 4. To insist on openness and honesty from fellow partners; 5. To veto the introduction of a new partner; and (s24(7)). 6. Responsibility for sharing any losses made by the business (s24(1)).
<p>Decision Making</p>	<ul style="list-style-type: none"> ❖ Partners make decisions by a majority vote (s24(8)). ❖ However: <ul style="list-style-type: none"> ○ A decision to change the nature of the partnership business can only be done unanimously (s24(8)). ○ New partners can only be introduced with the consent of all existing partners (s24(7)).

Partner’s Responsibilities

- ❖ *Business Law & Practice, 15.2 – 15.3*
- ❖ Partners are under a duty of the **utmost fairness and good faith** to each other.
- ❖ s28 – s30 PA 1890 expands upon this duty, providing that partners are under the following duties:

<p><u>s28 PA 1890 – Divulge Information to Other Partners</u></p>	<ul style="list-style-type: none"> ❖ Partners must divulge all relevant information connected with the business and their relationship to the other partners. <ul style="list-style-type: none"> ○ E.g. if, when selling business premises to the partnership, a partner suppresses information about the value of the premises.
<p><u>s28 PA 1890 – Accounting for Benefits</u></p>	<ul style="list-style-type: none"> ❖ Partners must account to the firm for any benefit derived without the consent of the other partners from a transaction concerning the partnership. <ul style="list-style-type: none"> ○ Has the partner derived a benefit? ○ Was this with the other partner’s consent? ○ E.g. if a partner is asked by a client of the firm to do some work in his spare time, the money received from this will be <u>cash of the partnership</u> unless the other partners consent to him keeping it.
<p><u>s30 PA 1890 – Account for profits from competing businesses.</u></p>	<ul style="list-style-type: none"> ❖ If a partner runs a business “of the same nature” and competes with the firm, he must account for any profits made by this unless he has the consent of the other partners. <ul style="list-style-type: none"> ○ This catches businesses in direct competition with the partnership. ○ This does not necessarily include similar, but non-competing businesses e.g. a business in a different part of the supply chain.

The Partnership Agreement

❖ [Business Law & Practice, Chapter 14](#)

❖ **Fundamental Principle:**

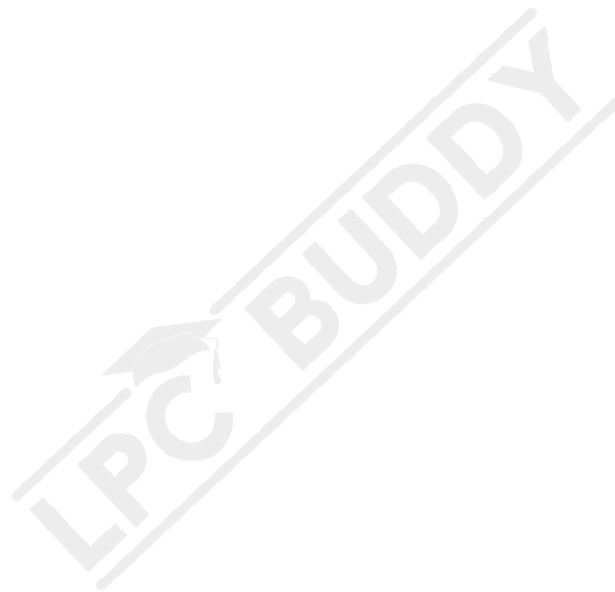
- The **Partnership Act implies basic terms** into every partnership agreement.
- These **terms will not necessarily be appropriate for every partnership agreement** and the terms are not comprehensive in what they do cover, so a written agreement is often necessary.

Area of Issue (A-Z)	What the Partnership Act Implies	Why is this problematic/what terms are desirable?
Arbitration Business Law & Practice, 14.8	❖ Nothing	❖ Can be useful to include an arbitration clause to resolve disputes and avoid publicity, delay and expense of litigation.
Commencement Date Business Law & Practice, 14.2	❖ Nothing. ❖ The partnership comes into being when the s1 definition is satisfied.	❖ Desirable to include a clause which specifies the start-date of the partnership so it is certain when rights and obligations arise.
Dissolution Under s33 PA 1890 Business Law & Practice, Chapter 17.2.4	❖ Death or bankruptcy of a partner will automatically dissolve the partnership (s33).	❖ It is normally desirable to depart from this and provide that the remaining partners will automatically continue in partnership on buying out the deceased/bankrupt partner's share.
Drawings Business Law & Practice, 14.6	❖ Nothing	❖ May be desirable place a monthly limit on how much each partner can draw from the business to prevent a partner draining funds.
Duration and Dissolution Business Law & Practice, 14.3	❖ No duration supplied by the Act. ❖ If there is no agreement to the contrary, the partnership will be a "partnership at will" (s26). ❖ "Partnership at will" means that the partnership continues unless a partner gives notice to terminate the partnership.	❖ Any partner may terminate the entire partnership "at any time by giving notice of his intention to do so to all the other partners" (s26). ❖ Notice is immediate , and does not need to be in writing unless the partnership agreement is made by deed (s26(2)). ❖ Flexible for the partners, but unsecure for the business as whole partnership can be brought to an end on the whim of a single partner. ❖ Amendments might include: <ul style="list-style-type: none"> ➤ Specifying a <u>minimum period of notice</u>. ➤ <u>Agreeing a fixed term</u>, perhaps continuing thereafter to be terminable with a minimum notice period. ➤ <u>That the partnership shall continue as long as there are two surviving partners.</u>
Expulsion Business Law & Practice, 14.15	❖ Nothing ❖ The PA 1890 does not provide for the possibility of a partner to	❖ Desirable to provide a term enabling the partners to expel a partner in prescribed circumstances.

<u>Area of Issue (A-Z)</u>	<u>What the Partnership Act Implies</u>	<u>Why is this problematic/what terms are desirable?</u>
	<p><u>be expelled</u> by the other partners without his consent.</p>	
<p><u>Non-Competition Clauses</u> <u>Business Law & Practice, 14.17</u></p>	<p>❖ <u>Nothing in the Act prevents partners from setting up in competition</u> on leaving the partnership.</p>	<p>❖ Where the firm continues, it is important to provide a <u>term limiting the outgoing partner's freedom to compete</u>.</p> <p>❖ Such clauses <u>must not be unreasonably broad</u> or they will be void:</p> <ul style="list-style-type: none"> ➤ The clause must: <ul style="list-style-type: none"> ▪ <u>Protect a legitimate interest</u> <ul style="list-style-type: none"> • E.g. the <u>firm's business connections, employees, confidential information</u>. ▪ <u>Be reasonable to protect that interest</u>. <ul style="list-style-type: none"> • Is the clause wider than it needs to be? • Should be <u>limited in its geographical scope and duration</u> e.g. restrictions lasting more than 3 years over an unduly wide area more likely to be unreasonable. <p>❖ <u>Consider less burdensome clauses which do not restrict trade as a whole</u>, as these are more likely to be reasonable:</p> <ul style="list-style-type: none"> ➤ <u>Non-dealing clause</u> i.e. preventing the partner from entering contracts with customers etc. ➤ <u>Non-solicitation clause</u>: preventing the partner from soliciting contracts.
<p><u>Outgoing Partner's Share</u> <u>Business Law & Practice, 14.16</u></p>	<p>❖ If the partnership continues but there is a delay in payment of an outgoing partner's share, that <u>partner/his estate will be entitled to either:</u></p> <ul style="list-style-type: none"> ➤ <u>5% interest on his share or</u> ➤ <u>Such profits as are attributable to his share (s42).</u> 	<p>❖ When a partner leaves the business, the remaining partners will need to pay for his share or this could be sold to an external third party.</p> <p>❖ It is desirable to have terms set from the outset e.g.:</p> <ul style="list-style-type: none"> ➤ Whether the partners have an <u>obligation or an option</u> to purchase an outgoing partner's share. ➤ The <u>basis on which the share will be valued</u> and how to resolve disputes as to

Area of Issue (A-Z)	What the Partnership Act Implies	Why is this problematic/what terms are desirable?
		<p>the valuation (e.g. professional valuation).</p> <ul style="list-style-type: none"> ➤ Date on which payment will be due. ➤ Indemnity for liabilities of the firm. ➤ Valuation of goodwill.
<p>Retirement (leaving the partnership) Business Law & Practice, 14.14</p>	<ul style="list-style-type: none"> ❖ Nothing. ❖ Partners have no right to retire under the Act. ❖ However, partners CAN vary the partnership agreement by unanimous consent (s19). 	<ul style="list-style-type: none"> ❖ It is desirable to include a term enabling a partner to retire without unanimous agreement.
<p>Sale of Capital Assets and Sharing of Capital Increases Business Law & Practice, 14.7</p>	<ul style="list-style-type: none"> ❖ Partners share equally in the capital of the business (s24(1)). ❖ Increases/decreases in the value of assets are therefore also shared equally. 	<ul style="list-style-type: none"> ❖ Partners may want to deviate from this to reflect the capital contribution of each partner to the business. ❖ E.g. if Partner A provides a factory worth £50,000, and Partner B puts in £10,000 cash, under the PA 1890 if the factory increases in value to £60,000, the £10,000 increase would be split 50/50. Similarly, if the factory is sold, Partner A will only receive £30,000 despite contributing an asset worth £50,000. ❖ It may be worth specifying in the agreement what assets are “Partnership Assets” in which all partners will have a beneficial interest, and which are assets belong to individual partners to prevent disputes.
<p>Sharing of Profits/Losses Business Law & Practice, 14.5</p>	<ul style="list-style-type: none"> ❖ Profits/losses of the business are to be shared by the partners equally (s24(1)). ❖ s24(6) explicitly prohibits partners from receiving a salary unless an agreement to the contrary excludes this. 	<ul style="list-style-type: none"> ❖ Partners may want to deviate from this to reflect the contribution of each partner to the business e.g. in terms of time/experience/capital contribution ❖ E.g: <ul style="list-style-type: none"> ➤ By paying on a salary basis. ➤ By specifying that partners are allowed interest in proportion to their capital contributions – incentivises investment. ➤ That profits/losses be shared in specific percentages as opposed to equally.
<p>Work Input Business Law & Practice, 14.10</p>	<ul style="list-style-type: none"> ❖ Partners have a right, but not an obligation, to take part in the management of the business (s24(5)). 	<ul style="list-style-type: none"> ❖ Under the Act, it is perfectly permissible to have a “sleeping partner” who effectively contributes nothing to the business. ❖ Partners may, therefore want fix each partner’s obligations and avoid a scenario where a partner may do nothing but nevertheless be entitled to an equal share in the profits of the partnership.

Area of Issue (A-Z)	What the Partnership Act Implies	Why is this problematic/what terms are desirable?
		❖ E.g. a partner must “ <i>devote his whole time and attention to the business</i> ” or specify a number of hours per week etc. The clause would need to cover sick leave, holiday entitlement etc.



Liability for Partnership Debts

❖ [Business Law & Practice, 16.2](#)

- ❖ During the course of partnership business, contracts may be entered into either by (a) **all of the partners collectively**, or (b) by **an individual partner purporting to act on behalf of the partnership**.
- ❖ Such contracts will always bind the partner(s) who entered into the contract, but will only sometimes create liabilities which bind the partnership as a whole. The position, in summary, is as follows:

Summary	<ul style="list-style-type: none"> ❖ The debts / liabilities of a partnership can be enforced against: <ol style="list-style-type: none"> 1. The Partner Who Made the Contract <ul style="list-style-type: none"> ➢ Can always be sued - there will be privity of contract between the partner and the other party. 2. The Firm: <ul style="list-style-type: none"> ➢ The firm will be liable if the contracting partner had: <ul style="list-style-type: none"> ▪ Actual authority or ▪ Apparent / ostensible authority (see below). ❖ If the firm is liable, the creditor can sue: <ul style="list-style-type: none"> ➢ The firm as a whole, OR ➢ Any individual partner at the time the debt was incurred. <ul style="list-style-type: none"> ▪ Under s9, partners are jointly and severally liable i.e. each individual partner is fully liable for the performance of contractual obligations which bind the partnership. ▪ If the partner entered into the contract with apparent authority only, he will have to indemnify the other partners for any liability / loss they incur.
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Actual and Ostensible Authority

<p>Actual Authority</p> <p>s6 PA 1890</p> <p>Business Law & Practice, 16.2.1</p>	<ul style="list-style-type: none"> ❖ Actual Authority is where a partner was actually authorised by the partnership to enter into an agreement. ❖ This will ALWAYS bind the partnership: <ul style="list-style-type: none"> ➢ s6 Partnership Act 1890: an instrument executed in the name of the firm by any person authorised to do so, whether a partner or not, will bind the firm and all the partners. ❖ Actual authority may be express or implied: <ul style="list-style-type: none"> ➢ Express: i.e. there was a specific agreement between the partners granting the partner authority. ➢ Implied: e.g. by one partner being <u>regularly responsible for a particular course of dealing in relation to which the others have acquiesced.</u>
<p>Apparent/Ostensible Authority</p>	<ul style="list-style-type: none"> ❖ If a partner does not have actual authority, the partnership may still be bound under s5 if the partner had "apparent" or "ostensible" authority.