

Battling to save a failing business can put directors at risk

As the recession deepens, more and more company directors could find themselves battling to keep their businesses afloat.

While they will naturally want to do everything possible to come through these current economic difficulties, they must guard against soldiering on for too long trying to rescue a business which has no chance of survival.

If they do they could be accused of wrongful trading and run the risk of financial ruin as they become liable for the debts of their business – even if it is a limited liability company. The danger is that some directors may fail to recognise or refuse to accept that their business has no chance of avoiding insolvency. Understandably, they may have an emotional attachment to a firm they have set up themselves and feel a tremendous loyalty to their staff. Or they may be trying to avoid having to pay back company loans which they have personally guaranteed.

This can make them carry on regardless, hoping against hope that things will improve even though that can sometimes makes things worse because the law is quite clear about what should happen in these circumstances. As soon as a company becomes insolvent, directors have a legal duty to protect



the interests of creditors. When formal insolvency procedures get underway, the behaviour of directors over the previous few years could come under investigation.

They could become liable for wrongful trading if it's found that they continued entering into contracts or accepting credit after they knew or should have known there was no reasonable chance of avoiding insolvent liquidation.

The court could then order them to use their personal assets to help settle the company's debts. Directors of insolvent companies are also obliged to treat all creditors equally so they must not give preferential treatment to friends or a company that is threatening to sue them.

The problem for many directors is identifying the point at which they become insolvent so they should seek professional help as soon as problems start to emerge.

Persistence is a good quality in business but directors must also recognise when the cause may be lost and then make sure they meet their legal obligations.

Builders win dispute with contractor over payments

It is always advisable for businesses to draw up a contract before beginning work for a client, especially if it is a large project involving significant sums of money.

However, even if there is no written contract, it is still possible to take legal action to recover money due as was shown in a recent case involving a firm of builders.

The builders had agreed to refurbish a house and outbuildings for a contractor. There was no written contract but the builders issued statements of account for the work as it was carried out and the contractor made regular payments.

A dispute then arose about the amount being charged. The contractor refused to make further payments and the builders were ordered off the site. The builders contended that the contractor

had agreed to pay the amounts shown in the statements of account and should honour that agreement. The contractor argued that the project was to be carried out on a cost plus basis. The amounts he had already paid were not in response to the individual invoices but on account for the final bill.

The builders also argued that they had been wrongfully expelled from the site and were entitled to compensation for the loss of profit on the work they had been asked to do. The contractor counter claimed saying some of the work was defective and he was entitled to end the contract because of the builders' delay in completing the work.

In the absence of a written contract, the court had to decide whether the contractor had agreed to pay the prices as they were set out in the statements of account or whether he had merely agreed to pay a reasonable price on a cost plus basis.

The court held that the payment procedure had changed as the project



progressed. It began with the contractor paying individual invoices but then changed to a system by which he agreed to pay a reasonable price for the whole project. That, however, was overtaken by him ordering the builders off the site in the course of the dispute.

The court considered the expulsion to be unjustified because there had been no delay or other problem that entitled the contractor to terminate the contract.

The builders were therefore entitled to recover their losses for the uncompleted work.

It would have helped, of course, if the terms of payment and other issues had been written into an agreement before work began, but the case shows that the courts can still help when disputes arise.

Expulsion from site 'unjustified'

Employment Act sweeps away unpopular dispute resolution procedures

The Employment Act 2008 has received the Royal Assent and will now sweep away the dispute resolution procedures which have proved so unpopular with employers since they were introduced in 2004.

One of the main changes is that the dismissal of an employee will no longer be considered automatically unfair if there is a breach of procedure by the employer.

It will still be possible for a dismissal to be deemed unfair on procedural grounds but a tribunal will be able to adjust the level of compensation - or decline to award compensation at all - if it considers that the dismissal would have taken place anyway, even if the correct procedures had been followed.

Tribunals will also have the power to adjust awards by 25% if either side has failed to reasonably comply with a relevant code of practice. In unfair dismissal cases, this will be the new Code of Practice on Disciplinary and Grievance Procedures drawn up by ACAS.

The Act gives tribunals the power to determine a case without a hearing if both parties put their consent in writing or if the respondent in the case fails to present a response.

Tribunals will also be able to award compensation for financial loss in certain cases, for example, where an employee is making a claim in relation to deductions from wages or redundancy payments.



The Act also introduces tougher sanctions against employers who fail to pay the National Minimum Wage (NMW).

There will be a new way of calculating arrears for workers who have been underpaid. The arrears will be calculated with reference to the NMW rate at the time when the underpayment is rectified as well as the rate at the time when the underpayment originally took place.

It means the employee could be repaid the arrears at a higher rate than he would have originally received had no underpayment taken place, assuming that the NMW has increased in the meantime. The formula for the calculation will take into account the length of time the arrears have been outstanding. This is intended to compensate the employee for having to wait for full payment and also to act as a deterrent to employers.

Revenue and Customs officers will be given further powers to obtain information from employers relating to NMW payments and will be able to take documents away for copying.

Enforcement officers will also be able to impose penalties for underpayment.

There will also be changes to the way criminal offences under the NMW Act are investigated and enforced with the most serious cases being tried in the Crown Court.

The changes introduced in the Employment Act are likely to affect all employers. Please contact us if you would like more information.

EU votes to end Britain's opt-out from the 48-hour maximum working week

The European Parliament has voted to scrap the UK's right to opt out of the 48-hour maximum working week. MEPs voted by a majority of 148 that the opt-out should end within three years of the new EU Working Time Directive being adopted.



the Parliament will now have to negotiate a compromise.

If they can't reach agreement then the directive will fail and the opt-out will remain in place. Those negotiations should be concluded by May.

If the directive is adopted then the opt-out clause will end three years later and UK workers will not be allowed to work more than an average of 48 hours a week, even if they want to do so.

We shall keep clients informed of developments.

The vote puts the parliament in conflict with the Council of Ministers which negotiated a deal with the UK government last summer allowing the opt-out to continue in return for Britain accepting improved rights for temporary workers. It means that the Council and

Court says same complaint by tenant cannot be heard twice

A tenant has failed in her attempt to bring court proceedings for a second time in relation to a problem with dampness in her flat.

The court ruled that as the case had already been dealt with once it should not be heard again and so was struck out.

The case involved Ealing Borough Council and one of its tenants. The tenant had experienced problems with dampness in her flat and so had started proceedings alleging that Ealing had breached its duty under the Landlord and Tenant Act 1985.

She did not produce any expert evidence as to the cause of the problem. The judge then found that there was no evidence of structural damage and the most likely cause of the dampness was condensation. The tenant's claim therefore failed.

The tenant then tried to make a second claim, calling on expert evidence suggesting that the most likely cause of the dampness was the fact that there was no membrane under the floor.

However, the county court struck out her claim on the grounds of res judicata – a legal principle that prevents courts

from hearing the same case twice. It's designed to ensure a finality to legal proceedings. The tenant appealed to the High Court saying the principle should be set aside because the Landlord and Tenant Act 1985 placed a continuing duty on landlords to keep properties in good repair. Therefore, to continue with the principle would frustrate the will of Parliament.

The High Court dismissed her appeal, however, saying it was in the public interest that there should be a finality to litigation and there was no reason why res judicata should not apply to the Landlord and Tenant Act.

The danger for landlords in not pursuing overdue rent

The danger for landlords in not chasing up overdue rent and attending to legal detail has been illustrated in a recent case before the Court of Appeal.

It resulted in a landlord having to grant a 21-year-lease to a tenant he would have preferred to evict.

The case involved a landlord who had granted a tenant a 15-year-lease on some retail premises. The retailer later vacated the premises and a new tenant moved in and started trading without the landlord's knowledge.

The landlord did not object at first when he discovered the change and then in 1998 began negotiations to grant the new occupier a 21-year-lease. The tenant carried out repairs to the premises as part of the proposed lease.

However, the two parties then fell out over various matters including the fact that the tenant was persistently late in paying his rent. The landlord gave notice that he was terminating the tenancy.

The tenant claimed the landlord was prevented from denying his right to a



lease by the principle of proprietary estoppel. This is a principle that can be used to protect the interests of a person who has been given reasonable grounds to believe that he will acquire rights over a property and has taken action to his detriment on that basis, such as by carrying out expensive repairs.

The judge ruled that the tenant had in fact established an equitable tenancy and was entitled to be granted a 21-year-lease.

The judge also held that the tenant's claim could not be dismissed just

because he had persistently delayed paying the rent.

The Court of Appeal has now upheld the judge's ruling. Commenting on the issue of late payment of rent, the judges said that the landlord's case had to be considered in the light of his actions. He could not have considered it a serious problem because he never did anything about it apart from write the occasional letter.

The tenor of the landlord's communication at the time had been that, in spite of the tenant's poor payment record, the lease could still go ahead.

The current credit crunch has no doubt encouraged most landlords to keep a tight rein on rent arrears but cases like this provide another incentive. They also highlight the need to pay close attention to legal detail when negotiating leases so that problems like these can be avoided.

Please contact us if you would like advice or information relating to landlord and tenant issues.

OFT to assess the process of buying and selling homes

The Office of Fair Trading is to conduct a study into the buying and selling of homes to ensure consumers are being protected and to see if the system can be improved.

The study will look at the traditional models involving estate agents and consider possible alternative approaches.

The OFT says it will concentrate on three main issues: the level of competition between service providers in terms of price and quality, the extent to which the existing regulatory framework protects consumers, and the potential for entry for new providers including internet property retailers.

It may also examine the relationships between estate agents, mortgage brokers, surveyors, solicitors and other professions.

Market studies by the OFT are carried out under the Enterprise Act 2002 which enables them to look at both competition and consumer issues.

We shall keep clients informed of developments.

A new way to tackle 'Coke Cola' style copycat branding

The Companies Act has provided a new streamlined way for businesses to protect their trademarks.

It was used for the first time recently in a case involving a firm calling itself Coke Cola Ltd. It may seem surprising that someone thought they could get away with registering a name so similar to one of the world's leading brands.

Until recently, however, Coca Cola might have found it difficult to deal with the problem because although a company could take action if a firm tried to use the same name, the scope for objecting to names that were merely similar was much more limited.

That has now changed because of provisions in the Companies Act 2006 which came into effect last October.

Now it is easier for companies to take action against opportunistic registrations of names which are the same or similar to their own.

Such opportunism includes cases where someone registers variations of the name of a well-known company in order to get that company to buy the names back. Or it could be that someone hears of a proposed merger between two firms and then registers several

variations of the kind of name the new firm is likely to adopt. The Company Names Tribunal was set up to adjudicate on such matters and the Coke Cola affair was its first case.

Coca Cola argued that the registration of Coke Cola Ltd was opportunistic and designed to take advantage of its famous brand name. The Tribunal moved quickly and ordered Coke Cola Ltd to change its name within one month. If it failed to do so then the Tribunal would choose a name for it.

It was also ordered to pay Coca Cola's application fee of £400 and £300 towards its costs.

The tribunal only deals with opportunistic registrations and there will still be times when companies may need to pursue infringements through the courts as before.

However, this new system provides companies with a quick and relatively cheap way to protect their brand. The application fee is only £400 and there are short time limits for the exchange of evidence so a case is unlikely to drag on incurring prohibitive costs.



Factory owner successful in right to light case

A factory owner who was willing to lose some of his right to light to accommodate a new development but then objected when the loss was much greater than agreed has won his case in the Court of Appeal.

The owner had entered into an agreement with the developer in which he accepted that a new development would have an adverse effect on his right to light but he would not take any action to enforce that right. Once the development had been completed, however, the developers then began

Legal rights had not been lost

work on another building. They registered a light obstruction notice against the factory on the basis that it could be affected by a wall that might be built close by.

The factory owner began legal proceedings to protect his right to light on the basis that the new proposal would cause far more of an obstruction than the

one that had been originally agreed. The case went all the way to the Court of Appeal which has now ruled in favour of the factory owner. It held that on a fair reading of the agreement, the owner had only consented to a development that would cause some loss of light. He had not consented to a completely separate development that would block out all light.

In entering into the original agreement, the factory owner had not abandoned his right to light nor lost his entitlement to enforce that right.

Directors pay dearly for not following their articles of association

The need for directors to follow their company's articles of association when trying to resolve a dispute was highlighted in a recent case before the Court of Appeal.

It involved a man who was removed as a director of a company in which he owned 25% of the shares. Under the company's articles of association he then had to transfer his shares back to other directors.

The procedures laid down in the articles meant that if the two parties could not agree a fair price for the shares, as in this case, then a third party accountant would be appointed to provide an independent valuation.

The company's board identified a firm of accountants and signed a letter of engagement asking them to carry out the valuation. The director transferring the shares indicated his willingness to accept the appointment but he did not sign the letter.

Instead, he reserved his position. The company went ahead with the



appointment but when the accountants provided a valuation the director refused to accept it. A judge then held that he was not bound by the valuation because he had not signed the engagement letter and agreed to its terms.

The company appealed and there then followed some legal argument about whether the director's actions in indicating his willingness to accept the appointment amounted to him having actually accepted it and whether he should therefore be bound by it.

However, the Court of Appeal has ruled in favour of the director, saying

that the company's interpretation of its own articles of association would lead to surprising consequences. The accountancy firm held a powerful position because it not only valued the shares but it could also decide who should bear the costs of resolving the dispute.

With so much at stake it would be very surprising if the accountants could act as an impartial third party when they had only been nominated by the company.

The fact that the director had indicated his willingness to accept the appointment of the accountants was not enough to constitute an agreement.

The company's articles of association required that both parties and the accountants should agree and sign the terms of engagement before the valuation process could proceed and become binding.

Please contact us if you would like more information about this or any aspect of company law.



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