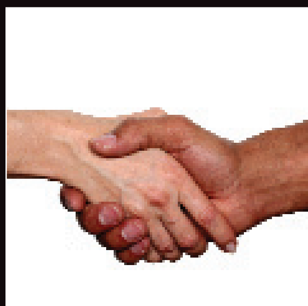
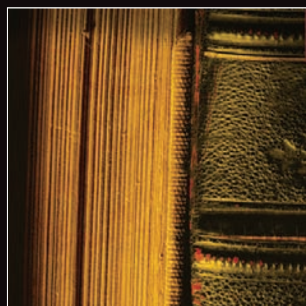
THE SUNDAY TIMES

BUSINESS DEVELOPMENT SERIES

Essential Law for Your Business

A practical guide to all legal and financial requirements





Patricia Clayton

13TH EDITION

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A practical guide to all legal and financial requirements

Patricia Clayton

To Dennis, Richard, Jane and Charles
With love and thanks

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Preface

This is a 'how-to' – not 'do-it-yourself' – guide to your legal and financial responsibilities as an entrepreneur and employer: how to start your business, how to keep it going and how to avoid the legal pitfalls that beset your path. You are forewarned and forearmed but *not* equipped to be your own lawyer.

Chapter 1 outlines business structure. Later chapters deal with the impact of your choice of structure on various aspects of your business dealings. Some land, tax and insurance law and relevant areas of commercial law are covered as well as health and safety and employment legislation and litigation.

This is, however, a slimmed-down, easy-reference edition of the original *Law for the Small Business* and the law is set out in broad terms. If you run into problems you must dig deeper and consult legal and/or financial experts.

But the pile of legislation daily grows higher. In many areas ignorance is no defence and you cannot afford to risk yourself and your capital in the legislative jungle without some knowledge of the terrain.

Setting up and running a small business as a Limited Liability Company (LLP) or private limited company under the protection of limited liability is now more attractive under the Companies Act 2006. The Act aims to provide a straightforward, efficient and cost-effective framework for entrepreneurs in the twenty-first century and imposes similar regulations on LLPs and small and medium-sized private limited liability companies.

A general note: our law is now part of the commercial and social law of the European Union, a common market for capital, labour and goods. EU law applies directly in the member states and cannot be altered or amended by

reference to our earlier or later legislation. Common standards of quality and safety are being imposed on goods and services, procedures are becoming more open and increasing attempts are being made to reduce burdens on the smaller business.

The law stated is at 1 June 2008 but the date label on the law is no indication that it is in force and some legislation, including the 2006 Companies Act, is still in the process of being implemented. If in doubt, seek legal advice. Your local Citizens' Advice Bureau, Consumer Advice Centre, trade or employers' association or Chamber of Commerce may be able to advise you and various government departments publish useful and informative pamphlets.

1

Starting out

Going into business can be simple enough but the financial implications are complicated. Independence is tempting, partnership has its pitfalls and behind the facade of many a private limited liability company is an entrepreneur as fully exposed to outrageous business misfortune as the sole trader.

The choice of business structure, however, is essential to the way you operate. It is the legal framework within which is determined your share of profits and losses and your responsibilities to associates, employees, creditors and anyone investing in your expertise.

Choices

Sole trading

The sole trader is the ultimate entrepreneur. You put your own money on your own expertise, taking out and putting into the business as much money and time as you choose, and you are financially committed to the extent of everything you own. If you fail, creditors can demand payment in full, seizing and selling everything you own, including most personal possessions, or making you bankrupt.

Personal assets can be put beyond the reach of business creditors – for instance, assets can be put into relatives' names with the proviso that they invest in the business – but this reduces flexibility. They may not stand by you and transferring the family home into your spouse's or partner's name can be disastrous if you end up in the courts. Also, there may be liability for tax and/or stamp duty and some transactions can be set aside if you go bankrupt

or defraud creditors. You should therefore seek expert advice before taking action.

Partnership

Partners share problems and profits but the price may be high. The partnership is not a separate legal 'person'. Partnership law is being reviewed, particularly the problems arising from lack of independent legal personality, the break-up of the business on change of ownership and the partners' unlimited liability, but currently you, your partners and the business stand or fall together and an insolvent partner can put the partnership out of business. Partners are jointly and severally liable for all the partnership's commercial obligations, although you are responsible only for your partners' dishonest acts if you are involved in them. When you leave the partnership, you take financial responsibility with you unless you publicly announce the split by notifying business contacts and advertising it in the official *Gazette*.

Partnerships can be based on oral, informal agreements but the law puts a full agreement together if details are not specified. It is therefore best to have a formal, signed and witnessed, agreement. This sets the pattern of your current and future financial life and you should take legal advice before finalising it, so that you and your partners fully understand its implications.

Sleeping partners have the same liability as other partners even if their only involvement is investment in the business in return for a share of profits.

Limited partnership

Partners can put limits on financial commitments but at least one partner must have unlimited liability for business debts. The limited partner has limited rights and can only give general advice, and involvement in the business brings unlimited liability. Essentially the position is that of a lender to the business receiving interest at a rate varying with profits. But the limited partner is not a creditor and can only resign with the other partners' consent, unless other arrangements are agreed.

Limited partnerships must be registered with the Companies Registrar. Registration costs £2 and the Registrar must be notified of changes within 15 days. Details of the limitation and/or change must also be sent to the *Gazette*.

Limited liability partnerships (LLPs)

An LLP is organised like a partnership, but the members (partners) have limited liability. Their duties are specified and include those usually carried out by company directors or secretaries – for instance, signing and filing annual accounts and putting together the statement of business affairs in insolvency.

Disclosure requirements are similar to a company's, including the requirement to file annual returns and notify changes in membership, changes of members' names and addresses and a change in the Registered Office address.

Like companies, LLPs are legal entities separate from their members, so the LLP is liable to the full extent of its assets and members have limited liability. Third parties will usually contract with the LLP rather than with members, but individual members may, in some circumstances, be liable for negligence.

Incorporation is achieved by registration at Companies House and costs £20, or £50 for one-day registration. Members provide the working capital and share the profits. Income is treated similarly to partnership. The LLP is taxed as a partnership and members pay Class 1 and Class 4 National Insurance Contributions (NICS).

Partnerships converting to LLPs receive relief from stamp duty on property transferred in the first year, subject to conditions. New and existing partnerships of two or more persons can incorporate as LLPs but not an existing company.

Franchising

A franchise agreement licenses the franchisor's goodwill through an agreement with the franchisee, who can be a sole trader, partnership or company. The franchisor gives ongoing support and advice, licensing a package of rights – for instance, copyrights, patents and know-how – and monitoring the franchisee, mainly by financial and quality controls. The franchisee pays a fee plus royalties and/or dividends. The franchisee owns the business but must conform with 'house-style' and the franchisor has ultimate control.

The franchise agreement must comply with both UK and EU law relating to unfair competition and restraint of trade, and the law is complicated. You are therefore advised to consult specialists in the field.

Limited companies

Trading as a private limited liability company enables you to enjoy the profits of the business while distancing yourself from its debts and obligations. The company can be formed with one shareholder/director but he or she cannot also be the company secretary.

Incorporation

Incorporating business activities brings the business to life as a separate legal person. Corporate structure facilitates outside investor participation and expansion. Debts are the company's debts and business goes on in spite of the resignation, death or bankruptcy of management and shareholders.

The fastest route to incorporation is to buy a ready-made 'off-the-shelf' company from a registration agent. Existing shareholders resign in favour of your shareholders and you appoint your own director and secretary. You can change the company name, but first check to see that the 'objects' clause of the Memorandum – which covers the activities of the business – fits your business.

You can register a brand new company with Companies House for £20, or £50 for one-day registration, but it involves delays, extra documentation and advertisement in the *Gazette*. The ready-made procedure is straightforward and faster but there are technicalities and you should seek professional advice before buying.

The Memorandum and Articles of Association

The Memorandum of existing companies, 'an old-style' Memorandum, states that the company is in business to make a profit and that the liability of the members (shareholders) is limited to the nominal value of their shares. The Articles deal with the company's internal organisation and its relationship with shareholders and the shareholders with each other. As from October 2009 the provisions in the old-style Memorandum will be treated as provisions in the Articles.

The Memorandum of companies incorporated under the 2006 Companies Act states that the subscribers wish to form a company, that they have agreed to become members and agree to take out at least one share each; the provisions of an earlier company's Memorandum are treated as provisions of the company's Articles.

Directors, shareholders and limited liability

Whoever subscribes for and holds company shares must pay the company for them and responsibility for company debts is limited to the nominal (face or par) value of their shares. If they are fully paid up, the company cannot call on them again, even if the business is insolvent. It is the directors and management who are responsible to the company, shareholders and creditors, but, unlike sole traders and partners, only in specified circumstances. If they do not go beyond the limits of the authority given by the company's Memorandum and Articles and act honestly and reasonably, creditors' claims can only be made against company assets.

Unlimited company shareholders are liable for all company debts, although creditors must go to court before they can obtain payment. LLPs and small companies can now file unaudited accounts with Companies House and do not have to file a members' or directors' report, so the dispensation absolving unlimited companies from the requirement to file certain reports and accounts is less attractive.

EU law

Community law applies directly in the United Kingdom and cannot be altered or amended by reference to our own earlier or later legislation. Changes to our company law mainly apply to public companies but community law has had and continues to have a major impact on our commercial and consumer legislation.

Loans

Sole traders can reduce or increase business capital as they please. Partners can borrow and lend to the business as agreed among themselves. Loans and guarantees made by members to an LLP are considered by Her Majesty's Revenue & Customs (HMRC – also referred to as the Revenue) to be contributions to capital, and details of some loans to directors, and guarantees and securities given by directors, have to be given to, and approved by, shareholders.

When the business borrows money, sole traders' and partners' contingent liability – that is, their ultimate responsibility for business debts – is enlarged

accordingly. Loans to an LLP or company do not affect the partners or directors and shareholders' contingent liability. Additional shareholders and debenture-holders buy a share of existing and future profits, but, like any other lender or investor, their only claim is against company assets.

When the business borrows money, sole traders' and partners' contingent liability – that is, their ultimate responsibility for business debts – is enlarged accordingly. Loans to the company do not affect the directors' and shareholders' contingent liability and additional shareholders and debenture-holders buy a share of existing and future profits, but, like any other lender, their only claim is against company assets.

Retaining control

Partnership or company, the majority rules the business. Without the protection of a shareholders' agreement, majority shareholders can often ride roughshod over minority shareholders' and dissenting directors' objections. Unless otherwise agreed, however, the resignation of dissenting partners dissolves the partnership and in some circumstances a partner can only be bought out or forced out in accordance with the terms, if any, set out in the partnership agreement.

Formalities

Sole traders and partnerships trading in their own names can simply open their doors for business. Paperwork and administration are their own – and the VAT and tax inspectors' – business and the partnership agreement is mainly for the protection and information of the partners.

Partnerships and companies must present accounts in a prescribed form, have an annual audit and keep certain registers. Companies and LLPs must file accounts and annual returns, listing changes made during the year, with the Companies Registrar. Unlimited companies do not have to file reports and accounts but they must send in the annual return. Documents filed with the Registrar are available for public inspection. There is therefore some inevitable publicity for even the smallest company.

Dealing with Companies House

You can now incorporate your limited liability partnership or company by filing the necessary documents electronically through incorporation agents. After incorporation you can register your business name and keep Companies House informed electronically yourself and download company and other searches. Details of the system can be found on the Companies House website (www.companieshouse.org.uk).

Close companies

There is a tax disadvantage for family and director-controlled companies controlled by up to five 'participants' and their 'associates'. Associates include family and nominee shareholders. Participants – that is, anyone with a claim to the company's income or capital – pay additional income tax on some fringe benefits and both participants and associates are liable for income tax on loans.

If loans were made to participators during an accounting period you must notify HMRC that the company is a close company and there could be liability to tax.

Tax comparisons

Sole traders, partners, directors and partnerships pay income tax; companies pay corporation tax. Trading on your own account takes assessment to tax from Schedule E to Schedule D, from the category of an employee to the self-employed. Schedule E taxpayers are taxed at source under PAYE and must fight for tax concessions after tax has been deducted. The Schedule D taxpayer has more control over income, outgoings and tax and, if well advised, can usually retain more earnings.

Sole traders and partners pay the lower self-employed rate of National Insurance Contribution in Class 2 and Class 4. Company directors pay Class 1 contributions as employees and the company contributes as employer. The amount is a percentage of income and varies depending on whether or not the employment is contracted-out.

Sole traders and partners are personally liable for tax on business profits. The company is responsible for its own tax bill and, unless it is a close company, directors and shareholders pay tax only on their own earnings.

Closing down

Sole traders and partners can simply close the doors on the business, but unless they sell out completely – and selling the business can be a complicated matter – the ghost of business failure can follow them into the bankruptcy court.

It is easier to buy and sell shares in your company. If the company or LLP is insolvent, business assets must be liquidated to meet creditors' claims, although creditors have no claim on personal assets unless fraud is proved or there are personal guarantees.

Quick comparisons

Although there are legal restrictions on companies and LLPs, the difference between trading as a sole trader, a partnership or a company is often only one of machinery.

Some concessions have already been made but the life of an LLP and company is still relatively expensive. The gradual implementation of the 2006 Companies Act is making life easier and less expensive for small private companies. But LLPs and companies must still comply with the LLP and Companies Acts and the documents filed with Companies House, which include annual accounts, are of course open to public inspection.

However, LLPs are free to pursue any business venture with the agreement of the majority of the partners. They have no share capital and are therefore not subject to company law rules governing the maintenance of capital.

Sole traders and partners lead less complicated legal lives and can generally choose their own route to success or failure.

The advantages of limited liability and flexibility given to the partners in an LLP are, however, counterbalanced by the lack of privacy, the need for an LLP agreement and legal uncertainty – the structure is new to our law and all eventualities have not yet been covered. Shareholders in private limited companies are in a similar position, but they are not bound by an

LLP agreement and the company operates within a well-developed and sophisticated legal structure.

However, unless you have attached restricted voting rights to shares, a bare majority of your company's shareholders can dictate policy, appoint and set directors' salaries, declare dividends and, subject to rather unclear limitations, ratify the acts of directors. Tax is no longer charged at a lower rate on profits retained in the company than the rate charged on the business income of sole traders and partners, regardless of what they drew in cash, and even limited liability is illusory if you are called upon personally to guarantee business debts.

Statutory references

Companies Acts 1985 and 2006
European Communities Act 1972
Limited Liability Partnership Act 2000
Limited Partnership Act 1907
Partnership Act 1890
Single Market Act 1987

Also see statutory references in Chapter 6.

2

Getting going

The sole trader for the most part goes his or her own way. If you take on partners, disagreement between the partners can force a winding up of the business and you need the protection of ground rules set out in a partnership agreement. As director of a limited company or partner in an LLP you may be even more restricted because you must comply with the LLP and Companies Acts.

Business names

Sole traders and *partners* can trade in their own names or under an additional name indicating they have taken over an existing business. Any other name must be registered with the Registrar of Companies. Almost any name is acceptable unless prohibited or misleading and Notes for Guidance are obtainable from Companies House.

Limited partnerships and *limited liability partnerships* must file the partnership name with the Registrar of Companies. The name must not 'offend' the Secretary of State or be a name the use of which would constitute a criminal offence. Again, suitable names are set out in the Notes for Guidance available from Companies House.

Unless you trade in your own name, the business name and your name must be on all business documents with an address at which service of documents concerning the business is accepted. The business name must also be displayed prominently at business premises. Anyone who does business with you but does not visit the premises must be notified in writing of the business name and address.

The partners' names must be on letterheads. If there are more than 20 partners their names can be omitted, provided the address of the principal place is included and a list of partners' names is available there for inspection during office hours on payment of a reasonable fee.

Companies can use business names showing a continuing connection with the previous proprietor's business.

Companies and LLPs

A brand-new company's name costs £20 on application for incorporation. Changing the name costs £10.

The last word of a company name must be 'limited', or 'cyfyngedig' if the registered office is in Wales. The name must not be 'offensive' to the Secretary of State or one which, if used, would constitute a criminal offence or be the same or similar to that of an existing company.

The Registrar's Index of Company Names should be checked, but it does not show pending applications. You may therefore have to make a change within 12 months of registration if the name is the same or 'too like' an existing company name. If the Secretary of State feels misleading information was given or undertakings and assurances given on registration are not met, he has five years during which he can direct that a change be made.

The Registrar reserves the name pending the passing of a special resolution of 75 per cent of the shareholders, a copy of which must be sent to the Registrar with the registration fee. The name cannot be used until you receive the Registrar's certificate and permission may be withdrawn before issue.

Directors are personally liable on contracts made before issue of the certificate and breach of the regulations applying to business and corporate names is a criminal offence.

The company or LLP's name, registered number, registered office address and the names of the directors or designated partners must be on all business documents, including formal notices, cheques, letters of credit, bills of exchange, promissory notes, endorsements, invoices, receipts and orders for money or goods signed by, or on behalf of, the company or LLP.

The LLP's letterhead must also state that it is a limited liability partnership. If there is more than one business address, you should specify which is the registered office.

The company or LLP's name must be prominently displayed at your main business premises, and LLPs must also display the name prominently and

legibly outside their offices and places of business, including, if a place of business, a partner's home.

Domain names

You should also register a domain name on the internet (see page 174).

Trademarks

Trademarks must be separately registered with the Trade Marks Registry (see Chapter 11).

The partnership agreement

You should have a formal agreement executed in a deed (that is, signed and witnessed) to include:

- **The partnership name and address and the nature of the business.** Business is usually done in the partnership name but implicitly entered into by all the partners, so they are directly liable for business activities. Partnership assets should be put in the partnership's name, or in the name of a maximum of four partners as trustees for the business, to differentiate business assets from personal assets.
- **The date you start and end the partnership.** Fixed period partnerships continue unchanged after the stated date but a single business project partnership ends when the project is completed. If no fixed period or specific business venture is agreed, the partnership ends when a partner gives notice. It is best therefore to state that the partnership can only be terminated by mutual agreement.
- **The amount of capital contributions.** No interest is payable on initial contributions, investments and advances unless stated in the agreement. You should specify whether interest is to be paid on initial contributions before profits are calculated.
- **The bank account.** A statement of who can sign cheques and a provision that payments received for the business are paid into the partnership account.

- **How profits are to be calculated and divided.** In the absence of this clause the partners are entitled to equal shares of cash received, less cash paid, without consideration of book and bad debts, whatever they initially put into the business. It is also advisable to include:
  - the spheres of activity of each partner;
  - whether part-time partners are to draw salaries instead of sharing profits;
  - a provision that drawings can be made against future profits;
  - what items, such as cars, not exclusively used for business, can be charged to expenses.

  You may also want to specify a top limit on expenses and a figure above which no partner can enter into transactions without the other partners' consent.
- **Accounts.** A provision requiring regular accounts and an annual balance sheet showing what is due to the partners in respect of capital, share of profits and salary.
- **A clause** referring partnership disputes to arbitration.
- **A clause** indemnifying a partner for claims arising from partnership activities.
- **A clause** permitting arrangements to be made with creditors through the courts if there are cash flow problems.
- **Dissolution.** Failing agreement to the contrary, the partnership is automatically dissolved on a partner's retirement, death or bankruptcy. You should therefore specify how retiring and deceased partners' shares are to be valued and paid off. Alternatively, you can agree to pay an annuity out of profits.

An LLP's agreement should in addition set out:

- the names of the designated partners;
- which partners are to manage the business;
- how much time each partner should contribute to the business;
- what sort of decisions require the all the partners' agreement;
- the capital contributions while the business is a going concern and (if any) on liquidation;
- dispute resolution;
- details of termination of the LLP;

and provision should be made for amending the agreement.

The agreement is binding and can only be altered with the consent of all the partners. *But* it is a private document recording agreement between the partners. If you are a partner with your name on the letterhead, you are responsible for the firm's actions, debts and liabilities unless outsiders are told you are not.

Bullet points 2 and 9 above are important because for some partnerships a change of partners is a discontinuance of the old partnership and a commencement of a new one for tax purposes. Discontinuance technically dissolves the partnership and the business is taxed as if you had stopped trading and begun again. Each partner is assessed on, and is solely responsible for, the tax on his or her share of partnership profits.

Incorporation

LLPs

The incorporation documents obtainable from Companies House require:

- the LLP's name;
- the address of the registered office in England and Wales, in Wales, or in Scotland, Wales or Northern Ireland;
- the members and designated members' full names, addresses, and dates of birth.

LLPs must have at least two designated members with responsibilities similar to directors. A sole remaining member automatically acquires unlimited liability for partnership debts. If there are more than two members you must state whether two or all of them are to be designated members.

You can, however, be sole director of a company without taking on unlimited liability but you cannot then also serve as Company Secretary.

At the time of writing partners must still apply to the Company Law and Investigations Directorate, 1 Victoria Street, London SW1H 0ET (Tel: 020 7215 0225 – www.uksa.law.uk) for a Confidentiality Order if they do not want to reveal their usual residential address and instead give an alternative address for service of documents, but they must show that disclosure would expose them to actual or serious risk of violence or intimidation. Some authorities, including the police, have access to the residential address.

Details are also available on the Department for Business, Enterprise and Regulatory Reform's website, www.berr.gov.uk.

Companies

As from 1 October 2008 the provisions of a Memorandum of Association (an 'old-style Memorandum') of existing companies are treated as provisions of its Articles and the following incorporation documents must be filed with Companies House.

An *Application for Registration of the Company*, setting out:

- The company's name and registered office address. The name must include the word 'limited' if you are trading for profit and the address must be in England and Wales, or in Scotland, Wales or Northern Ireland to establish domicile for tax purposes.
- That the liability of the shareholders is limited by (their) shares.
- The amount of initial nominal (or authorised) capital and how it is divided into shares (which fixes the fee payable on incorporation). From October 2009 new companies do not have to specify authorised share capital. It will instead be included in the initial statement of capital on incorporation and updated when necessary, eg when new shares are issued.
- That the company is to be a private company.

A *Statement of Capital and Initial Shareholdings*, stating:

- The total number of the company's shares to be taken up by the subscriber(s).
- The total number of shares, their aggregate nominal value and the rights, if any, attached to them.
- The amount to be paid up on the shares and the amount (if any) to be unpaid on account of their nominal value or by way of premium.
- The number and nominal value of each share to be taken by each subscriber on formation.

A *Statement of Proposed Officers* with details of:

- The first director(s), the date of birth, full name, previous names, occupation, other directorships, usual residential address *and* service address for receiving company and legal documents. The service address will be on the public record but the residential address is protected information under the 2006 Companies Act; if the residential address is the service address the fact that the two addresses are the same is protected information.
- The secretary or joint company secretaries, if any – private companies are not now required to have a company secretary. They need only give their name and previous name. The address can be the residential address or the company's registered office address.
- Consent to act signed by the first director(s) and secretary, if any, and the subscriber(s) to the Memorandum (or an agent acting on their behalf).

A *Statement of Compliance with the Requirements on Application for Registration of a Company* signed and dated by the proposed director(s) or company secretary (if any), or by a solicitor dealing with the company's formation and sworn before a commissioner for oaths, a solicitor, a notary public or justice of the peace.

The *Memorandum of Association*, setting out:

- The names of the subscriber(s) who sign the Memorandum;
- That they wish to form a company.
- That they agree to become members/shareholders of the company, and they agree to take at least one share in the company each.
- If there are two or more shareholders, at least two of them must sign the Memorandum.

The *Articles of Association* deal with internal organisation, the company's relationship with shareholders and their relationship with each other, the issue of share capital, the appointment and powers of directors, and proceedings at meetings. New private companies can use shortened and simplified Articles under the 2006 Act. Until October 2009, however, they have to use 'draft model Articles' because the Articles are still under discussion. Finalised Articles will apply to companies that choose to adopt them, to companies

that do not register their own Articles and to companies incorporated on or after 1 October 2009. The new Articles can be entrenched, that is, they can state that some Articles can only be amended or altered if specific conditions are met or procedures followed.

Selling to an LLP or limited company

Promoters are personally liable in any transaction made on behalf of an LLP or company before incorporation unless there is specific agreement to the contrary. As from the date of issue of the Certificate of Incorporation the new LLP or company becomes a body corporate exercising its own powers and must therefore consent to any profit made from the sale of assets to them and full details of the transaction must be disclosed.

Promoters can, however, contract on the basis that they are no longer liable once the contract is put before the designated partners or the company's board of directors or shareholders' general meeting, whether or not the LLP or company adopts the transaction. Once adopted, the preliminary contract is then replaced by a draft agreement which is executed by the LLP or company on incorporation.

Alternatively, they can enter into a contract for the benefit of a not-yet-incorporated LLP or company, provided that the LLP or company is specifically identified in the contract by name or description. On incorporation, the LLP or company will have the same rights and remedies under the contract as if it had been a party to the contract.

Statutory references

Arbitration Acts 1950, 1975 and 1979
Business Names Act 1985
Companies Acts 1985 and 2006
Contracts (Rights of Third Parties) Act 1999
European Communities Act 1972
Income and Corporation Taxes Act 1970 (as amended)
Limited Liability Partnership Act 2000
Limited Partnership Act 1907
Partnership Act 1890
Registration of Business Names Act 1916

3

Money

What you put into the business and what you take out are basic. The sole trader's and partner's freedom to choose their route to profit is counter-balanced by their exposure to personal unlimited liability for business debts, but the directors and management of limited companies are to a large extent protected by the companies legislation.

Sole trader

Business capital is the cash and assets which you put into the business and extra capital can only be raised by way of a loan. Financial commitment is total and takings should not be seen as personal income but as interest-free working and growth capital for the business.

Partnership

Partners are in a similar situation to sole traders but the partners can agree that interest is paid on loans to the business. Failing agreement, there is a 5 per cent limit on advances exceeding initial contributions, unless a different rate can be implied from the custom of the trade or the course of dealing between the partners.

The partnership agreement should therefore specify an annual rate of interest payable on capital from time to time standing to the partners' credit.

The amount should be stated to be an outgoing, and deducted and paid as a business expense before profits and profit shares are calculated.

Certain loans of more than £25,000 including the cost of the credit must comply with the Consumer Credit Act 1974 (see Chapter 9).

You can raise outside capital by taking in a limited partner, whose liability is limited to the amount of the loan. No control is lost because involvement in the business imposes full liability on the limited partner.

Depending on your asset position and profit record, additional capital can also be raised as interest and/or on security.

One partner's signature is acceptable in most transactions but your agreement should specify the amount and the kind of transaction which partners can complete on behalf of the business. Loans secured by a charge or mortgage should be approved by all the partners.

Partnership profits

Unless specified in the agreement:

- profits less expenses are business receipts without taking into account work in progress, stock in trade and book debts;
- profits are divided equally;
- partners cannot draw for current expenses against future profits;
- increases in goodwill are not taken into account.

The agreement should therefore make appropriate provision for the above in the annual accounts.

Corporate capital

A company's capital structure is more complicated. If two directors each contribute £300 to form a company with a nominal or authorised capital of £1,000, each taking £50 shares with a par (or nominal) value of £10 per share, or the sole director of a single-member company puts up £600, taking up 100 shares with a par value of £10 per share, the £600 is the company's *paid-up capital.* The £1,000 is the *nominal or authorised* capital, that is, the maximum share capital which the 'old-style' Memorandum of companies incorporated before 1 October 2008 authorises the company to issue. From

October 2009 new companies will not have to give this figure. It will instead be included in the initial Statement of Capital on incorporation and updated when necessary, eg when new shares are issued.

References to share capital on letterheads and documents must be to paid-up capital. This fixes the minimum value of the net assets which must be raised initially and as far as possible maintained in the business, but usually has no relationship to the value of company assets or the market value of the shares. To see if a company is undercapitalised you must look at the balance sheet.

Corporate profits

Payment for shares can be in cash or in kind, including goodwill, know-how or an undertaking for work or services. The contribution of capital gives a right to a share of distributed profits but does not necessarily fix the proportion to which the contributor is entitled.

Rights attached to shares, including the right to vote and receive dividends, depend on the Memorandum, Articles, and shareholders' agreement, if any. Control is retained if you hold 75 per cent of the voting shares.

Most rights can be varied with the consent of three-quarters of the shareholders affected, by their extraordinary resolution or in accordance with a clause in the Memorandum or Articles. Thereafter, changes can only be made by consent and class rights stated to be unalterable in the Memorandum can only be varied with the consent of all the shareholders or by a scheme of arrangement.

Preference shares have a preference over other shares in repayment of capital and/or dividends which are paid at a fixed percentage rate before ordinary dividends. Unless otherwise stated, dividends are cumulative. Arrears must therefore be paid before ordinary dividends but non-cumulative dividends are lost if not paid when due.

Redeemable preference shares are more like debentures, which are dealt with below.

Share warrants, with or without voting rights, are usually issued only to fully paid-up shareholders, although they are sometimes attached to debentures with an option for future conversion to fully paid-up shares. They are negotiable and if lost, the holder may lose dividends which are usually paid when the coupon attached to the warrant is sent to the company.

Increasing the company's capital

As from 1 October 2009 restrictions on providing financial assistance to potential or actual shareholders to acquire or purchase the company's shares and relevant provisions in the old-style Memorandum will be deemed to be provisions in the Articles and will be removed. Until then increases in capital permitted by an old-style Memorandum must also comply with the Articles but both Memorandum and Articles can, if necessary, be changed.

Under the draft model, Articles of companies incorporated under the 2006 Act; however, the company's capital can be increased by issuing more shares by simple majority resolution. If there is no provision in the Articles for a new issue, an appropriate Article can be added by special resolution of three-quarters of the shareholders. The new capital can be by issue of ordinary, or deferred shares, paid for on instalment terms.

The Registrar must be notified of the increase within 15 days of the passing of the enabling resolution, sent a copy of the resolution with a copy of the minutes and, if changed, copies of the amended Article and a copy of the minutes of the meeting.

Shareholders have pre-emptive rights to new issues in proportion to existing holdings, unless this is excluded by the Articles, payment is not in cash, there is a fixed dividend or the directors are authorised to allot shares.

If there is only one class of shares, the directors can now issue and take up more shares of the same class, grant rights to subscribe for them or issue securities convertible into shares, without first offering them to the other shareholders unless this is prohibited by the Articles.

If there is more than one class of shares the directors can only allot shares if authorised by ordinary shareholders' resolution or the Articles. The authority must specify the maximum number of shares that can be allotted and when the authorisation expires, which must be a maximum of five years from the resolution authorising the allotment or five years from the date of incorporation if specified in the Articles. The authorisation can be renewed for a maximum of five years, or revoked or varied at any time by shareholders' resolution.

If the authority permits the company to make an offer or agreement the directors can continue with the offer or agreement even if shares will or may be allotted after the authority expires.

A copy of the resolution must be sent to the Registrar within 15 days. No capital duty is payable.

The company and its officers are liable to fines of up to £1,000 plus a daily default fine of £100 if shares are allotted without authority. They do not, however, require authorisation to allot shares under an employees' share scheme and the shares do not first have to be offered to other shareholders.

If the Articles have no provision for variation of class rights – there is no such provision in the draft model Articles – the variation must be approved by a three-quarters majority of that class of shareholders; when the rights have been varied, 15 per cent of those shareholders can apply to the court to have the variation cancelled.

Shares cannot be issued at less than par value. If new shares are issued at over par value, the premium must be transferred to a share premium account. This is part of the company's capital and can only be used to write off the expense of another issue, plus any commission paid on the issue of the shares, or for new fully paid up bonus shares.

Reducing the company's capital

A company can currently reduce its capital by buying back its shares if the finance comes out of distributable profits, ie profits available for payment of dividends, the proceeds of a fresh issue of shares or out of capital. When the buy-back is completed, the shares are cancelled. This is effectively a cash distribution to shareholders which can of course be done by way of dividend. But with buy-back, you can maintain or increase earnings or net assets per share.

Transactions in small family-run companies are, however, treated as straightforward sales of shares and the proceeds of sale may be treated as a 'distribution' and taxed as income. If, however, the transaction has a genuine commercial purpose, there may be instead be a Capital Gains Tax (CGT) liability. There are heavy penalties if you make mistakes and expert advice should be sought before taking action.

Private companies can now also redeem fully paid up redeemable shares to the extent of the 'permissible capital payment' (PCP). The PCP is computed in such a way that some or all of the cancelled capital is not replaced and the company's capital is reduced. The payment must, however, use up all available profits and all the proceeds of its available new share issues. Again, this is a complicated procedure and expert advice should be sought.

The company's share capital can also be decreased by passing an ordinary resolution cancelling shares which have not been, or agreed to be, taken up.

As from October 2009 private companies will be able to reduce their capital by a simpler procedure by special resolution supported by a solvency statement from each of the directors.

Loans

Some loans and credit facilities of under £25,000, including the cost of the credit, must comply with the Consumer Credit Act 1974 (see page 132).

Companies

The following loans and credit arrangements made with directors and quasi-loans – payments made on their behalf to a third party where the borrower is liable to reimburse the creditor – require no approval. The restrictions also apply to shadow directors – persons in accordance with whose directions or instructions the directors are accustomed to act:

- Loans, credit transactions and quasi-loans up to £50,000 incurred on company business and to pay the costs of defending a regulatory authority's investigation.
- Loans and quasi-loans up to £10,000.
- Credit transactions up to of £15,000.
- Credit transactions, loans and quasi-loans made by moneylending companies, in the ordinary course of business on the same terms and no greater than the company would have offered to an independent third party of the same financial standing.
- Home loans by a moneylending company in the ordinary course of its business for the borrower's principal private residence on the company's usual terms for loans to employees.

Loans to directors and shadow directors and guarantees and security given by them in connection with loans made to a third party must be approved by shareholders within a reasonable period.

The shareholders must receive a memorandum setting out the nature of the transaction, the amount and purpose of the arrangement and the extent of the

company's liability. This must be available for inspection 15 days before the meeting at the registered office, or if to be approved by written resolution, sent to shareholders with the resolution.

The shareholders' approval is also required for lending or giving collateral to a director or shadow director in return for a benefit from the company.

Company non-cash assets – ie property or an interest in property, other than cash

Shareholders' approval is also required if directors, shadow directors or their 'connections' acquire a substantial non-cash asset from the company or the company acquires a substantial non-cash asset from them.

A non-cash asset – property or an interest in property, other than cash – is substantial if at the time worth over £2,000 and exceeding 10 per cent of the company's net assets, or worth more than £100,000.

Failing disclosure and approval the transaction can be set aside and the director or shadow director may have to account to the company for any profit.

*But s*hareholder approval is not required if the company is in administration or being wound up, unless it is a shareholders' voluntary winding up (see Chapter 13).

'*Connected persons*' are: a director and shadow director's business, professional and civil partner, spouse, person with whom the director or shadow director lives as partner in an enduring family relationship, the partner's child and stepchild under the age of 18 who lives with them, and the director or shadow director's child, stepchild or parents. Also included are companies with which the director and shadow director are associated and of which he or she controls at least one-fifth of the votes at general meetings, a trustee of any trust under which he or she, the family group or associated company are beneficiaries, and the partner of a 'connected person'.

A trust under which *all* the employees can obtain shares is not 'a connected person'.

A private company can assist anyone to acquire or buy its shares by way of gift, loan guarantee, security, indemnity or any other financial assistance.

Currently the company's assets must not be reduced or, if reduced, the loan must come out of distributable profits. The assistance must be given in good faith, in the company's interests and with the shareholders' consent. The directors must make a statutory declaration with details of the transaction and

their opinion as to the company's financial viability and the auditors must state whether the directors' opinion is reasonable. As from October 2009 these restrictions have been abolished.

Fines and penalties

Transactions made in contravention of the legislation may be cancelled. Repayment or restitution may be ordered by the court and company officers can face fines and imprisonment.

Dividends

Dividends must come from profits, not capital. Profits mean accumulated realised profits after account has been taken of depreciation, not previously used for distribution or capitalisation, from which is deducted accumulated realised losses not previously written off.

Dividend declarations are self-contained, so previous losses need not be set against profits and losses, nor do losses on fixed capital have to be made good before profits are ascertained, but you must make up losses of circulating capital.

Loans to companies and LLPs

Trading businesses can borrow and give security without specific provision in the Memorandum and Articles or partnership agreement but both the Memorandum and Articles or the partnership agreement should give the company and its directors or the designated partners the widest possible powers.

Additional capital can be raised by issuing debentures. These can be in a series with similar rights attached or one of a class when the debenture can be transferable or negotiable.

Debentures secured on specific assets are fixed charges. Charges over all business assets, including stock in trade, goodwill and so on, are floating charges. This type of charge permits free dealing with the assets but the charge automatically becomes fixed if the business is wound up or stops

trading, or is in default of the terms of the loan and the debenture-holder proceeds to enforce the security. Separate fixed and floating charges can be created but the floating charge is always enforceable after the fixed charge, whenever made, unless the fixed charge prohibits a loan with prior rights and the lender under the fixed charge knows of the restriction.

The 1989 Companies Act lists the kind of charges which must be registered at Companies House and the Registrar must be notified of repayment. If not registered, debts are valid but only as unsecured debts. Fixed charges on registered land must also be registered under the Land Registration Act 2002 and on unregistered land under the Land Charges Act 1972.

Companies and LLPs must keep their own register of charges at the registered office and it must be available for public inspection. Copies of the charges must also be available at the registered office for inspection by creditors and shareholders or partners.

If the company or LLP is jointly liable with an individual and the loan falls within the Consumer Credit Act 1974, the loan must comply with the Act.

Both companies and LLPs must produce a certificate under the Companies Act as proof that the charge has been registered.

Statutory references

Companies Acts 1985, 1989 and 2006
Consumer Credit Act 1974
Finance Act 1982
Income and Corporation Taxes Act 1970 (as amended)
Insolvency Act (No 2) 1994
Land Charges Act 1972
Land Registration Act 2002
Limited Liability Partnership Act 2000
Limited Partnership Act 1907
Partnership Act 1890

4

Running the business

Sole traders are restricted only by access to capital and their ability to generate profits. Partners and directors share the load but their agreement and cooperation is vital to business success and you may be liable for their incompetence or dishonesty.

Fraud

Sole traders, partnerships and directors can be convicted of fraud if they:

- make a dishonest false representation in words or conduct intending to make a gain or cause someone loss or risk;
- wrongfully fail to disclose information – eg where a professional advisor with a duty to safeguard clients' interests dishonestly profits from their position;
- dishonestly abuse a position – eg by cloning software in order to sell it;
- obtain services dishonestly, *or*
- possess articles, including computer programs, for use in fraud.

Partners' responsibilities

Partners act on behalf of the partnership and their partners. The law implies that they deal with one another fairly and in good faith.

You must therefore account to the business for profits and monies made on business assets and you are liable for any shortfall in payments made by other partners unless the transaction is their personal responsibility. Whatever the partnership agreement states, outsiders can assume partners act for the partnership unless they are informed to the contrary or the transaction is outside the partnership's usual business.

If you do not make specific provision in the agreement the following applies:

- All partners in a trading business can borrow on security and draw, sign, accept and negotiate negotiable instruments; in any other business, they can only draw and endorse ordinary cheques.
- All partners take part in management. If they do not work full time in the business, the partnership can be dissolved – the agreement could permit partners to go into business on their own account, provided they are not in competition with the partnership.
- Decisions are by partners' majority vote – the agreement could therefore have an arbitration clause so decisions can go to arbitration rather than the courts.
- Profits and losses are divided equally – the agreement should therefore make provision for sharing profits, and paying salaries and interest on capital contributions.
- The agreement should state whether business assets are owned wholly or partly by a partner or the partnership. If the partnership is a partner's tenant and this is not in the agreement, the partnership can only be evicted if the partnership is dissolved. Assets acquired after you start trading belong to the partnership if purchased for business use or on its account, but land is a special case. It is classified as 'personal property', not real estate; thus it is considered as a cash sum and must be sold if a partner dies or the partnership is dissolved.

LLPs

Every member/partner is the LLP's agent, so the LLP is bound by anything done by a partner unless:

- the partner had no authority to act in that capacity on the LLP's behalf; and

- the person with whom the member is dealing knows that the partner had no authority to act or did not know that the person was a partner in the LLP.

AND former partners are considered as continuing partners *unless* notification has been given that they have ceased to be partners to:

- the person with whom the former member was dealing; or
- the Registrar.

Third parties will usually contract directly with the LLP, which, like a company, is a separate legal entity. The partners are therefore protected by limited liability although individual partners are liable for fraud and negligence.

LLPs: designated members' responsibilities

Designated members have the same rights and obligations as the other partners but they have in addition a duty to:

- appoint auditors (if required);
- sign the accounts on behalf of the members;
- deliver the accounts to the Registrar;
- notify the Registrar of mortgages and charges;
- notify the Registrar of changes of members/partners, debenture-holders and their details, changes to the registered office address, or the LLP's name, and the place where the Register of Debenture-holders is kept;
- prepare, sign and deliver the Annual Return to the Registrar;
- act on the LLP's behalf if it is wound up or dissolved.

The designated members can be prosecuted and face fines of up to £5,000 for each offence if certain documents are not filed. They may also be disqualified from being a designated member or company director for up to five years.

The partners can decide at any time to appoint any member a designated member on notice delivered to the Registrar, and designated members can resign from office with the agreement of the other members any time after incorporation, but they must inform the Registrar within 14 days of the change.

Directors' responsibilities

Whatever the title, a director is anyone occupying the position of a director and anyone in accordance with whose directions the directors are accustomed to act, except for professional advisers. Directors aged under 16 cannot be registered in Scotland. Currently there is no minimum or maximum age in England and Wales but the young director must be able to sign the consent to act and you should take legal advice if you want to appoint someone very young. *But* as from 1 October 2009 no one under the age of 16 can be a director and anyone under 16 acting as a director will be disqualified. Some foreign nationals are excluded, so check with the Border and Immigration Agency, Lunar House, 40 Wellesley Road, Croydon CR9 2BY (Tel: 0845 101 6677) or their website, www.ind.homeoffice.gov.uk, before appointing a non-British director. There is no longer a requirement that a director holds shares in the company.

Directors are bound by the powers given by the Memorandum and Articles and their responsibility is to the company, not individual shareholders. The draft model Articles under the 2006 Companies Act state they are responsible for managing company business for which purpose they may exercise all the powers of the company. They therefore have unlimited powers to bind and act on behalf of the company and to authorise others to do so, This is, however, subject to any restrictions imposed by the Memorandum and/or Articles and provided everyone acts in good faith, although outsiders are not required to enquire if their powers are in any way restricted.

The 2006 Act specifically requires directors and shadow directors:

- to act within their powers given by the Memorandum and Articles;
- to promote the success of the company;
- to exercise independent judgement;
- to exercise reasonable care, skill and diligence;
- to avoid and disclose – in writing – any conflict of interest;
- not to accept benefits from third parties; and
- to declare their interest in proposed transactions and arrangements.

And the shareholders must be informed about and approve the directors' substantial property transactions with the company and any loans and credit facilities provided by the company to them.

Shareholders can now bring a derivative action on behalf of the company against a director, former director or shadow director for negligence or breach of duty and they can ratify a director's negligence, default, breach of duty or breach of trust, prospectively or retrospectively, unless prohibited by the Articles.

And, if the director obtains judgment, he or she is entitled to be indemnified from company assets against any liability incurred in defending civil or criminal proceedings.

Directors are not responsible for their co-directors' dishonesty. They are, however, personally liable to outsiders, the company and shareholders for anything done without reference to the company – for instance, placing orders without referring to the company or paying by cheque not properly made out in the company's name.

Executive and non-executive directors have the same liability, but only if they are negligent or dishonest and intend to act fraudulently is there a liability for consequential loss caused to the company. Active involvement in a company carrying on business for a fraudulent purpose and continuing to trade when there is no reasonable prospect of creditors being paid can bring a personal liability without limit for all the company's debts and, in addition, a fine and/or imprisonment.

The directors and the company have responsibilities under the employment, industrial training and health and safety legislation and they can be convicted of crimes – for instance, offences under the Road Traffic Acts. The directors are also liable for deficits in the employer's slice of employees' National Insurance Contributions and VAT. Directors are required to take note of employees' as well as shareholders' interests but they must also have regard to the best interests of the company.

Directors and shadow directors' service contracts for over two years, or if not in writing a memorandum setting out their terms, must be available for shareholders' inspection at the registered office or principal place of business and approved by shareholders. If you have not changed the standard Articles or there is no special provision in the service contract, a director can be removed from office by shareholders' majority vote and entitlement to compensation depends on the contract. Directors must give written notice of resignation and appointments of successors must be confirmed by the shareholders. The Articles usually provide for a third of the directors to retire each year in rotation but they can be immediately re-elected and a managing director can only be appointed if permitted by the Articles.

Details of directors' share and debenture dealings must be given to the company within five days of the transaction.

The Registrar must be kept informed of changes to the directors and the registered office and where contracts, memoranda and copies are kept. Directors can be prosecuted if certain documents are not filed or not filed on time and can be fined up to £5,000 for each offence. They are responsible for filing proper accounts and there is a separate civil penalty if the accounts are not filed on time. Directors, shadow directors and anyone who ostensibly acts as a director can also be disqualified from taking part, directly or indirectly, in the promotion, formation or management of a company, and from being a company's liquidator or manager, or receiver or manager of company property for up to 15 years.

The company secretary

Private companies are no longer required to have a company secretary. If you have or wish to appoint one he or she can also be a director – although not sole director – but cannot then sign documents in both capacities. The secretary's liability is similar to a director's but involvement is often confined to administration, including ensuring documents and returns are sent to the Registrar and proper company registers are kept. The secretary cannot commit the company in business transactions unless authorised by the directors.

Single-member companies

The single-shareholder company must also have at least one director and the company secretary, if any, cannot be the sole director. The single shareholder, in person or by proxy, is a quorum for meetings whatever is stated in the Articles and 'meetings' must be minuted and decisions formally notified to the company, unless made by written resolution.

Details of unwritten contracts between the company and the single shareholder/director must be set out in a memorandum or recorded in the minutes of the next directors' meeting, unless the contract is made in the ordinary course of the company's business.

Auditors

LLPs and companies must appoint auditors at any time before the beginning of the first period for appointing auditors – at least 28 days before the day on which copies of the accounts and reports, if any, are circulated or, if earlier, the day on which they are circulated, unless the designated partners or directors decide to deliver unaudited accounts. They continue in office unless dismissed by ordinary (majority) vote of the shareholders or new auditors are appointed.

Accounts

The only purpose of accounts for the *sole trader* and *ordinary partnerships* is to record receipts and payments, profits and losses, and to chart business progress. Annual accounts are then drawn up showing assets and liabilities and, for the partnership, what is due to each partner. Partners must have access to the books but they are not available to anyone else except the inspector of taxes and the VAT inspector.

Businesses with a turnover of under £15,000 can submit simplified three-line accounts to the Revenue showing only annual turnover, total purchases, expenses and the resulting net profit.

The LLP's and the company's first accounts start on the day of incorporation and the first financial year must end on the accounting reference date (ARD) or a date up to seven days either side. It is fixed within nine months of incorporation by notice given to the Registrar. If none is fixed, the ARD is the last day of the month in which the anniversary of incorporation falls. Subsequent accounts end on the next ARD or, again, a date up to seven days either side.

The accounting reference period (ARP) – the date for the financial year – is fixed according to the accounting reference date (ARD) and the first ARP must be for between six and 18 months, beginning with the date of incorporation. Subsequent ARPs are for 12 months.

LLP accounts must at the time of writing be filed 10 months after the relevant ARP and private company accounts nine months after it. If first accounts cover more than 12 months, the period allowed for filing is calculated from the first anniversary of incorporation or three months after the end of the ARP, whichever expires later. If the ARP has been shortened, the accounts can be filed up to three months from the date notice of change was filed.

The designated partners or directors are liable to fines of up to £1,000 if accounts are not filed within the time limits.

'Small' LLPs and companies with a turnover of up to £5.6 million and/or with a balance sheet total of not more than £2.8 million and/or with an average of no more than 50 employees can file Abbreviated Accounts. Two out of three of the criteria categorise the LLP or company and current and preceding years must be taken into account.

You do not have to include the full balance sheet, profit and loss account and designated partners' or directors' report, but you must file:

- a short version of the balance sheet with aggregated amounts for each item except debtors and creditors *and* notes explaining how the figures are made up;
- a special auditor's report – unless you are also claiming audit exemption (see page 35), explanatory notes and a special auditors' report, unless claiming audit exemption.

The balance sheet must include a statement that the accounts are prepared in accordance with Section 441(1) of the Companies Act 2006 relating to small LLPs and companies *and* the auditor's report must state that in their opinion you are entitled to submit abbreviated accounts.

Copies of the full accounts – that is, the balance sheet, profit and loss account, auditor's report and the designated partners' or directors' report must be sent to partners or share- and debenture-holders 21 days before the partners' or shareholders' meetings and to anyone entitled to receive notice of the meetings. They can be sent summary instead of full financial statements if the accounts are audited. Partners or share- and debenture-holders must also receive copies of the last accounts. The accounts can now be prepared in compliance with the accounting requirements of the Limited Liability Partnership Act or Companies Acts (UK GAAP) or the EEC's International Accounting Standards (IAS).

The designated partners or directors are responsible for preparing the annual accounts and for filing them with the Registrar within the required time limits. They are liable to fines and/or imprisonment for accounts that do not comply with the Acts and late filing. Persistent offenders may face disqualification from acting as designated partners or directors for up to 15 years.

LLP and company records must comply with the Limited Liability Partnership and Companies Acts and be specific. They must explain transactions and disclose the financial position of the business with reasonable accuracy. Daily receipts and expenses, sales and purchases and details of stock, assets and liabilities must be recorded. Records must be kept for three years and books must be available at the registered office or other place designated by the partners or directors.

Exemption from audit for small LLPs and companies

Small LLPs and companies entitled to file abbreviated accounts can file unaudited accounts.

As from 6 April 2008 the unaudited balance sheet must include a statement by the designated partners or directors stating that:

- For the year ending… the partnership or company was entitled to the exemption under section 477 of the Companies Act 2006 relating to small companies.
- The members or shareholders have not required the partnership or company to obtain an audit of its accounts for the year in question in accordance with section 476.
- The designated partners or directors acknowledge their responsibilities for complying with the requirements of the Act with respect to accounting records and the preparation of accounts.

The LLP agreement or Articles must permit use of the exemption. Company shareholders with at least 10 per cent of the company's issued capital or of any class of shares can, however, demand an audit on at least a month's notice to the company's registered office given before the end of the financial year.

And it should be borne in mind that banks and credit managers rely on financial information to assess creditworthiness and like to have the reassurance of an independent audit.

The audit exemption for earlier years can be claimed if the accounts are approved by the board and delivered on time but they must then be accompanied by an independent auditor's report prepared by a qualified accountant, who need not be a registered auditor but must be a member of:

- The Institute of Chartered Accountants in England and Wales;
- The Institute of Chartered Accountants of Scotland;
- The Institute of Chartered Accountants in Ireland;
- The Association of Chartered Certified Accountants; or
- The Association of Authorised Public Accountants.

The same accountant can prepare the Accounts and make the report.

Some flat management companies may have to file audited accounts in compliance with the terms of their lease.

Annual returns

LLPs and companies must deliver an annual return to Companies House on the anniversary of incorporation and once every 12 months within 28 days of the date when the return is completed.

The return summarises information in LLP and company records, including principal business activities, the address where some registers are kept if not at the registered office and details of debentures and debenture holders. LLPs must give the partners' addresses; companies must give the addresses of directors, the company secretary, shareholders and former shareholders and their shareholdings, as well as a statement of capital.

Subsequent returns must list changes in principal business activities, the registered office address, the address where the registers are kept, the partners or directors and shareholders and their addresses, and the resignation of company officers. Companies must include changes in capital, new issues and the resignation of company officers, but some details concerning shareholders are only required every three years.

Keeping the shareholders informed

Copies of accounts and reports must be circulated to shareholders and debenture-holders and to anyone entitled to receive notice of meetings, including the auditors. If the company prepares summary financial statements they may, however, choose instead to be sent summaries.

The small company's directors' report must list:

- the names of the directors;
- the qualifying indemnity provisions covering directors; and
- the company's principal activities.

Details will be given on the Companies House and DBERR websites of regulations under the 2006 Act, specifying other items to be included in the directors' report which were previously required under the 1985 Companies Act.

Regulations under the 2006 Act will be given on the Companies House and BERR websites of regulations listing other matters to be included in the reports which were formerly required under the 1985 Companies Act, including valuation of fixed assets, political and charitable contributions, employee involvement, policy and practice concerning creditors, future developments and changes during the financial year.

Partnership meetings

Although partnerships and LLPs are not required to have formal meetings or to make decisions by formal resolution, managing partners and designated members have a personal responsibility to keep members informed about business activities.

Shareholders' meetings

Private companies no longer have to hold Annual General Meetings or any other meeting, except to remove a director or auditor. Contact with shareholders and debenture-holders can be by post, e-mail or the company's website and almost all decisions can be made on written resolutions by simple or 75 per cent majority.

Shareholders acting together can do anything within the powers of the company's Memorandum and Articles, unless prohibited by the Companies Acts, outsiders or creditors are affected, or there is a public interest issue.

If meetings are called, notice must be given of the meeting and the agenda in accordance with the Articles. The draft model Articles specify 14 clear days, unless shareholders holding at least 90 per cent of the voting shares have agreed shorter notice. Twenty-eight days' special notice is required for resolutions to dismiss or appoint new auditors or prevent their reappointment and to remove or replace directors. Notice by post is given when posted and

received 48 hours afterwards. Otherwise it can be given partly or wholly in hard copy, electronically or on the company's website. It must give the time, date and place of the meeting and the general nature of business to be discussed, and website notice must remain on the website until the meeting has concluded. Notice can be waived with the consent of a majority of the shareholders, holding 90 per cent of the voting shares, and its accidental omission does not invalidate proceedings at meetings.

If a quorum – two shareholders or the single shareholder in a single shareholder company or their proxy – is not present within half an hour of the specified time, the meeting must be adjourned to the same time, day and place the following week, or a time and place designated by the directors.

Private companies do not have to serve notice of resolutions provided they can be approved by the company, or any class of shareholders, by the required majority of shareholders entitled to vote. Written resolutions and relevant documentation and information as to voting, the majority required and the date on which they must be passed can be sent as hard copy and/or electronically and/or posted on the company's website and/or, if it would not cause undue delay, by passing resolutions from one recipient to another. Written resolutions cannot be used to remove directors or auditors before the end of their term of office.

Resolutions can be ordinary – passed by a straight majority of shareholders entitled to vote; or special – passed by a three-quarters majority.

Twenty-eight days' special notice is required for *special resolutions* to:

- dismiss or replace a director;
- dismiss auditors;
- appoint new auditors.

Special resolutions must be stated as such. They are required to:

- amend the Articles;
- reduce and to re-denominate share capital;
- approve a payment out of the company's capital for redemption or purchase of its shares;
- opt into or out from automatic suspension of potential barriers to takeovers on a takeover bid;
- resolve on a voluntary winding up – unless the Articles provide that the company be wound up after a fixed time or on a specified event;

- approve the acceptance by the liquidator in a shareholders' voluntary liquidation of shares of another company to which assets of the liquidating company are to transferred;
- give the liquidator in a shareholders' voluntary winding up powers to pay a class of creditors in full or make a compromise or arrangement concerning the company's debts or a debt owed to the company;
- petition to the court for a compulsory winding up.

Copies of special resolutions and resolutions which become part of the company's constitution and affect outsiders, for instance debtors, creditors and prospective shareholders, must be filed with the Registrar within 15 days of the meeting or decision.

Five per cent of the shareholders can at their own expense require the company to circulate a resolution, provided it is not defamatory, frivolous or vexatious or, if passed, would be ineffective, together with an explanatory statement of not more than 1,000 words.The company and anyone claiming to be aggrieved by the resolution can apply for a court order to prevent its circulation.

Under the draft model Articles voting is by a show of hands, but the chair, any two shareholders or a shareholder with at least a tenth of the total voting rights can demand a poll, when voting is usually based on one vote per share. Otherwise proxies are entitled to vote and special voting rights are taken into account before deciding whether a motion is carried. A director's personal interest in a company contract disqualifies the director from voting; if he or she does so the transaction can be set aside.

Directors' and board meetings can be run in any way the directors think fit. In practice, they usually run the company and minutes of their meetings are only available to the directors, the company secretary, if any, and the auditors.

Records must be kept of decisions whether made at meetings or by written resolution, including:

- copies of resolutions;
- minutes of proceedings; and
- details of decisions, including the decisions of the sole shareholder of a sole shareholder company.

The company and officers in default are liable to fines of up to £1,000 and a daily default fine of up to £100 if records are incomplete and/or copies are not sent to the Registrar within the time limits.

Statutory references

Business Names Act 1985
Civil Liability (Contribution) Act 1978
Companies Acts 1985, 1989 and 2006
Company Directors Disqualification Act 1986
Fraud Act 2006
Industrial Training Act 1982
Insolvency Act 1986
Limited Liability Partnership Act 2000
Limited Liability Partnership Regulations 2001
Limited Partnership Act 1890
Registration of Business Names Act 1916
Road Traffic Act 1972
Transport Act 1968

5

Premises

You should seek legal and financial advice before investing in business premises and rent, which can be a substantial investment and a major part of your overheads.

Planning permission

Check whether current use, proposed use or alterations are permitted by the local authority and/or local by-laws and if there have been complaints about use of the premises.

If you need consents it is worth making preliminary investigations yourself. You should also check whether you need anyone else's agreement, including someone with an interest in the premises, such as the freeholder and lessees with tenancies with at least 10 years to run.

Some building does not require planning permission, including, subject to conditions, a 10 per cent addition to cubic content – not square footage. Some changes of use are also permitted, for instance from one shop to another. You need consent for 'material' change, demolition, most building works and 'material' widening of access to the highway, and sometimes for outside advertisements.

If the vendor has outline permission, check that time limits have not been exceeded – full, as opposed to outline, permission normally lasts for five years.

Unauthorised continuous use since the end of 1963 can be regularised with an established use certificate, otherwise it is unlawful. The occupier is liable

for unlawful use and a vendor's undertaking, and indemnity for damages is no protection. Suing for misrepresentation and/or breach of covenant in a lease is expensive and of little value compared with the expense and impact of eviction without notice.

A recent decision under the Human Rights Act struck at the basis of this area of law, where many decisions are made by government. There is currently therefore a question mark over our planning law, and you should take expert advice before proceeding.

Leases

The landlord may have to consent to sale, alteration and/or change of use under an existing lease. Consent must be given within a reasonable time unless it is reasonable to withhold it and the landlord must serve written notice of the decision, specifying any conditions attached to the consent or the reasons for withholding it.

The landlord may have to consent to sale, alterations and/or change of use under an existing lease. Payment cannot be demanded from the incoming tenant, and if there are no structural alterations, the rent should not increase even if permitted by the lease. But the incoming tenant may have to undertake to reinstate premises if this is reasonable and pay for damage or diminution in value to the property or the landlord's adjoining property, as well as legal and other expenses.

The lease can prohibit change of use, alterations and improvements and the landlord can refuse consent unless the lease states consent cannot be 'unreasonably withheld'. Reasonable reasons must be given by the landlord; requiring more than the cost of actual compensation constitutes unreasonable refusal. The landlord cannot unreasonably withhold consent or impose unreasonable conditions if you make a written request to make reasonable alteration to the premises to accommodate disabled employees (see page 111).

An incoming tenant should ensure the vendor has a right to sell or sublet. Landlord and tenant can agree when the landlord can refuse to permit a sale of the lease, for example by forbidding a sale in the first or last three years of the term. They can also agree conditions, for example requiring an incoming tenant to give a personal guarantee. But if the landlord or a third party is unilaterally able to decide when and/or on what conditions the tenant can sell, the terms of the lease must either require the decision to be reasonable or give

a right to have the matter independently decided. If this agreed term in the lease is worded inappropriately the landlord cannot unreasonably withhold consent, whatever the circumstances. If the sale requires the landlord's consent, a suitable tenant must be accepted, unless refusal is reasonable on grounds which would have been valid when the lease was created or it last changed hands. Payment for consent to sale or sublet can be demanded only if permitted by the lease. Consent must be given within a reasonable time unless it is reasonable to withhold it, and the landlord must serve written notice of the decision, specifying any conditions attached to the consent or the reasons for withholding it.

If, unknown to the purchaser, the vendor has no right to sell or sublet, the landlord must accept the purchaser and seek compensation from the vendor, but the purchaser may have to vacate if change of use is in breach of a superior lease or planning consent.

Leases granted for more than seven years must now be registered, otherwise the lease has no legal effect. Assignments of unregistered leases with more than seven years unexpired and the transfer of any registered lease, whatever its remaining length, must also be registered. Landlords consenting to assignment should require the assignee to register the lease, otherwise notices served by the landlord may not be effective. Leases of any length must also be registered if the lease does not commence until more than three months after the grant.

The Landlord and Tenant Act (LTA) 1954 protects business tenants whose (written) lease does not exclude the provisions of sections 24 to 26 of the Act, but some tenants are excluded, eg tenants living on the premises, although they may be protected under the Rent Acts.

The parties can agree to opt out from the Act's protection. The landlord must then serve a Notice – dubbed a 'health warning' – advising the intended tenant not to commit him- or herself to relinquishing statutory protection without professional advice and summarising the legal rights which will be lost. The Notice must be served on the tenant at least 14 days before concluding the tenancy agreement or surrendering a lease, and before the lease is completed or the agreement for a lease is entered into, the tenant must sign a Declaration that the Notice has been received and accepted. If the Notice is served less than 14 days in advance, the tenancy can still be contracted out but the tenant must then make a Statutory Declaration that it has been received and accepted; similar provisions apply to an agreement to surrender a protected lease.

Protected tenants can simply walk away on expiry. If they continue in occupation after the expiry date they must give the landlord three months' notice before leaving; renewal is subject to negotiation and strict formalities and time limits apply.

The landlord must usually give between six and 12 months' notice, setting out the tenant's rights, and serve a Notice to Terminate either:

- terminating the tenancy on a ground contained in the 1954 Act – the grounds are broadly similar to those in commercial leases, including:
  - delay in paying rent;
  - failure to maintain, repair, use or manage the premises;

  and the tenant must move if the landlord:
  - offers suitable alternative accommodation; or
  - has owned the premises for five years and the landlord is to develop or use them;
- *or* specifying the basic terms of the new tenancy.

No response is required *unless* the tenant wants to renew.

The tenant's Request for a New Tenancy must set out the terms of the new tenancy and the landlord must respond within two months with agreement to the new tenancy or stating the ground on which it is opposed.

The Notice to Terminate and Request for a New Tenancy must state the date on which the *new* tenancy is to end. This is the date when, failing agreement, the landlord or tenant can apply for a decision to the County Court. An extension can be agreed, but written agreement is advisable as evidence that the date has been extended.

If neither landlord nor tenant applies to the court, the lease expires and the tenant has no right to remain in the premises.

If an Application is issued, the court manages the case. Proceedings can be delayed for three months, but the parties must in the meantime prepare for the hearing and they will be encouraged to reach agreement, if necessary by independent arbitration. The Application should be protected by notice under the Land Registration Act 2002. Both parties can apply for a decision as to interim market value rent.

The court must grant a tenancy of up to 15 years on similar terms to the old one if the landlord is unable to prove a statutory ground.

It may be cheaper and faster to use the Royal Institute of Chartered Surveyors and Law Society's Professional Arbitration on Court Terms (PACT) arbitration scheme if the only issue is the terms of the new lease.

If the landlord proves his or her case, the tenant must move and is entitled to *compensation for improvements*, provided the tenant served three months' notice of the intention to do the work and the landlord did not object. If there is an objection the tenant can apply to court for a Certificate stating it was reasonable to do the work and again there are time limits.

Continuous occupation for 14 years entitles the tenant to *compensation for disturbance* if the landlord is to let the premises as part of a larger unit or intends to redevelop or use them himself.

Outgoing tenants and their guarantors are automatically released from the covenants when the lease is sold, but their involvement does not necessarily end. If the lease requires the landlord or anyone else to consent to the sale and also requires the outgoing tenant to guarantee the incoming tenant – under an 'authorised guarantee agreement' – the outgoing tenant or the guarantor can be called upon to remedy the incoming tenant's breach of certain covenants. If the outgoing tenant or guarantor then 'remedies the breach', for example by paying the amount or taking the action demanded by the landlord, either can claim a lease of the premises. This overrides the incoming tenant's right to occupy.

NB: These provisions are fenced around with rules and regulations, requiring formal notices to be served on the various parties within specified time limits. Both tenants and landlord should therefore ensure they are fully informed as to the implications of the legislation.

Public access to the Land Registry

Documents held by the Land Registry are open to public inspection but the registrar has a discretion only to allow inspection of some documents, including leases and mortgages. You may want to apply for exemption for commercially or personally sensitive information, such as the identity of your guarantors.

Stamp duty land tax rates

Transfers of non-residential land and buildings

Rate	**Total amount paid**
Zero	£0 to £150,000
1%	Over £150,000 to £250,000
3%	Over £250,000 to £500,000
4%	Over £500,000

New non-residential leases – Duty on rent

Rate	**Net present value of rent (NPV)**
Zero	£0 to £150,000
1%	Over £150,000

The NPV calculation is reduced by £125,00 before applying the 1 per cent rate and duty on the premium is the same as for transfers of land, but special rules apply if rent exceeds £1,600 pa.

Rent arrears

The landlord can seize the tenant's assets – levy distress – and sell them if rent is in arrear but only:

- if the tenant has a continuing tenancy; or
- if the tenancy has ended, during the six months after expiry;

and then only in daylight hours from Monday to Saturday inclusive. The right to levy distress is subject, and without prejudice, to the rights of prior creditors. If the landlord breaks the rules he or she is liable to damages.

NB: Landlord and tenant law is a technical area with infinite possibilities for expensive error, and before taking on a lease you should take legal advice.

Conditions of work

The Health and Safety at Work Act 1974 applies to premises where anyone is employed and covers employees, independent contractors, visitors, trespassers and the general public. You may also be held liable for damages.

The Act is primarily aimed at preventing accidents and imposing fines and penalties and both you and the business can be prosecuted. There is strict (automatic) liability for business activities which affect the health or safety of the public and if there is pollution the local authority can order works to be carried out or close you down. There is no time limit for prosecutions. Serious offences carry unlimited fines and up to two years' imprisonment and there is a continuing daily fine for some offences. It may therefore be helpful to consult the inspectorate and Employment Medical Advisory Service (EMAS) if business activities are likely to cause problems.

You must provide training and an appropriate working environment for disabled employees. This category includes employees suffering from HIV, multiple sclerosis and visual or other impairment. You must take reasonable steps to deal with physical features that act as a barrier to disabled people, taking into account cost and the size and type of the business. For instance, you may have to improve access to toilet and washing facilities, replace stairs with a ramp or provide more legible signs for employees with visual impairment.

Employees must work in reasonable safety and comfort, welfare and catering arrangements and toilet facilities must be clean and safe, and you are responsible for clothing left on the premises. Continuing instruction, information, training and supervision must be provided to protect employees' health and safety, particularly if they are inexperienced or have a poor command of English and they must use the protection and information provided.

Employees working with dangerous substances must be monitored and records kept for at least five years. If some dangerous substances are used, the employer must pay for employees to have regular health checks. Similar obligations apply to workers in the electrical industry.

Employers' liability to employees cannot be excluded or restricted for death or injury caused by defective plant, machinery, equipment or protective clothing and equipment. The liability cannot be delegated, unless it is reasonable to rely on expert advice or information or on the established practice of the trade. Both you and your employees are liable for non-compliance

with the Management of Health and Safety at Work Regulations 1999; if you do not comply with the 1997 Fire Precautions (Workplace) Regulations your employees can claim compensation for consequential injury or illness. The Regulations are on HSE's website www.hse.gov.uk.

If employees are sent to someone else's premises, your responsibility is reduced to taking 'reasonable' care that they have a safe system of work and usually the responsibility then passes to the owner of the premises. Owners of machinery or equipment left on your premises are liable to anyone using it with their consent.

If you employ more than five people, *health, safety, welfare information and emergency safety procedures* must be displayed on the premises and rules about health and safety with details of management's and employees' responsibilities must be set out in a written statement which must be kept up to date. Employees who belong to a trade union can appoint a safety representative who must be consulted about your procedures and he or she can ask for a supervisory safety committee to be appointed. Drivers of vehicles carrying dangerous substances must be informed of the hazards involved and of emergency avoidance action. The information must be displayed in the cab of the vehicle.

Codes of practice covering health and safety procedures are available from The Stationery Office. It is a defence to show that you took all reasonable precautions and exercised due diligence. Accordingly, although non-compliance is not an offence, it can be persuasive evidence against you.

If you manufacture, supply or import goods, plant and machinery, systems of work and methods of handling, storage and transport must be safe, suitable and without risk to health.

Manufacturers, suppliers, installers and anyone responsible for maintenance and handling a defective product are liable to you and anyone employed by you or injured on your premises. The employer, however, still has primary responsibility even if an accident is due to someone else's careless or intentional act.

Designers, manufacturers, importers and suppliers of goods are responsible for them, unless the buyer carries out his or her own safety checks. But, unless you can reasonably rely on someone else's research, you must give proper instructions for use and carry out research to minimise health and safety hazards.

Claims for compensation for personal injury must usually be made within three years of the injury and may be reduced to reflect a claimant's own carelessness. The employer must carry compulsory insurance and a copy of

the policy must be displayed on your premises unless you only employ close relatives or independent contractors. Employees can also claim for industrial injury under the Social Security Act 1975, payable by the Department for Work, Family and Pensions.

Businesses can now be prosecuted under the Corporate Manslaughter and Corporate Homicide Act 2007 and face unlimited fines, publicity and remedial orders for gross failure in the management or organisation of their activities which results in someone's death.

The organisation, not individuals, are prosecuted. The offence is aimed at management and responsibility cannot be delegated.

Management systems and health and safety procedures are taken into account and a substantial part of the failure must have been at a senior level, including central and operational management. Individuals can, however, be prosecuted for gross negligence, manslaughter and health and safety offences.

Employees' responsibilities

Employees must follow reasonable orders and safety regulations and take reasonable care of themselves and anyone else affected by their work. The law assumes they work carefully, competently and reasonably skilfully and take proper care of your property, but if there is an accident you may be liable for employing unsuitable people. Even if you specifically forbid an action, you are usually responsible for damage caused by an employee in the course of his or her employment, although the employee may be wholly or partly liable for his or her own deliberate and voluntary act which puts him- or herself and others at risk.

Employer's vicarious liability

You and your business can be convicted for offences committed by an employee which are regarded as your offences – for instance, if your lorry is on the road with an insecure load – and for an employee's negligence or theft on the job. Offences must be seen in the context of the harm they are designed to avoid and there are some defences, but, broadly, the test is would a reasonable man say:

- that the employee's act is part and parcel of the employment, even though unauthorised or prohibited – *vicarious liability and employer liable*; or
- that it is so divergent as to be plainly alien to it – *employee liable*?

In transactions with businesses – but not consumers – you can exclude civil liability by contract. But it must be reasonable for the risk to fall on the other party and the clause must be clear, unambiguous and brought to the other party's attention before you contract.

Independent contractors and the self-employed

Independent contractors and the self-employed have their own responsibilities. They must not expose co-workers to risk, but even if contracts provide for split liability, all the responsibility falls on one party if the other is unable to pay compensation.

Temporary workers

Responsibility for and to temporary workers depends on whether they have a contract of employment or have worked sufficiently long for you to be considered their employer. If engaged through an agency, you are responsible for them only if there is a personal obligation to do the work or the agency is a placement bureau.

Factories

When employees do manual work for pay the premises are transformed into a factory and brought within the ambit of the Factories Act and the employer in 'control' of the premises takes on occupier's liability. Even running a self-service car wash may give sufficient control, although a 'responsible employee' may also wholly or partly share liability.

The Act aims to protect workers in an industrial environment against risks to which they are exposed daily. There must therefore be a safe system of

work, the premises and access must, so far as is reasonably practicable, be made and kept safe and potentially dangerous machinery must be fenced. Floors, steps, stairs, passages and gangways must be soundly constructed and maintained and, so far as is reasonably practicable, be free from obstruction and substances likely to cause anyone to slip. Liability here may be shared with independent contractors and you should specifically so provide in your contracts with them.

Health and welfare provisions, similar to those applying to offices and shops, are summarised below and the Health and Safety Executive must be given details about the employer, the business, the work and whether any mechanical power is used. Written notification of accidents causing death, or disablement lasting more than three days which precludes normal work, and of certain specified industrial diseases must also be given.

Offices and shops

Under the Offices, Shops and Railway Premises Act 1963:

- An office is any building solely or principally used as an office or for office purposes and to further such activities, including rooms used as staff canteens and storage.
- A shop is premises used for retail trade; and a shop assistant is anyone wholly or mainly engaged to serve customers, take orders or dispatch goods.
- Trade includes buying, selling, retail sale at auction, lending books for profit, hairdressing, barber shops, the sale of refreshments and intoxicating drinks, buildings where wholesalers keep or dispose of stock or to which the public have access to effect their own repairs, premises used to store and sell fuel and staff canteens.

The prospective occupier must give the local authority two copies of a written notice stating his or her intention to take over premises at least a month prior to occupation or use and must notify the local authority of accidents and industrial diseases in accordance with the 1974 Act.

Health and welfare provisions

Again, the aim is to protect workers in their everyday working environment and you must register with the Health and Safety Executive or local authority.

You must assess risks, decide how to manage health and safety and discuss it with your workforce or trade union representatives. The decision is your health and safety policy, employees must be provided with written details and they must be displayed on the premises.

The temperature must be comfortable – at least 16°C or 13°C if severe physical effort is involved. Premises must be clean and sanitary, dirt and refuse must be removed daily, and there are detailed provisions for washing walls and ceilings and redecorating. Drainage must be provided where necessary.

Factories must not be overcrowded and similar provisions apply to the parts of shops and offices which are not open to the public or used for the sale of goods to customers.

Proper and suitable lighting, heating and ventilation must be provided, with sufficient, suitable, clean and properly lit sanitary conveniences. One lavatory and washbasin with hot and cold water must be available for up to five female employees, two for up to 25 and three for up to 50 – rules are different if you have only male employees. You must provide appropriate and secure changing rooms and comfortable facilities for rest and to eat meals. Drinking water must be accessible. First aid supplies must be kept on the premises with a responsible person in charge – a nurse or person qualified in first aid if there are more than 50 employees. Medical supervision may be required if there is a risk of injury to health, new processes or substances are introduced, or young people are employed, and some work related-accidents, diseases and dangerous incidents must be reported to the authorities.

Employees working with computers on your premises and at their home have special protection and you should:

- check the workstation and assess and reduce risks;
- ensure the workstations meet safety requirements;
- arrange for breaks or changes in the work;
- if appropriate, arrange an eye test;
- provide health and safety training and information.

Detailed information is available on the Health and Safety website, hse.gov.uk, and on their infoline: 0845 345 0055. The publications orderline is 01787 881165.

Employer protection

The safety at work scheme should be reviewed annually. Protective clothing and equipment with instructions for use should be provided and employees should be reminded of risks. Emergency and safety procedures and directions for the use of protective clothing and equipment should be displayed on the premises. If use of safety equipment is part of the contract of employment or a provision of works' rules, employees can be fairly dismissed – after due warnings – if they do not observe procedures. You should also have the back-up protection of voluntary and compulsory insurance.

Special legislation for certain trades

Some trades require special licences, and you should therefore check with your local authority as to current requirements.

Premises selling food and/or drink, including off-licences, private members' and social clubs, cinemas and anyone organising occasional entertainments must apply to the local council's Licensing Committee for a premises licence. If alcohol is on sale, the person managing the premises must have a personal liquor licence. Public performance by even one musician, professional or amateur, amplified or not, including performances in church or a private club, must also be licensed. There are some exemptions, including broadcasts, purely background music and unamplified music accompanying folk dancing.

A single application covers licences to sell and supply alcohol and to provide regulated entertainment and late-night refreshment. The permission is set out in a single authorisation, either a 'premises licence', a 'club premises certificate' for qualifying clubs or a 'temporary event notice'.

The local authority can serve abatement notices and impose fixed penalty fines or prosecute owners of licensed premises who ignore warnings to reduce noise levels.

The 2005 Gaming Act requires the local licensing authority to issue:

- licences for casinos, betting offices, race tracks, bingo clubs and adult gaming centres – the person running the premises requires a personal licence;

- permits for members' clubs, licensed premises and family entertainment centres if gambling is to take place or there are gaming machines on the premises;
- Temporary Use Notices and Provisional Statements for occasional events involving gambling.

The Gambling Commission can impose conditions and issue codes of practice but the licensing authority monitors and enforces the legislation and deals with fines and penalties.

Casinos licensed under earlier legislation are unaffected, as their licences will be transferred to the new regime. The licensing authority will continue to register small society lotteries.

Retail shops

You should check with the local authority to find out if there are restrictions on opening hours and if you need permission to load and unload goods before 9 am on Sundays.

'Small shops' with a floor area of less than 280 square metres (3,000 square feet) can stay open as long as they like on Sundays, Easter Sunday and Christmas Day but staff may have special employment rights (see page 98).

Shops in England and Wales with a larger floor area may face more restrictions. Many can only open for a continuous period of six hours between 10 am and 6 pm and cannot open on Easter and Christmas Day. Conspicuous notices of opening hours must be placed inside and outside the shop.

However, Sunday trading rules do not apply to:

- shops selling only or mainly alcohol;
- shops in airports, railway stations and service stations;
- registered pharmacies only selling medicinal products and medical and surgical appliances;
- farm shops mainly selling their own produce;
- shops that wholly or mainly sell motor or bicycle supplies and accessories;
- shops that only supply goods to aircraft or sea-going vessels on arrival at, or departure from, a port, harbour or airport;
- exhibition stands selling goods.

There are substantial fines for failing to comply with the Sunday trading requirements.

Statutory references

Arbitration Act 1996
Christmas Day (Trading) Act 2004
Clean Air Act 1993
Clean Neighbourhoods and Environment Act 2005
Congenital Disabilities Act 1975
Consumer Protection Act 1987
Control of Pollution Act 1974
Corporate Manslaughter and Corporate Homicide Act 2007
Disability Discrimination Acts 1995 and 2005
Employers' Liability (Compulsory Insurance) Act 1969
Employers' Liability (Defective Equipment) Act 1969
Environmental Protection Act 1990
Estate Agency Act 1979
Factories Act 1961
Fatal Accidents Act 1976
Gambling (Amendment) Act 1990
Gambling Act 2005
Health and Safety at Work Act 1974
Land Registration Act 2002
Landlord and Tenant Act 1954 (Part II)
Landlord and Tenant Acts 1927 and 1988
Landlord and Tenant (Covenants) Act 1995
Latent Damage Act 1986
Law Reform (Contributory Negligence) Act 1945
Law Reform (Miscellaneous Provisions) Act 1934
Licensing Act 2003
Limitation Act 1980
Noise Act 1996
Occupiers' Liability Acts 1957 and 1974
Offices, Shops and Railway Premises Act 1963
Race Relations Act 1976
Regulatory Reform (Business Tenancies) (England and Wales) Order 2003

Rent Act 1977
Sex Discrimination Act 1975
Social Security Act 1975
Sunday Trading Act 1994
Town and Country Planning Act 1971
Unfair Contract Terms Act 1977

6

Tax

A short guide to tax is included for completeness, but your first and best adviser is your accountant, who has a broad general knowledge and experience of finance and the law. Accountants are, however, general practitioners and you are advised to ask to be referred to a specialist for difficult questions of law.

The tax bill

Tax is paid on business profits, but the calculation and amount depends on whether you are personally assessed for tax – as sole trader, partner or director – or whether the business is taxed separately. Sole traders and partners pay tax on business profits, but the company pays its own tax.

The tax on business profits for sole traders and partners is paid in three instalments:

1. 'Interim payments' – payments on account on 31 January.
2. A payment on 31 July in the year of assessment; these are usually 50 per cent of the preceding year of assessment's income tax liability, less tax deducted at source.
3. A payment on 31 January following the end of the year of assessment. This comprises the balance of income tax due plus capital gains tax.

No interim payments are due in the year in which you start business, and if you stop trading or profits fall and you think you are liable to less or no tax,

you can make an appropriate claim to Her Majesty's Revenue & Customs (HMRC).

Directors are taxed on their income – that is, salary and dividends. The company pays corporation tax (CT) on profits no later than nine months and one day after the end of the accounting period – that is, on profits for the period for which the company's accounts are drawn up. If you have a close company (see page 7), CT and income tax may also be due on loans to participators and their associates in a close company.

Independent taxation

Married couples are taxed as separate individuals. Income and capital gains are taxed separately. For 2008/09 everyone has a single person's allowance of £5,435, increasing to £9,030 for taxpayers between 65 and 74, and £9,180 for taxpayers over 75. By April 2011 pensioners over 75 will not pay any tax until their annual income reaches £10,000. A married couple living together are entitled to married couple's allowance against their tax bill of £6,535 if either is aged less than 75 and was born before 6 April 1935. This increases to £6,625 if either is aged 75 or over; but these higher allowances are reduced by £1 for every £2 by which income exceeds the £21,800 limit until reduced to the normal allowance; personal allowance is reduced before married couple's allowance and reduces to a minimum of £2,440. The married couple's allowances can be transferred to the spouse paying the higher rate of tax. There is also a blind person's allowance of £1,800.

Child tax credit and working tax credit have replaced working families' and disabled person's tax credits. Rates vary but people on middle incomes may qualify if they pay for childcare. Details can be found on the HMRC website.

Married couples holding joint income-producing assets each bears half the tax on income unless they make a declaration stating assets are not owned equally. Both can claim Enterprise Investment, Venture Capital Trust and Corporate Venturing Scheme reliefs and their own deductions for trading losses, pension contributions and so on. Chargeable gains are also taxed separately.

Self-assessment

Sole traders, partners and companies now calculate their own tax bill or ask HMRC to do it for them.

Self-assessment brings heavy responsibilities for the taxpayer. There is an automatic penalty of at least £100 if returns are filed late or rejected. Interest and a surcharge is charged on tax paid late. HMRC pays interest at the same rate on overpayment, which is treated as business income and is therefore taxable.

There are fines of up to £3,000 if you cannot produce evidence to support your calculations. All documents relevant to tax affairs should therefore be retained, such as incidental receipts and details of taxable benefits, including tips and expenses. Traders should retain copies of sale and purchase invoices and a daily record of goods taken from stock for private use and goods and services bartered with other traders. If telephones and cars are for both private and business use, itemised bills should be appropriately marked to show which charges relate to the business. The self-employed and companies should retain these records for six years from 31 January following the tax year and employees for about two years, or from the end of the accounting period, and employers for three years. HMRC can take proceedings up to 21 years after the end of a company's accounting period if there is negligence or fraud and can charge a tax-related penalty of up to a maximum of the understated tax.

Tax and the European Union

Basic elements for the harmonisation of *corporate* tax systems have been agreed, but have not yet been implemented.

The uniform business rate (UBR)

This is a local property tax paid by occupiers of business premises based on rateable value (RV), which is determined by market rents and updated (revalued) every five years. The most recent revaluation came into effect on 1 April 2005; a new valuation is due on 1 April 2010. If you use part of your home for business, you may be liable for business rates on that part. The

extent of business use must, however, be clearly identifiable – for instance, business use of a specific room or garage – and you may be able to set off the expenses on that part of your home against your income tax bill.

The local council works out the bill by multiplying the RV by the multiplier or UBR, set by the government every 1 April. The UBR is linked to inflation and expressed as pence in the pound. From April 2008 the higher standard multiplier is 46.2p and the multiplier applying to businesses eligible for small business rate relief is 44.8p. With an RV of £10,000, the small business bill is £4,580, before applying transitional or other reliefs.

Business rates are not payable in the first three months on empty premises, and six months for some industrial premises. Thereafter the full basic occupied business rate is payable.

Details of the charge for England and Wales are on www.voa.gov.uk and www. businesslink.gov.uk. Information for Scotland is on www.saa.gov.uk. Your local Valuation Officer can advise you how to appeal if you think you are paying too much.

The sole trader and the partnership

The sole trader and the partners are personally liable for tax on business profits, and retiring partners take their tax liability with them. If they die, it passes to their estates.

If you are self-employed you must register with the Revenue within three months of starting work or you may have to pay a fine of £100. Details are available on 08459 15 45 15; if you do construction work you may have to register with the Construction Industry Scheme and obtain a Subcontractors Tax Certificate or Registration Card. Details are available at your local Inland Revenue Office or on the Subcontractors' helpline, 0845 300 0581.

Although the partners are separately assessed to income tax, the partnership must send in a Partnership (Tax) Return setting out the partnership's profits or losses and showing how they are divided between the partners.

If annual turnover is less than £15,000, you do not have to provide detailed accounts and information in your tax return. You can instead state your profit or loss based on turnover, including business receipts, goods taken for personal use and balancing charges *less* expenses allowable for tax, including capital allowances.

The sole trader is taxed as if business income is his or her income. Both sole traders and partners are personally liable for tax deducted from employees' pay and partners are personally liable for tax on their share of partnership income, which must be included in their tax return.

For your first year, you pay tax on a current-year basis on profits from your start date to the following April. The second period is generally 12 months ending on a date that is then your usual 'year end' or 'accounting' date.

Some business expenses, such as wages, rent and rates, qualify for tax relief if incurred not more than three years before you start trading.

For 2008/09 sole traders and partners – like employees – pay tax on income less personal tax reliefs at 20 per cent (the basic rate) on the first £36,000 of earned income excluding dividends and 40 per cent (the higher rate) thereafter. From 6 April 2009 the higher rate threshold rises to £43,000.

Basic rate taxpayers pay an additional 10 per cent income tax on dividends and higher rate taxpayers 32.5 per cent on dividends exceeding £36,000.

Unlike employees, sole traders and partnerships can deduct from profits day-to-day (revenue) expenses wholly and exclusively incurred in carrying on business. The previous year's losses are also deductible against income. Any balance remaining can be carried forward and set off against future profits or carried back and set off against earlier profits. Losses in the first four years' trading can be set off against earlier income from any other source in the three years before starting the new business, and a limited partner is entitled to tax relief for the full amount of his or her share of the loss, even if it exceeds the original contribution.

Allowable business expenses

The main expenses that can be deducted from profits as revenue expenses are:

- Running costs, including heating, lighting, rent, rates, telephone, postage, advertising, special clothing, cleaning and repairs, but *not* improvements (a capital expense). If you live on your business premises, you can claim a proportion, but may then be liable to CGT and business rates.
- Research and development (R&D) costs. You can claim a deduction of 175 per cent (instead of 100 per cent) of qualifying expenditure for

2008/09 subject to state aid approval. If the company is not making profits you can exchange qualifying R&D losses for a cash payment from the government. Staff wages and relevant consumables constitute qualifying expenditure, as well as some costs of subcontracting R&D.

- Goods bought for resale and materials for manufacturing, but *not* plant, cars or machinery (capital expenses), although some smaller items may be allowable.
- Carriage, packing and delivery costs.
- Wages, including your spouse's and the directors', but *not* a sole traders or the partners'.
- Interest on business loans and overdrafts, but *not* on partners' advances.
- Charges for hire, hire purchase and leasing, but *not* the cost price (a capital expense).
- Insurance, but *not* NICs or your life insurance.
- Premiums for employees' liability insurance, including directors' and officers' liability and professional indemnity insurance, and payment of work-related uninsured liabilities.
- Subscriptions to professional and trade organisations.
- Expenses of business trips, but *not* travel between home and a fixed place of work.
- Car running expenses, plus the cost of fuel used for business purposes. Up to £5 (£10 when abroad) for employees' personal expenses when away from home on business.
- Other overseas expenses – weekend and overnight conferences – may also be deductible.
- The cost of an annual staff party to a maximum of £150 per head per annum.
- Some professional fees, eg audit fees, legal advice and the cost of legal proceedings relating to the business, but *not* penalties for breaking the law, eg fines.
- Bad debts, but *not* a general provision for a percentage of unspecified bad debts.
- VAT on business expenses, eg petrol, but *not* if you are a taxable trader for VAT purposes.
- Charitable gifts, including gifts of shares to charities.
- Long service awards after at least 20 years' service of £50 for each year of service.

- Business gifts, but not cash of up to £50 per annum to any one recipient.
- Donations to Learning and Skills Councils.

Companies' allowable expenses against profits are similar to those for the sole trader and partnership, except you can also deduct directors' pay. If there is no dispute, the company can claim repayment of income tax (eg deducted at source on interest received) and tax credits (on UK dividends) before profits are agreed.

Homeworkers

Payments of up to £2 a week to employees working at home are not taxable. Anything over £2 is taxable, unless there is evidence of additional household costs.

Business Premises Renovation Allowance

Businesses in designated disadvantaged areas can claim 100 per cent capital allowances on the cost of renovating or converting business properties that have been vacant for more than one year if the costs are incurred on or after 11 April 2007.

Capital allowances

For both income tax and CT, the depreciation to be deducted in the accounts is replaced by capital allowances, which are deducted from the tax bill. The main capital allowances are:

- *Private cars:* 100 per cent first year allowance (FYA) for:
  - new cars for business use with CO_2 a maximum of 110 grams per kilometre plus 20 per cent pa writing down allowance (WDA) on the reducing balance to a maximum of £3,000 pa per car; from April 2009 the WDA on cars with CO_2 emissions above 160 grams per kilometre will be 10 per cent, increasing to 20 per cent on cars with less than 160 grams per kilometre.

- gas and hydrogen refuelling equipment at refuelling stations *provided* the car is unused, not second-hand and first registered on or after 17 April 2002, or is an electric car and purchased between 17 April 2002 and 31 March 2008;
- cars costing over £12,000 – annual allowance of not more than £3,000.

Allowances for leased or hired cars are restricted unless they have low CO_2 emissions if the contract is concluded and the hire period begins 1 April 2008

CO_2 emission figures are on the vehicle registration document or obtainable from the Vehicle Certification Agency's website, www.vc.go.uk.

- *Plant and machinery:* Energy efficient and environmentally beneficial technologies (ECAs), ie natural gas and hydrogen refuelling equipment purchased between 17 April 2002 and 31 March 2008, 'green' technology assets for leasing, letting or hire, and energy-saving and water-efficient plant and machinery: 100 per cent FYA, thereafter 20 per cent pa on the reducing balance *or* 10 per cent pa for long-life assets, ie plant and machinery with a useful economic life of more than 25 years. From April 2008 a loss attributable to the enhanced capital allowance on ECAs can be surrendered for a cash payment of 19 per cent of the loss to cover the liability for PAYE and NICs to a maximum of £250,000.

  A 10 per cent WDA is to be introduced for features integral to buildings, eg lifts and electrical and lighting systems.

  From April 2008 an annual investment allowance – effectively an FYA – of 100 per cent of the first £50,000 of expenditure on plant and machinery, including integral features and long-life assets but not cars, is proposed.
- *Industrial Building Allowances (IBAs) and Agricultural Building Allowances (ABAs)* previously at the rate of 4 per cent per annum are to be reduced between 2008 and 2011 by 1 per cent per annum. Transitional measures have been outlined for transfers of buildings between 21 March 2007 and 2011 so buyers can claim the allowance previously claimed by sellers. The 100 per cent allowance for commercial and industrial buildings in an enterprise zone (EZA) will continue to qualify for a 100 per cent allowance until 2010/11.

- *Hire purchase and lease agreements:* Capital allowances can be claimed on the deposit; the rest of the capital cost qualifies for allowances when the equipment is used. Tax relief for rental payments can be deducted for the years in which payments are made but hire purchase contract rules apply if the lease provides that the lessee shall or may become the owner*;* the lessee may also be able to claim capital allowances if it is a long funding lease of over five years.

Companies must disclaim allowances if they do not wish to use them, but claims can be amended at a later stage.

Research and development (R&D)

R&D allowances (RDAs) apply to capital expendure, ie purchases of equipment, *not* land and dwellings. RDAs are normally 100 per cent of qualifying expenditure, but if a disposal for value is brought into account for the expenditure in the chargeable period, the RDA is 100 per cent of the expenditure less the disposal value.

You do not have to claim the full 100 per cent but you cannot claim the balance at a later stage. There is no balancing allowance. There is a balancing charge if there is a later disposal event which exceeds the amount of unclaimed RDA. The balancing charge is the lesser of the amount by which the disposal value exceeds unclaimed RDA, and the RDA.

R&D tax credits – the small and medium-sized companies (SME) scheme

This allows a deduction for SMEs, not sole traders or partnerships, of 175 per cent of qualifying expenditure on R&D in calculating taxable profits. The company must have fewer than 500 employees and annual turnover of under £50 million or a balance sheet total under £43 million. *But* the increase from 150 to 175 per cent has to be approved by the European Commission.

Qualifying conditions include:

- There must be annual R&D qualifying expenditure of at least £10,000.

- The company must be entitled to ownership of any intellectual property.
- This must be the only notified state aid for the project.
- No credit can be claimed for expenditure funded by someone else.
- There must be no contract to carry out the activities.

But if the last three conditions are not met you may be able to claim 130 per cent of qualifying expenditure under the large company scheme. This requires the work to be relevant to your trade and to be revenue expenditure incurred on either:

- consumable items;
- consumable stores;
- software;
- staffing;
- external provided workers.

Or it requires the work to be relevant to your trade and to be revenue expenditure on work contracted by your company to be carried out by:

- a qualifying body;
- an individual;
- a partnership, each member of which is an individual.

Details of both schemes can be found on HMRC's website.

Rollover relief

This relief allows tax arising on the sale of business assets to be deferred or 'rolled over' if the proceeds are used to acquire another qualifying business asset.

Claims can be made up to five years from the 31 January in the year following the tax year when: the old asset is disposed of, or – if later – the new asset is acquired.

The deferred charge is reinstated when the replacement asset is sold.

Stock relief

Stock must be valued at each accounting date. To take account of inflation, HMRC allows a relief calculated by applying the increase in value (based on the 'All Stocks Index' to March 1984) to the value at the beginning of the period. Special provisions apply to the first period of trading and you can make a partial claim or apply for succession relief.

Benefits in kind

Directors and employees whose annual salary is £8,500 and over (including benefits) have to pay tax on their income, plus the cash equivalent of the benefit.

Exemptions for computers and mobile phones loaned to employees

Employees loaned a computer for private use are liable to tax. They are not liable for tax on the loan of one mobile phone but will be charged to tax if they borrow a second phone.

Employee computer use

Unlike most assets loaned to employees, you do not have to pay tax or NICs on the value of computers worth up to £2,500 loaned to employees for business purposes and no tax is payable if employees later buy the computer from you at market value.

Company car taxation

Employees, including directors, earning at least £8,500 pay tax on private use of a company car, including journeys to and from work. For 2008/09 the tax payable is calculated by multiplying the price of the car – usually the list price plus accessories and VAT, less capital contributions – by the 'appropriate percentage' based on the car's approved CO_2 emissions figure, with some supplements and reductions to take account of the different fuels set out in Table 6.1.

Table 6.1 Tax on private use of company cars first registered on or after 1 January 1998

Fuel type	P11 code	Standard adjustment from 2006/07	Other adjustments
Petrol	P	none	none
Diesel (not Euro IV)	D	Supplement 3%	none
Diesel Euro IV first registered on or before 31 Dec 05	L	Cancel type D supplement above	none
Diesel (Euro IV) first registered on or after 1 Jan 06	L	Supplement 3% (as Type D)	none
Electric only	E	Reduction 6%	none
Hybrid electric	H	Reduction 3%	none
Gas only	B	Reduction 2%	none
Bi-fuel with CO_2 emissions figure for gas	B	Reduction 2%	use lowest CO_2 figure
Bi-fuel conversion, other Bi-fuel conversion or other fuel not within type B	C	none	none

NB:

1. Diesel cars must meet approved Euro IV emissions standards.
2. Hybrid electric cars have an internal combustion engine and a battery electric system capable of propelling the car. The vehicle's documentation must make it clear that the car is a hybrid electric car.
3. Bi-fuel cars first registered on or after.
4. Subject to the overall maximum of 35 per cent.
5. Adjustment for all years from 2002/03: use lowest CO_2 figure.
6. The appropriate percentage for cars with automatic transmission first registered on or after 1 January used by employees with a disabled person's badge is based on the approved CO_2 emissions figure of the closest manual equivalent.

From April 2008 the lower threshold – the CO_2 emissions figure setting the appropriate percentage for *all* cars – is 135 and there is a new:

- '10 per cent band' for cars with a CO_2 emissions figure of exactly 120 g/km or less – 'qualifying low-emissions cars' or QUALECs. Diesel adjustments apply but no other reductions; normal rounding up does not apply. Thus, the appropriate percentage for a QUALEC to which the diesel supplement applies is 13 per cent; 10 per cent applies to *all* other cars. Electric-only cars retain their appropriate percentage.
- 2 per cent reduction for cars manufactured to run on E85 fuel – type G on forms P46(car) and P11D.

Table 6.2 Cars without approved CO_2 emissions figure

Cylinder capacity	Appropriate percentage
1400 or less	15
1401–2000	25
Over 2000	35
Cars with no pinternal combustion engine with reciprocating pistons.	
if propelled solely by electricity eg battery	15
otherwise	35

Van benefit

From April 2008 employees pay £3,000 for the use of vans available for private use, including journeys to and from work.

Fuel-only mileage rates

Employees using their own cars for business can claim the fuel allowances in Table 6.3 based on HMRC's Advisory Fuel Rates for Company Cars from 1 January 2008.

Table 6.3 Rates for tax and NIC free mileage allowances for employees using their own vehicle

	Rate per mile
Cars up to 10,000 business miles	40p
Cars over 10,000 business miles	25p
Motor cycles	24p
Business passengers	5p
Bicycles	20p

NB The amounts are accepted for VAT purposes if employers retain receipts

VAT scale charge: VAT due per quarter per car

VAT scale charges are as shown in Table 6.4. From 1 May 2008 the charge is based on the car's CO_2 emissions. A different amount applies for each 5g/km increase between 135g/km (minimum) and 235g/km (maximum).

Table 6.4 VAT scale charges per three-month period for private use of business fuel

CO_2 emissions rating	Net expenditure	VAT payable
120 or less	£117.45	£20.55
121–139	£176.17	£30.83
Rising per 5g/km by approx £11.74*		£2.05
235 or above	£411.06	£71.94

* exact amounts are obtainable from the HMRC website

Congestion charges

The London congestion charge is part of your business travelling expense and is deductible for tax purposes if it is wholly and exclusively incurred for the purpose of business. Employees can be reimbursed without incurring any liability to tax if you obtain a 'dispensation' from your PAYE tax office. Other cities are considering imposing a similar charge.

The Small Firm's Guarantee Scheme (SFLG)

The SFLG, funded by the Department for Business, Enterprise and Regulatory Reform (BERR), offers loans of up to £250,000 for up to 10 years to businesses established for five years with an annual turnover of up to £5.6 million. The loan is covered by a guarantee paid for by the borrower by adding a 2 per cent premium to the amount of the loan.

Outside investment

The Enterprise Investment, Venture Capital Trust and Corporate Venturing Schemes are only available to companies with less than 50 full-time employees at the date the relevant shares are issued and there is no tax relief if the company has raised at least £2 million under any of the schemes in the previous 12 months.

The Enterprise Investment Scheme (EIS)

The EIS is a form of high-risk, high-return sponsorship where an outsider invests between £500 and an annual maximum of £500,000 in unquoted company shares to fund a start-up business and retains the shares for three years. The various income tax (IT) and CGT reliefs include:

- income tax relief at 20 per cent on up to half the amount invested in the first six months of the year to a maximum of £50,000 can be carried back to the previous tax year *but* dividends are taxable and the relief is clawed back if the shares are sold within three years;
- relief for any allowable losses against income *or* chargeable gains;
- loss on disposal of shares – an allowable loss for CGT purposes;
- deferral of CGT on disposal if the gain is reinvested in shares.

No inheritance tax is payable if the shares are held for two years. The scheme covers most businesses, but some are excluded, including financial services and overseas companies.

The Venture Capital Trust (VCT) Scheme

VCTs are companies listed on the Stock Exchange that invest in small higher-risk unquoted trading companies. The Scheme covers the same businesses as the EIS and the investor can spread the risk over several qualifying companies obtaining:

- income tax relief at 30 per cent on an investment in new ordinary shares with an annual limit of £200,000 – the shares must be retained for at least five years;

- deferral of CGT on disposal if the gain is invested in shares for which IT relief is obtained;
- exemption from CGT on disposal of ordinary shares;
- exemption from IT on ordinary share dividends.

Corporate Venturing Scheme (CVS)

This is another tax incentive scheme to encourage companies to invest in small higher-risk unquoted trading companies, enabling the investor company to:

- obtain corporation tax relief at 20 per cent on amounts invested in new ordinary shares held for at least three years;
- defer tax on gains which are reinvested in another shareholding under the scheme;
- claim relief against income tax for capital losses net of corporation tax relief on disposals of shares.

Some small companies whose income mainly derives from licence fees and royalties are included in the Scheme. The corporate investor's maximum stake cannot exceed 30 per cent and individual shareholders in the small company must retain at least 20 per cent of the small companies share capital.

Corporation tax (CT)

The rates of CT for 2008/09 are shown in Table 6.5.

Table 6.5 Corporation tax rates

Small company rate	20%	on	£0–300,000
Marginal relief		on	£300,000–£1.5 million
Main rate	30%	on	£1.5 million plus

The marginal relief fraction for profits between £300,000 and £1.5 million is 1/400 (27.5 per cent).

The small company rate is to increase to 22 per cent and the main rate to be reduced to 28 per cent as from 1 April 2009.

Profits are adjusted by the various allowances and deductions to calculate taxable profit for CT are based on the relevant accounting period. Losses can be carried back against the previous year's profits. A three-year carry-back is available for losses arising in the last 12 months before cessation.

A notice to deliver the Company Tax Return is sent to the company between three and seven weeks after the end of its accounting period, requiring the completed Tax Return for a period of not more than 12 months to be sent to HMRC by the statutory filing date, ie within three months of receipt of the Notice or 12 months after the end of the accounting period, depending on when the Notice is received and the company's accounting date.

The Tax Return is a self-assessment of the company's tax liability and you must send in accounts drawn up in accordance with the Companies Acts or computations showing how the figures have been arrived at from the figures in the accounts, and the other documents required by the Companies Acts, such as the directors' report, the auditors' report and details of close company's loans to participators and their associates.

Profits are adjusted by the various allowances and deductions to calculate taxable profit for CT based on the relevant accounting period.

Accounting records should be retained for at least six years from the end of the accounting period, either originals or an acceptable alternative form, eg in an optical imaging system or other system which shows you have made a complete and correct Company Tax Return and you must retain original vouchers for tax deducted or tax credits.

Payment is made in a lump sum nine months after the end of the accounting period electronically through BACS and CHAPS or by GIRO or cheque to your company's Inland Revenue Accounts Office at Cumbernauld or Shipley. Interest on late payments is a deductible business cost and interest paid by HMRC on early payments and over-payments is taxed as income.

The Revenue has at least 12 months to question the assessment. The company is notified of an enquiry and when it finishes and of any adjustments in the tax due.

Contact your local HMRC Enquiry Centre if in doubt as to the deadline for payment or what has to be done.

Employees can buy, or acquire options to buy, company shares under various schemes. Savings attract tax-free bonuses, and there are tax advantages for the company and employees when shares are sold at a profit, but before setting up a scheme you should take expert advice.

Inheritance tax (IHT)

IHT for 2008/09 on lifetime gifts over £312,000 is 40 per cent, but no IHT is payable on transfers over £312,000 unless made within seven years of death. The threshold increases to £325,000 in 2009/10 and £350,000 in 2010/11.

There is no IHT on gifts up to £3,000 in each tax year and you can carry forward all or part of the £3,000 exemption you do not use to the next year. Transfers into a company above the IHT nil rate band, taking into account chargeable gifts and transfers made in the previous seven years, are chargeable to 20 per cent IHT on the excess. If the donor dies within seven years of the transfer on which 20 per cent IHT has been paid, the IHT payable is recalculated based on the rate applicable on death. If no IHT was due, the amount of the transfer is added to the deceased's estate in calculating the IT. A surviving spouse or civil partner can, however, make use of the deceased's unused IHT nil rate band.

Capital Gains Tax (CGT)

Capital gains for individuals and companies are taxed as income. The amount chargeable to CGT is added to the individual's income and is taxed at the rate paid on the top slice of income. Companies pay at the CT rate. Disposals for 2008/09 are exempt where the real or notional gain is less than £9,600. Thereafter CGT is chargeable at 18 per cent. There is no longer any tapering relief or indexation allowance but 'Entrepreneur's relief' at a reduced 10 per cent rate is chargeable on a lifetime allowance of £1 million as from 5 April 2008.

Disposal of the business is liable to tax, but if you sell and buy another business within three years, you can defer payment until you finally dispose of the new business and stop trading. The relief is particularly helpful if you have been using your home as business premises and claiming tax relief for part of the running expenses.

Value Added Tax (VAT)

As from 1 April 2008 if annual taxable outputs of the business (charges for goods and services) exceed or are likely to exceed £67,000 including VAT, you must register with HMRC for VAT. The limit is based on the past 12 months' turnover and if at the end of a month, taxable supplies in the last 12 months exceed the limit or might do so in the next 30 days, registration is compulsory. You can apply for registration if turnover is below the limit but there is a discretion to refuse it.

If you think your annual turnover will not reach £65,000 excluding VAT, you can apply for cancellation.

You can account for VAT based on actual receipts and payments instead of invoice dates if your annual turnover excluding VAT does not exceed £1.35 million. You can continue on this basis for six months after annual turnover excluding VAT reaches £1.6 million.

If you have not registered for VAT and dispose of capital assets and obtain a VAT refund you may have to pay over the VAT to HMRC.

Invoices must show your VAT-registered number and details of sales including the rate charged and the amount and they must be available for inspection. VAT returns must be completed at the end of the VAT accounting period to show total outputs and the VAT charged. Against this is set total inputs and the VAT paid. If outputs exceed inputs, the balance must be paid to HMRC and if you paid out more than you received, you can claim the difference.

Loans, some property transactions, insurance and some types of education and training are exempt from VAT and are not part of taxable turnover. Some services from abroad, such as advertising, data processing, consultancy and legal, accounting and professional services, are treated as if you supplied them and included in your taxable turnover.

There are special schemes for retailers and special rules for discounts, free gifts, samples, hire purchase and 'self-supply'. The 'flat rate scheme' for businesses with annual turnover excluding VAT of less than £150,000 or annual 'total turnover' of under £187,500 permits you to calculate your VAT payment as a flat rate percentage of turnover. 'Total turnover' is the value including VAT of all business supplies, including exempt and non-business income and the percentage is decided according to the type of business. Some property conversion, renovation work and installations of energy-saving materials and heating equipment are liable to VAT at 5 per cent instead of the usual 17.5 per cent rate. Bad debt relief is available.

Records must be kept for three years, increasing to four years on 1 April 2010, and you complete your obligation as your own tax collector when you post the completed form and appropriate payment to the HMRC.

Up-to-date information is available at www.hmrc.gov.uk and from the National Advice Service on 0845 020 9000.

PAYE

Employers are responsible for deducting PAYE from wages and paying it over monthly to HMRC – including PAYE from their own salary. Small employers with a monthly bill for PAYE and NICs of less than £1,500 a month can pay quarterly. Deductions are based on the tax code number and HMRC supply tables. Employees must receive Form P60 with details of pay and tax deductions at the end of the tax year. Form P35 goes to HMRC, summarising their tax and NICs. Leaving employees must receive a P45 – part of which goes to your tax office – to hand to their new employer to ensure the tax record continues.

National Insurance Contributions (NICs)

All employees over the age of 16 and under State Pension age and their employers pay NICs. If you earn more than £105 a week payments build up entitlement to social security benefits, including the State Pension. Rates for the tax year 2008/09 are shown in Table 6.6.

The State Pension age is currently 65 for men and 60 for women. For women it rises gradually to 65 from 2010 to 2020 and thereafter it will rise gradually for both men and women from 65 to 68 by 2046.

HMRC's website has information about tax, NICs, telephone helplines and Business Support Teams. Their Employer CD ROM contains forms and built-in calculators to help you work out PAYE, tax, NICs, benefits and Statutory Payments.

Table 6.6 National Insurance Contributions (NICs) 2008/09

Lower earnings limit (LEL), primary Class 1 per week	£90
Upper earnings limit(UEL), primary Class 1 per week	£770
Primary threshold per week (PT)	£105
Secondary threshold per week (ST)	£770
Employee's Primary Class 1 rate between PT and UEL	11%
Primary Class 1 rate above UEL	1%
Employee's contracted-out rebate	1.6%
Employer's contracted-out rebate salary related scheme (COSR)	3.7%
Contracted out rebate money-purchase scheme (COMP)	1.4%
Married women's reduced rate between PT and UEL	4.85%
Reduced rate above UEL	1%
Employer's secondary Class 1 rate above ST	12.8%
Contracted-out COSR	3.7%
Contracted-out rebate COMP	1.4%

NB:

1. The contracted-out rate only applies between the LEL and the UEL.
2. The employee's rebate is deductible from the employee's total contributions or in some circumstances from the employer's remittances to HMRC.
3. The employer's rebate is deductible from remittances to HMRC.
4. Employee contributions at 12.8% are also due on most benefits in kind and on tax paid on an employee's behalf under a PAYE settlement agreement.

Class 1A

12.8% payable in respect of benefits and expenses to directors and employees earning over £8,500. Payment is due by 19 July or 21 July if paid electronically. Payment gives no national insurance benefit rights.

Other classes

Class 2 Self-employed £2.30 per week flat rate

Class 3 Voluntary	£8.10 per week
Class 4 Self-employed	8% on profits between £5,435 and £40.040 pa and 1% thereafter. If profits are less than £4,825 you may be entitled to the Small Earnings Exception (SEE)

No NICs are due if state retirement age is reached by the previous 6 April.

NB: Employees earning less than the LEL are treated as having paid NICs when claiming benefit, so you must keep their details on Form P11 or equivalent and report to HMRC at the end of the year on Form P14. HMRC's website has information about tax, NICs, telephone Helplines, Business Support Teams and calculators for working out PAYE, tax, NICs, benefits and Statutory Payments.

Pensions

Sole traders and partners are entitled to the self-employed person's flat-rate State Pension at retirement age, which is not related to previous income. They are not entitled to the State Second Pension (S2P – formerly SERPS). If they take out a private personal pension or a stakeholder pension what they receive on retirement depends on what they pay in, how well it has been invested and their retirement age. Premiums on self-employed policies are not allowable against income.

Employees, including directors, with earnings above a certain level (£4,680 in 2008/09) cannot leave the basic State Pension scheme but they can 'contract out' of S2P by joining a private pension scheme. If the business does nothing, it has 'contracted in', 'not contracted out' NICs apply and employees receive the State Pension. If you contract out, you pay lower NICS and make your own pension arrangements.

Tax relief

Tax relief on pension contributions depends on whether you pay into a personal pension or pension scheme that covers all your employees.

With schemes covering all your employees the employer deducts contributions from the employee's pay before deducting tax and the employee pays tax on the balance. Higher rate taxpayers obtain full tax relief immediately.

With personal pensions the pension provider claims tax back from the government at the basic rate of 20 per cent, so every £80 paid into the pension puts £100 in the pension pot. High-rate taxpayers can claim the difference through Self Assessment or by letter to their Tax office.

You can now put as much as you like into any number of personal and/or company pensions and there is no upper limit on pension savings. You can claim tax relief of up to 100 per cent of earnings to a maximum annual allowance of £235,000 in 2008/09, rising to £255,000 in 2010; the lifetime limit is £1.6 million in 2006/07, rising to 1.8 million in 2010.

In the light of the April 2006 changes the maximum annual tax-efficient gross contribution to age 75 is:

- £3,600 or 100 per cent of earnings to £235,000 for an individual in 2008/09, rising to £255,000 in 2010;
- £235,000 less employee contributions for employers in 2008/09, rising to £255,000 in 2010.

Only current earnings count for the 100 per cent limit in 2008/09.

This is, however, a complicated area and you should seek expert advice.

Contracted-out pension schemes

Members of Contracted-Out Salary-Related schemes (COSRs), Contracted-Out Money Purchase schemes (COMPs), Contracted-Out Mixed Benefit schemes (COMBs) and contracted-out occupational pension schemes and their employers pay lower NICs. Employees contracted-out through an Appropriate Personal Pension (APP) pay full-rate NICs but the Department for Work and Pensions (DWP) pays the difference between the contracted-out and non contracted-out rates.

The COSRs pension is based on salary, length of service and annuity rates (the rate at which the pension fund is converted into a pension) on retirement. Employer and employee make contributions and the scheme must comply with certain legal standards.

COMPs provide a flat-rate refund of NICs (the minimum payment) paid in by the employer, plus an age-related top-up (the age-related rebate (ARR)), paid by the DWP. Employers and employees usually make extra contributions, for which they receive tax relief.

COMBs have separate benefit and money purchase sections, both of which contract out.

Employers and employees contributing to occupational pension schemes pay lower NICs. On retirement employees receive a second pension from the employer's scheme plus S2P if they have paid into it.

Some occupational pension and personal pensions schemes are organised on a 'rebate-only' basis, ie the only money paid in is the employee's NICs. On retirement employees receive about the same amount they would from S2P.

Stakeholder pension schemes are low-cost schemes for employees earning more than LEL (£90 per week) who pay reduced NICs. They receive an annual rebate of their contributions from HMRC which is paid directly into their personal pension. If they choose not to contract out they are entitled instead to SP2. Access must be arranged to this sort of scheme unless:

- you employ fewer than five people; or
- you offer all employees over 18 a personal pension scheme through which you contribute an amount equivalent to at least 3 per cent of their basic pay; or
- you offer an occupational pension scheme they can join within a year of starting work.

Arranging access does not mean you must set it up and run the scheme. Commercial financial services can do it, and register the scheme with HMRC and the Occupational Pensions Regulatory Authority. It is, however, up to the employees whether they wish to join the scheme.

Personal pension premiums paid on or after 6 April 2001 attract immediate basic rate tax relief at source. Premiums paid on 6 April 2008 can be carried back to 2002/03 to use up unused relief from earlier years.

Statutory references

These are kept to a minimum; further details are available from HMRC and the DWP and their websites.

Capital Allowances Acts 1968 and 1990
Companies Act 1985
Employee Share Schemes Act 2002
Finance Acts 1965, 1966, 1972, 1975, 1976, 1980, 1982, 1984 to 2007
Finance Act (No 2) 1997
Income and Corporation Taxes Acts 1970 and 1988
Income Tax Act 2007
Income and Corporation Taxes Acts 1970 and 1998
Income Tax (Earnings and Pensions) Act 2003
Income Tax (Trading and Other Income) Act 2005
Local Government Act 1988 as amended
Pensions Acts 1995 and 2007
Pensions Schemes Acts 1993 and 1995
Social Security Act 1998
Social Security Contributions and Benefits Act 1992 as amended
Taxation of Chargeable Gains Act 1992
Tax Credit Act 2002
Value Added Tax Act 1994

7

Insurance

Insurance is a gamble and you can cover almost any risk at a price. The only real difference between insurance and placing a bet is that insurance contracts are enforceable in English law.

The insurance contract

First you submit a proposal – application – to a broker or insurer giving details of the risk. The insurance contract is complete when your offer is unconditionally accepted, although the insurer can accept subject to payment of the premium. Non-marine policies can be agreed verbally if the items, the sum insured and the risks are specified. With other insurance you can, if those terms are agreed, be covered pending formal acceptance, but the insurer can withdraw after making enquiries.

Cover can be arranged informally on issue of a cover note. This is a temporary contract, distinct from the formal policy, unless the insurer combines them by sending the cover note on receipt of the premium as a 'deposit receipt'. Temporary cover notes renewing existing policies do not extend cover automatically and may be only an offer to insure, requiring acceptance. The note becomes a deposit receipt when the premium is paid. Some policies are self-extending, but if not, a new policy must be agreed, unless cover is renewed on the 'usual' or 'previous' terms.

The law of the contract

If you trade abroad, insurance may be governed by foreign law, unless the contract states it is to be governed by English law. Who receives the payment depends on the law of the place where the money is payable – whether money is owed is governed by the law of the contract but who receives it is governed by the law where it is to be paid out. Money is usually payable where insurers carry on business but life policies pay out in accordance with the law where the deceased was domiciled on death.

Terms and conditions

Legally, insurance contracts are contracts of *uberrimae fidei*. That is, they are made in 'the utmost good faith' and the parties must disclose everything affecting the risk. A mistake or inadequate disclosure may amount to misrepresentation and changes to the risk may invalidate the policy.

You can agree values initially under a 'valued policy'. Claims are based on that value but usually cover is limited to a specific amount, which is the maximum you can claim. Overvaluation can lead to cancellation and if no values are agreed you can usually claim the market value or the cost of repair or restoration to the limit of the sum insured, subject to averaging.

Most policies include an *average clause* that restricts claims to current market values, taking account of depreciation, which is usually less than replacement value. You can insure for replacement cost but premiums are higher.

If cover is only for loss of goods or damage to premises, there is no claim for loss of profits, loss of rent or loss of custom unless included in the policy.

Because you acquire new items to replace those depreciated in value by use, a discount on claims for goods lost or destroyed is usually included, but you can, if this is possible, require the insurer to pay for repairs instead.

Most policies set out terms and conditions, some describe legal effects and enlarge or restrict rights and obligations. On careful and expert reading you may discover you are entitled to damages if a claim is refused.

Cover

Claims are based on abnormal circumstances. Normal wear and tear and inherent vice – natural behaviour of the item insured – are usually excluded, even under 'all risks' cover (which means loss or damage caused in the circumstances set out in your policy). Most risks can be covered for a price, including terrorist attack, but riot, act of God, civil commotion and war are usually excluded. Accident policies cover accidents caused by carelessness, including the insured's, but deliberate damage is only covered if someone else is responsible.

Only risks occurring during the currency of the policy are covered. Transit risks are usually covered from the beginning to the end of the trip but you should check that loading and unloading, goods in storage, loaded overnight or unattended are covered and all methods of transport are included, in case there is an unforeseen change of route.

The time of loss is the time of the accident, whenever discovered, except in marine insurance, or if arising from an accident outside the period of cover. Causation can therefore be crucial.

Claims are based on one direct, operative cause – the 'proximate' cause – which cannot be an excepted risk or outside the risk period.

Goods in transit

If you use a 'common carrier', that is, public transport, the carrier insures your goods and is liable for their loss or damage, unless due to an act of God or the Queen's enemies or unless there is an agreement to the contrary. There is no contract between you and the carrier, and the amount you can claim is minimal. You can claim the full value if you declare the value on delivery, but the costs of carriage will then be raised accordingly.

Carriage by sea

Contracts for carriage by sea and contracts of affreightment are incorporated into in a bill of lading (see page 108) or a charter party, and you must insure the goods yourself.

If you deal directly with shippers and need to use all the space in a ship, the contract is usually contained in a bill of lading. This is a document signed by the ship owners, or on their behalf, stating that your goods have been shipped on a specified ship or have been received for payment; when signed by or on behalf of the carrier the bill of lading is handed to the skipper. The bill and the goods can be transferred by endorsement and delivery of the bill but it is not a negotiable instrument.

If you hire a ship directly from the ship owner to carry your goods, however, your contract is contained in 'charter party' which can be either:

- a voyage charter party – covering carriage in a specified ship from a named port to a named port for one or more voyages; or
- a time charter party – covering carriage for a specified period; or
- a charter party by demise – where you have complete control of the ship, its navigation and your own master and crew.

Marine insurance

Marine insurance covers 'maritime perils' incidental to 'marine adventures', ie ships and goods exposed to maritime perils and lost or damaged goods travelling by sea. You can extend the cover to inland waters.

Marine insurance contracts are made when the proposal is accepted by the insurer. Usually a document is issued – the 'slip' – which is a short memorandum of the contract when it is accepted by the underwriter. The broker acts as your agent and offers the slip to insurers, such as the underwriting syndicates at Lloyd's. Each agent of the syndicate writes a line, ie accepts a limited amount of risk – *pro tanto* – until the full amount on the slip is covered. The slip itself is an offer and the signature of the underwriters, through their agents, is their *pro tanto* acceptance. There is therefore a separate and binding contract between you and each underwriter even before the full amount on the slip is covered, although you cannot sue on the slip until the policy is issued.

You can take out:

- *voyage policies* – cover from port to port;
- *time policies* – cover for a specified period;
- *mixed policies* – cover for a specified voyage and period;

- *valued policies* – cover for a specified value;
- *unvalued policies* – where the value is calculated according to a formula and subject to the limit of the sum insured;
- *floating policies* – where details are defined by later declaration.

In marine policies, the value of claims is the value when the goods were insured, not their value at the time of loss and, unless expressly excluded, claims are subject to averaging.

Notice of loss

Notice must be given promptly and in accordance with the policy, with sufficient details to enable the insurer to ascertain the nature of the claim. Verbal notice may be accepted but it is advisable to have a written record.

You may have to prove loss, damage and the amount claimed and must usually report loss or theft to the police or appropriate authorities. Insurers often instruct assessors and loss of profits usually requires assessment by auditors.

Settlement

Claims are usually negotiated, and if substantial or complicated, you should instruct assessors. Entitlement under a cover note or after the renewal date depends on the circumstances and the type of insurance. Most insurers will agree to have liability – not the amount of the claim – decided in court even if there is an arbitration clause, unless you expressly agreed to the clause or it is a marine or aircraft policy.

Acceptance must be unconditional but payment can be recovered if the insurer can prove fraud or a mistake of fact.

Usually settlement is in cash and the insurer is entitled to claim lost or damaged goods as salvage.

Insuring business premises

Insuring the premises

A 1774 statute gives insurers the right to insist on rebuilding or reinstating business premises, and unless the policy sets a limit, they cannot limit the cost and work must be completed within a reasonable time. If damage is caused by fire, a landlord or tenant can force the insurer – but not a Lloyd's underwriter – to rebuild or reinstate unless an occupier is responsible. The insurers do not then have to replace trade or tenants' fixtures and can restrict the cost.

Leasehold premises

Landlord or tenant can insure leasehold premises. The tenant's insurable interest is only as tenant in possession, so he or she can only recover his or her own loss, unless liable for the value of the entire premises under a repairing covenant or the general law. Rent usually continues to be payable even if the tenant is not required to repair in the event of fire or the premises are destroyed.

The tenant therefore usually insures at the commencement of the lease if he or she covenants to repair. The tenant is in breach of covenant if renewal premiums are not paid and the landlord can claim damages or, if there is a right of re-entry for breach of covenant, forfeit the lease.

If the tenant is not bound to insure, the landlord must do so but the tenant is liable for increases in the premium due to changes on his or her own premises and cannot recover under the landlord's insurance, though he or she may be entitled to claim reinstatement under the 1774 Act. If the covenant benefits both landlord and tenant, the landlord must reinstate. You can extend fire cover to include 'special perils', including explosions, earthquakes and overflowing of water tanks, apparatus or pipes, on a replacement or reinstatement basis, as well as architects' and surveyors' fees, the building contents, stock, plant, machinery, fixtures and fittings, and the removal of debris. Fire insurance can also be restricted, but you are usually covered for your own damage by explosion on your premises but not necessarily for damage to other buildings unless caused by the fire itself.

Types of insurance

Burglary insurance

This covers theft involving forceful or violent entry and the insurer usually requires the premises to be properly protected.

Engineering insurance

Inspection by 'competent' engineers required by the Factories Act is offered by specialist insurers.

Money insurance

Insurance against loss of cash covers loss by any cause except theft by employees (insurable under a fidelity bond or policy – see below) and can include personal assault.

Insuring goods

Claims on goods, other than depreciation, depend on whether they are at your risk and rights may have to be ceded to the insurer. You can insure before you buy under a 'floating policy' covering 'all the goods in the warehouse or otherwise ascertainable' for a fixed amount, a 'declaration policy' for goods to be declared from time to time, or an 'open policy' insuring against all risks by sea and land. There are several commercial variants, including sellers' insurance inclusive CIF (cost, insurance, freight) for the buyer's benefit and FOB (free on board) insurance where the buyer pays premiums. You should check insurance and sales documents to ensure you are adequately covered.

Liability insurance

Liability insurance covers liability to employees and the general public as employer, owner and occupier of a building. Public liability insurance usually covers compensation for injury, disease or damage to the public and can be extended to cover accidents caused by defective goods but not injury to your own employees, damage to your property if you are in occupation and some kinds of liability under commercial contracts.

Because you are usually liable for injuries sustained by employees at work, you must be covered by appropriate insurance with authorised insurers,

unless you employ only family or independent contractors. The certificate of insurance must be displayed on the premises and details of injuries kept in an accident book.

Personal accident and/or sickness insurance

Schemes can be set up to provide employees with accident and sickness cover and health insurance.

Motor vehicle insurance

Legally you must carry 'road traffic cover', indemnifying you only against compensation for death or injury to third parties. 'Third-party cover' indemnifies you for damage to third-party property and can be extended to loss and damage to your own vehicle. Comprehensive cover also includes accidental damage to your vehicle.

You must inform the insurer if vehicles are used for business purposes. Even under road traffic cover you are usually insured personally to drive any vehicle, but you should check to make sure your policy is automatically transferred if you change your vehicle, it is stolen or destroyed, or if you make a claim.

Fidelity bonds and policies

Employees' theft, breach of confidence and fraud are covered by fidelity bonds and policies. They usually apply to particular employees in a stated capacity for a fixed period and loss arising from default within the period is covered, even if discovered after it. It is not usually necessary to give notice of suspicion.

Credit insurance

Debts are usually insured on the basis of an indemnity (but see pages 149–50 for business done abroad). Cover can be for default on the due date or in specified circumstances. Unless claiming an unpaid balance, you do not usually have to sue the debtor or enforce a security. Your rights are transferred to the insurers on payment but you may have to carry part of the loss. Debts and uncompleted contractual performance can also be covered by guarantees

and sureties. Under a guarantee you are guaranteed payment but a surety pays you on default and the principal debt remains unaffected.

If you provide payment protection insurance you may need permission to sell or administer regulated mortgage and general insurance contracts from the Financial Services Authority (FSA), 25 The North Colonnade, Canary Wharf, London E14 5HS (Tel: 020 7066. Details are available on their website, www.fsa.gov.uk.

Insurance against legal claims

Insurance is available to cover most civil claims brought against you in the courts, including legal costs.

Directors and auditors

Companies can indemnify officers and auditors for liability in some civil or criminal proceedings provided judgment is given in their favour, relief is granted by the court, or they are acquitted. If the Articles permit, additional insurance is obtainable to cover unindemnifiable risk.

Insuring key personnel

You can insure against loss caused by the death of senior management, for instance, to provide cash to buy out a deceased partner's share, or to engage someone to take over management.

Disputes

The Financial Ombudsman Service, on behalf of and under the rules of the Insurance Ombudsman Bureau, deals with insurance disputes. Details are available from the Financial Ombudsman Service, South Quay Plaza, 183 Marsh Wall, London E14 9SR (Tel: 0845 080 1800) and on their website, www.fiancial-ombudsman.org.uk, or e-mail, complaint.info@financial-ombudsman.org.uk.

Statutory references

Companies Act 1989
Defective Premises Act 1972
Employers' Liability (Compulsory Insurance) Act 1969
Employers' Liability (Defective Equipment) Act 1969
Factories Act 1961
Fire Prevention (Metropolis) Act 1774
Marine Insurance Act 1906
Occupiers' Liability Acts 1957 and 1983
Sale of Goods Act 1979

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Employers and employees

When you take on employees the law may take an active part in the business. You may have to comply with industrial practice and collective bargaining agreements. The network of legislation is studded with fines and penalties, and contravention can prove far more expensive than taking preventive measures.

Employers' obligations

The employment legislation covers all employees, including part-timers, except for:

- close family;
- non-executive directors;
- trainees under youth training schemes;
- employees working abroad;
- the self-employed.

Directors as 'office-holders' are excluded unless they are clearly employees – for instance, there is a service contract.

Self-employed workers are excluded from most of the employment protection and they also have their own responsibilities under health and

safety legislation. It is therefore important to know whether your workers are employed by you or by themselves. Key criteria include the job description, when and how payment is made, who pays tax and National Insurance, how far and to what extent the employee is integrated into your business and whether the 'employer' provides equipment, and who takes a profit or loss on the work.

Fixed-term employees are:

- doing 'seasonal' or 'casual' work with contracts ending on a specified date, or when a specified event does or does not happen or a specific task has been completed;
- on fixed-term contracts specifically covering maternity, parental, adoption or sick leave;
- hired to cover for peaks in demand where the contract expires when demand decreases.

They must not be treated less favourably than comparable permanent employees, unless this can be objectively justified. They are entitled to be told about vacancies and, unless it is objectively justified, to have access to occupational pension schemes.

They do not have the right to the same pay, conditions and benefits if their overall terms and conditions are as good, or better, than full-time employees – eg they receive higher pay in lieu of pension rights.

They may not be entitled to redundancy payments under the terms of their contract *but* failure to renew a fixed-term contract may amount to unfair dismissal if they are employed for at least a year and they may be entitled to redundancy payment if in continuous employment for at least two years, unless they waived their right to redundancy payments before 1 October 2002.

After four years on fixed-term contracts from 10 July 2002 they are considered to have a permanent contract; if offered a further fixed-term contract they are entitled to a written explanation. If this is unsatisfactory, the employer must confirm the contract as open-ended.

Apprentices, students on work experience placements of up to one year for part of a graduate, postgraduate or teacher training course and employees on government-supported training or retraining programmes are not fixed-term employees.

Agency workers

People taken on through employment agencies (which introduce them to the organisation as ‘hirers’, so that the employer’s contract is with the worker, not the agency) or employment businesses (which contract with workers, supplying their services to organisations as ‘users’) also have statutory protection.

Agency workers and temporary workers are covered by the National Minimum Wage and working time legislation (see below), as well as health and safety and social security provisions. They can leave jobs at short notice and, unless they have a contract, can be dismissed without notice and without any liability for unfair dismissal or redundancy pay.

They are to be given the same rights as full-time permanent workers after they have been working for you for 12 weeks. At the time of writing, however, their entitlement is to:

- paid holidays, although not necessarily the same as permanent employees, unless there is unlawful discrimination;
- rest breaks and limits on working time;
- have no unlawful deductions taken from their wages;
- the National Minimum Wage;
- not be discriminated against under the equality legislation;
- Maternity or Paternity Pay – but not Maternity or Paternity Leave;
- Statutory Sick Pay – after working with the same agency for more than three months.

If they have worked for an employer for many years and are treated as employees, they may be categorised as ‘employees’ with different rights and obligations.

Agency workers must be vetted by their agency, ‘temp to perm’ fees are restricted and the agency must state whether it acts as an agency or business and explain the difference.

In addition *employment agencies must*:

- not contract on behalf of workers or users without authority;
- give details of charges;
- give written details to workers of how they will find work;
- give workers written terms and conditions of their work.

And they must not:

- charge workers a fee;
- make workers use fee-paying services – eg obtain professionally written CVs;
- stop workers taking a permanent job with companies for which they have temped;
- stop workers registering with other agencies.

If employment agencies do not meet proper standards they can be fined and banned from operating for up to 10 years.

Employment businesses must:

- pay workers even if the user does not pay them;
- not pay or be connected with paying fees to anyone they introduce to a user.

Users must now pay temps themselves or accept supply through an arrangement that may cause problems for businesses that cannot fully recover VAT.

Home workers are entitled to the minimum hourly wage or 120 per cent of the wage for the hours an average worker would take to do the work.

If they use electronic equipment to contact their office base, however, they may be employees or self-employed.

Shift workers doing Sunday and/or night work can be paid:

- flat-rate allowances, per hour, shift or week, plus basic day rates;
- fixed percentage additions to day-work rates;
- basic day work-rates plus a higher rate;
- standard annual amounts paid to all employees on a specific shift;
- extra allowances for hours outside normal working hours.

If retirement is not reasonably justified, there may be a claim for unfair dismissal.

Shop workers with the same employer since or before:

- 25 August 1994 in England and Wales;
- 4 December 1997 in Northern Ireland;

and *betting workers* with the same employer since or before:

- 2 January 1995 in England and Wales;
- 26 February 2004 in Northern Ireland;

do not have to work on Sundays and can only agree to do so by giving written, signed and dated opt-in notice.

Workers in Scotland whose contracts require or may require them to work Sundays must work a three-month notice period if they opt out of Sunday work. Employees who are or may be required to work Sundays must receive a written statement explaining their rights within two months of starting work. If not and the employee gives opt-out notice, the three-month notice period is reduced to one month, ie the employee can stop Sunday work after one month instead of the usual three months. The right to opt-in and opt-out is continuous and can be exercised at any time.

Refusal to work on Sundays does not justify dismissal, redundancy or other detrimental treatment, eg refusing promotion. If rights are infringed by the employer there may be a claim for unfair dismissal or detrimental treatment. Procedures are set out on the Department for Business, Enterprise and Regulatory Reform's website, www.berr.gov.uk

Employee protection

Protection gives rights to guarantee redundancy payments, minimum periods of notice, compensation for unfair dismissal and other rights listed below. Once agreed, all employees (including part-timers) are entitled to the same sick leave, pensions, holidays, staff discount and share option benefits, including regular part-timers and casual part-time employees working on a day-to-day basis for over three months.

Within two months of starting work, employees must have a *written statement* giving details of employer and employee, a job description, the place of work, the date of starting work and what other work, if any, forms part of the 'continuous period of employment' (increasing the qualifying period for protection under the legislation). Working hours must be set out, the amount and time of payment, disciplinary procedures (but not grievance procedures if there are fewer than 20 employees), details of relevant collective agreements, pension rights, holiday and sick pay, length of notice and details of any contracting-out certificate (relating State pensions to earnings); length

of employment must be included for temporary employees. Details of pension schemes, sick pay, disciplinary rules and procedures, and notice can instead be in another reasonably accessible document. Employees must receive written notification of changes within a month of the change.

Pay statements must give details of gross and net pay, with details of the amounts and reasons for deductions.

After four weeks' work you and your employees are entitled to a week's notice. After two years employees are entitled to a week's notice for each year of continuous work to a maximum of 12 weeks but they can take payment in lieu.

Hours of work

All employees, including part-time, casual, freelance and agency staff, *but not* managing and executive staff and family members, are entitled to:

- Work no more than 6 days out of 7, or more than 12 out of 14.
- A minimum daily rest period of 11 consecutive hours in 24.
- A rest of 30 minutes every six hours, if working longer than six hours.
- A minimum rest period in seven days of 24 consecutive hours, that is, a full day, plus 11 hours of daily rest. Days off can be averaged over two weeks to give two days off a fortnight.
- A maximum average of 48 hours' work in seven days including overtime.
- A maximum of 48 hours' average working time in seven days.

Employees making their own decisions because of the nature of the job, eg senior managers, can opt out of the working time regulations and the full rest period entitlement does not apply if you agree different working hours.

Employees paid by the hour, paid overtime, working under close supervision or required to work longer hours, eg because of output requirements, cannot opt out but they must not be forced to work more than an average of 48 hours a week.

Young employees – you cannot employ a child under 13, unless he or she comes within the exceptions, eg acting, but working hours are strictly controlled and you usually require a local authority licence.

In England, Wales and Scotland young people between 13 and the minimum school-leaving age of 16 may not do paid or unpaid work:

- before 7 am or after 7 pm;
- for more than two hours on a school day or Sunday;
- for more than 12 hours a week during term time;
- for more than 25 hours a week in school holidays *or* 35 hours if aged 15 or over.

In Northern Ireland, young people under 15 may not do paid or unpaid work:

- for more than two hours on Sunday;
- for more than five hours on school days or Saturdays;
- for more than 27 hours in any week.

School-age children's work is governed by strict rules even if they only do a paper round. They must not be employed in manufacturing or dangerous activities and you may have to provide evidence the job is not dangerous.

Existing risk assessments must be checked, including health and safety arrangements, taking into account the teenager's immaturity and inexperience. The local authority must be notified and you may need a local authority or local education authority permit.

Employees aged 16 and 17 must:

- work for a maximum of 8 hours a day or 40 hours a week;
- have a break of 30 minutes every four-and-a-half hours;
- have a rest period of 12 hours between each working day;
- have two days off a week.

They can be employed in certain dangerous environments if necessary for training, so long as they are supervised and risks are minimised.

They may be entitled to paid time off for study or training. Employees aged 18 to 24 claiming Jobseeker's Allowance for at least six months may be entitled to two days off a week to study, plus at least one extra day, or its equivalent, for up to six months. Information about financial assistance for employers is available on the Department for Education and Skills (DfES) website, www.dfes.gov.uk. Refusing time off for training is a ground for a complaint to the employment tribunal.

Apprentices. Staff aged 16 to 24 may be eligible for apprenticeship and there are proposals to extend the age limit beyond 24. Details of schemes and financial assistance towards the cost of training are available on the Learning and Skills Council website, www.lsc.gov.uk

Night workers who work at least three hours between 11 pm and 6 am should only work an average of eight hours, calculated over 17 weeks. They cannot choose to exceed this unless allowed by a collective workforce agreement. They may be able to average night work over a period of 26 weeks *but not* if they deal with special hazards or are under mental and physical strain.

Night workers and employees are entitled to compensatory rest – ie they can accumulate rest periods and defer them to a later date; their average hours are calculated over 26 instead of 17 weeks – if they:

- work a long way from where they live;
- have to travel to different places for work;
- do security or surveillance work;
- have jobs that require round-the-clock staffing;
- work during exceptionally busy periods and emergencies.

'Mobile' employees, working in road, or inland waterways transport, must not work more than:

- an average of 48 hours per week;
- 60 hours in any single week;
- 10 hours in any 24-hour period, if working at night.

They cannot opt out of the average weekly working limit but can extend the reference period from 17 to 26 weeks and the amount of night work by collective or workforce agreement.

You must offer and keep records of free regular health assessments and retain them for two years. You may also need to assess your health and safety implications for night working, eg your fire-evacuation procedures and security arrangements.

Records should be kept to show compliance with working time and night work limits, with details of employees who agree to work more than 48 hours a week. If they seem to be nearing the time limits, they should be monitored to ensure compliance with the regulations.

Flexible working hours

Parents, adoptive parents, carers and guardians of children under 6 and disabled children under 18 who have worked for you for at least 26 weeks can apply to you once a year to be permitted to work 'flexible' hours. A refusal must be based on genuine business grounds. You must meet the employee for discussion within 28 days of the application. The employee can bring a companion to the meeting, and 14 days thereafter you must give written notification of agreement and the starting date of the new arrangement, which permanently changes the terms and conditions of employment.

Employees who are caring for dependants are entitled to flexible leave and time off for emergencies.

The employee has 14 days to appeal your refusal to ACAS, the employment tribunal or other form of dispute resolution. Refusal must be supported by written reasons. If you lose the appeal, you may be ordered to reconsider, and if the procedure has not been followed you may have to pay compensation of up to two weeks' pay.

Holidays

All workers, other than managing and executive staff and family members, but including those on short-term contracts, are now entitled to a minimum of 4.8 weeks' annual paid holiday – ie 24 days a year for employees working a standard five-day week. This can but does not include statutory and bank holidays. The entitlement increases to 5.6 weeks from 1 April 2009. Holiday entitlement for part-time staff is currently 4.8 times their usual working week.

Employees should be notified of the increase and told they are entitled to payment in lieu of holidays if the employment ends before they take a break.

Contracts of employment and senior employees' service agreements

The statement is not a contract but is evidence of some terms in a full service contract. This can be oral or written and should include everything in the

statement plus a requirement to follow the safety at work scheme, if any, and works' rules put together after consultation with staff or their representatives. (If rules are included, they must be changed by agreement; if not, they can be changed any time.) Changes are accepted if there is no objection within a reasonable time unless the contract permits variation or it can be implied from conduct or a collective agreement. Objection by resignation may be constructive dismissal and also unfair dismissal.

Wages

If payment is not agreed, reasonable remuneration can be claimed for work done.

All employees and workers, including part-time employees working away from their employer's premises, casual and agency workers, homeworkers, pieceworkers, and employees working under short-term contracts must be paid not less than the National Minimum Wage, currently £3.40 per hour for employees aged 16 and 17, and £4.60 (the 'development' rate) for employees aged 18 to 21 and employees during their first six months in a new job with a new employer who receive accredited training. The Minimum Wage for employees aged 22 and over is currently £5.52. In October 2008 the minimum hourly rates increase to £3.53, £4.77 and £5.73.

Apprentices under the age of 19 are not entitled to the National Minimum Wage. Over the age of 19 they are not entitled to the Minimum Wage until they have completed the first 12 months of their apprenticeship. If they are funded by the Learning and Skills Council (LSC) in England they receive a minimum income of £80 per week.

If any employees are paid less than the Minimum Wage, an Enforcement Officer can serve an enforcement notice requiring an employer to pay them the Minimum Wage for a current and future pay period plus arrears, and if the notice is not complied with the officer or employee can take proceedings in an industrial tribunal to recover underpayments.

Here, 'workers' are employees working under a contract of employment or agreement whereby they undertake to do or perform personally work or services. Clients, customers, the self-employed and members of your family are not workers.

Your records must show payments as an hourly rate, they must be sufficient to show compliance with legislation and must be produced on request to the

employee, the enforcement agency, tribunals and courts. HMRC deals with complaints and can enter premises, inspect records and issue enforcement notices. 'Penalty notices' may be served if the notice is not complied with – the employer will be fined and the employee may be awarded additional pay.

Deductions from the wages of 'workers' – here anyone working as an employee or self-employed, including apprentices but not those working directly for customers or clients – are unlawful unless:

- required or permitted by the law or the contract;
- the worker has given prior written consent.

And you can lawfully deduct:

- reimbursement for overpaid wages and expenses;
- payments made under statutory disciplinary proceedings;
- statutory payments due to a public authority;
- amounts due to third parties under contract – eg trade union dues – and to satisfy court orders;
- wages during a strike.

You can also make deductions for cash shortages and stock deficiencies from retail employees' wages to a total of 10 per cent of the gross wage.

Sick pay

You can agree whatever you like about sick pay, but if you have no sick pay arrangements, employees off sick for at least four consecutive days – including weekends, holidays and days off – can claim Statutory Sick Pay (SSP). SSP is only payable for qualifying days, ie days on which employees are required to work. Nothing is payable for the first three ('waiting') days. Qualifying days during the previous eight weeks when an employee is off sick for at least four consecutive days count towards waiting days and absences of at least four consecutive days link with other absences during an eight-week period. Sickness can be self-certificated on form SC2 but after seven days medical certificates should be provided.

SSP1 must be sent to employees off sick for four or more days who are *not* entitled, or cease to be entitled, to SSP so they can claim Incapacity Benefit.

The daily rate of pay is based on the weekly rate divided by the number of qualifying days in the week for which you pay SSP. Weeks begin on Sunday and each week commencing Sunday that the employee is sick is a separate pay period. SSP is treated like pay, so you must deduct PAYE, tax and NICs. You can also deduct the lawful deductions set out above. When the employee is paid daily or weekly, SSP will be below the NIC lower-earnings limit, but if you make any other payments in the same period – eg wages or occupational sick pay – tax and NICs must be deducted. SSP is included as part of the total year's pay for directors and employees with annual earnings periods.

Records must be kept on HMRC forms, your own computerised forms or magnetic tape and retained for at least three years. Forms and SSP2 records sheets are obtainable free of charge from HMRC, but you can use computerised forms if they include the necessary information.

If employees have more than one job, earnings from each job count separately for NICs and you can share SSP payments with the other employer. If the employee's other job is working for him- or herself, you are liable for the full amount of SSP.

If at least seven days' SSP is due to an employee who leaves the job, you must give a leaver's statement on SSP 1(L), but this is only needed by a new employer if the employee is sick for at least four consecutive days during the first eight weeks.

SSP is currently payable at the rate of £75.40 a week for a maximum of 28 weeks except to employees under 16 and over 65, employees on fixed-term contracts of three months or less and those paid less than £90 per week over a six week period before deduction of income tax and NICs. Agency workers can claim SSP from their agency if working under a contract of at least three months. Employees receiving statutory maternity, paternity or adoption pay cannot also claim SSP.

SSP ceases to be payable after 28 weeks or the employee becomes entitled to Maternity, Paternity or Adoption Pay or Allowance. You can recover payments under the Percentage Threshold Scheme (PTS) if total SSP payments exceed Class 1 NICs for the tax month less contracted-out rebate, if any, multiplied by 13 per cent of your NIC liability for the tax month. Records of total gross Class 1 NICs and SSP payments in each month should be entered in your HMRC payslip booklet P30BC, form P32 or your pay records. You can

deduct the amount you are entitled to recover from your contributions to HMRC. If you are entitled to recover more than the contributions due, you can deduct the excess from PAYE income tax due that month, entering the excess in the National Insurance box of the payslip, preceded by the letter 'M' (for minus), but *do not* alter the amount entered for PAYE tax.

Even if you have opted out, you can still recover payments up to the amount of SSP due under the PTS and deduct it from payments to the HMRC Accounts Office, but details must be recorded on forms P14 and P35. Write directly to the HMRC Accounts Office at the address on your P30(BC) if you need to recover the payments as a matter of urgency.

Details of the SSP scheme, explanatory booklets and forms are obtainable from HMRC.

You can opt out of the SSP scheme for all or part of your workforce if your occupational sick pay (OSP) scheme offers equivalent or better benefits whether or not your scheme is formalised. You can pay on an informal or discretionary basis, or you can pay the normal wage. You can also choose to pay OSP for a limited period and then opt an employee back into SSP.

You do not have to inform HMRC if you opt out and you can still claim the amount you could have recovered under the Percentage Threshold Scheme, provided you keep proper records.

This means that you do not have to keep two sets of records (for OSP and SSP), although in practice you must still keep most of your SSP records.

You can demand full *medical reports*, but employees must be informed that they have a right to approve or amend the report or, having seen it, to refuse to supply it, unless it refers to a third party. The doctor is entitled to refuse to make amendments or to permit disclosure on the ground that it would prejudice the employee's health.

If you suspect malingering, HMRC will assist, provided the employee has been off sick for four or more short periods in 12 months. A letter to the local HMRC (NICs) office with a report from the employee's doctor may persuade it to ask for a medical examination. HMRC will send the result of the examination to you, stating whether there are reasonable grounds for the absences or whether the employee is incapable of work. If the employee is capable of work, you must decide whether or not to continue paying SSP. The same applies if the employee refused to disclose a doctor's report. If you stop the payments at this stage, the employee is entitled to hear your reasons for doing so. If requested, you must give a written explanation and the employee can seek HMRC's formal decision as to entitlement to SSP.

Trade unions

Employees can belong to any union even if it is not the union with sole representational rights. Payment of subscriptions must be authorised by members at least once every three years and employees can participate in TU activities as agreed with you or as provided in the union membership agreement.

The 2004 Employment Relations Act has made it easier for trade unions to achieve recognition and meet statutory balloting and notification requirements. Some provisions are intended to prevent employers from offering inducements or subjecting employees to a detriment in order to avoid collective bargaining.

The rules for industrial action ballots and ballot notices have been eased and employees taking official and lawfully organised industrial action now have increased protection. Unions are entitled to expel members whose political behaviour is incompatible with union membership, eg members engaged in racist activities.

Union members must not be penalised for using the union's services. They are entitled to a companion at grievance and disciplinary hearings and to be informed and consulted on management decisions affecting their future.

You are entitled to at least seven days' written notice of official industrial action, to assist you in making plans and bringing information to the attention of employees. The union does not have to name the employees involved. After notice has been given and before action is taken, there must be a postal ballot of members. It is no longer unlawful if an individual who was denied a vote is called on to join the strike.

The union does not have to give further notice if continuous industrial action is suspended and then resumed.

Unions are not responsible for members' unofficial activities but they are liable for interference leading to breach of commercial contracts unless industrial action is in contemplation or furtherance of a trade dispute. They cannot bring in outsiders and picketing is only permitted at or near the employees' place of work. You may be able to bring proceedings if industrial action is unlawful.

Works Councils provide a formal framework for consultation between employers and workers' representatives. Legislation introducing Works Councils into our law, however, only applies to organisations with at least 1,000 employees across the EU or at least 150 in each of two or more member states.

Anti-discrimination legislation

You must not discriminate against full- or part-time employees because of colour, race, ethnic or national origin, sex, sexual orientation or marital status, age, their disability, or their religious or other beliefs.

But you can insist on employing men or women for specific jobs if their sex is a genuine occupational qualification, it is justified by the nature or circumstances of the job, or the employee is required to work or live in a private home.

It is now unlawful to harass, victimise or discriminate directly or indirectly against employees, job seekers or trainees because of their age. The 2006 Regulations have therefore:

- removed the upper age limits on claims for unfair dismissal and redundancy;
- introduced a national default retirement age of 65, making compulsory retirement age below 65 unlawful unless objectively justified; and
- given all employees the right to as to continue working beyond 65 or the retirement age set by their employer.

Sexual harassment at work – offensive, unwelcome and unreasonable conduct which is humiliating, hostile or intimidating – is now an offence. It includes:

- suggestive remarks or gestures;
- requests for sexual favours;
- insensitive jokes;
- innuendoes;
- lewd comments;
- forwarding inappropriate e-mails;
- accessing pornographic websites;
- unwelcome advances;
- threats of, or actual, sexual violence;
- fondling or touching;
- pestering for attention; or
- displays of unacceptable material, including pin-up calendars or graffiti.

Usually there will have to be three incidents to justify a complaint to the Employment Tribunal, although one sufficiently serious incident may be sufficient; aggravated damages can be claimed if the behaviour is particularly offensive. No minimum period of employment is necessary and there is no limit on compensation.

It is thought that the legislation will mainly affect employers of catering, hotel and retail staff and some professionals and teachers whose employers take no action when they are sexually harassed.

Women and men are entitled to be paid the same if doing the same or equivalent work, although economic factors affecting the business may justify paying different wages when they are not employed contemporaneously. They must also be treated in the same way in relation to employee-related benefit and occupational pension schemes.

Statutory Maternity Pay (SMP) and maternity leave and maternity allowance

If you do not have your own arrangements pregnant employees with 26 weeks' continuous employment by the fifteenth week before the baby is due can claim up to 39 weeks' Statutory Maternity Pay (SMP) from their employer, even if they do not intend to return to work, provided their average weekly gross earnings are not less than £90. If they stop, or continue to, work after the eleventh week, they can choose any day to start SMP but it cannot start earlier than eleven weeks before the baby is due. The latest it can start is the day after the birth, but it usually coincides with Maternity Leave. If average gross weekly pay is less than £90 they may be able to claim Maternity Allowance – see below.

SMP is paid at the rate of 90 per cent of average weekly earnings for the first six weeks and £117.18 or, if less, 90 per cent of average weekly earnings for the remaining 33 weeks. Payment for 52 weeks is under discussion but currently pay during additional maternity leave from the end of the statutory period to the end of the twenty-eighth week after the birth is subject to agreement, although return to work can be postponed for another four weeks because of illness or another proper reason.

Pregnant employees are also entitled to up to 26 weeks' Ordinary Maternity Leave (OML) however long they have been in employment and whatever their hours of work or how much they are paid. If they have 26 weeks'

continuous employment by the beginning of the fourteenth week before the beginning of the week that the baby is due. they can in addition claim an extra 26 weeks of Additional Maternity Leave (ADL) on the same terms and conditions that apply to ordinary leave, except for pay. If they cannot return to work because of redundancy, they must be offered suitable alternative employment.

Registered self-employed employees paying Class 1 NICs or holding a Small Earnings Exception certificate (see page 78) can claim Maternity Allowance (MA) for 39 weeks. They must have worked for you for at least 26 weeks of the 'test period' (ie 66 weeks up to and including the week before the baby is due) and earn an average of £30 in any 13 weeks in the test period. MA pays a standard weekly rate of £117.18 or 90 per cent of average weekly earnings before tax, whichever is the smaller; it is not subject to tax or NICs and is not paid during periods of work.

Employees must notify and confirm the pregnancy, and you can claim reimbursement of 92 per cent of SMP from the total amount of employees' and employers' NICs due to the HMRC Accounts Office.

Small Employers' Relief (SER) of 100 per cent of SMP, SPP and SAP plus 4.5 per cent of the amount as compensation is available if you pay or are liable to pay total employers' and employees' gross Class 1 NICs that do not exceed £45,000. If you pay contracted-out NICs, you should deduct the contracted-out rebate from your employer's NICs when calculating whether or not you qualify. SER not apply to Class 1A NICs on company cars and Class B NICs PAYE Settlement Agreements.

Records must be kept on HMRC forms, magnetic tape or in computerised form and retained for at least three years. Other forms can be obtained from your Social Security office, but problems are referred to HMRC. Payments must be noted on employees' Deduction Working Sheets (P11) and End of Year Returns (P14) and on your annual statement, declaration and certificate (P35).

Statutory paternity pay (SPP) and paternity leave

Female and male employees who have worked for 26 continuous weeks by the fifteenth week before a baby is due and who are not taking adoption leave (see below) can claim up to two consecutive weeks' paternity leave.

'Father' includes the biological father and the mother's husband or partner living in an enduring family relationship, as well as the adoptive parents, father and civil partner.

Employees must notify you of the intention to take this leave in the fifteenth week before the baby is due. You must provide a self-certificate for them to complete with details, and you must respond within 28 days. Leave must be taken within 56 days of the birth or placement for adoption, or from a fixed period or date after the baby is expected.

Statutory paternity pay (SPP) is claimed at the same rate and on the same basis as SMP, but is not payable if the employee receives SSP.

Statutory adoption pay (SAP) and adoption leave

Adoptive parents employed continuously for 26 weeks up to and including the week they are matched with a child can take 26 weeks' ordinary adoption leave plus 26 weeks' additional adoption leave. Leave starts from the date the child is placed or from a fixed date up to 14 days before placement. Adopters must tell you they intend to take the leave, and give details of the placement date and start of leave within seven days of being notified they have been matched for adoption. You must respond within 28 days with the date they are due to return to work. The adopters can change the start of leave on 28 days' written notice.

Either parent, partner or civil partner can claim but leave cannot be spilt between them. Male and female adopters can opt instead to take maternity or paternity leave.

Statutory adoption pay (SAP) is claimed at the same rate and on the same basis as SMP, but is not payable if the employee receives SSP.

Disabled employees

You must not discriminate against disabled persons, including people with HIV, cancer, multiple sclerosis and visual or other impairment. As with other anti-discrimination legislation, it is unlawful to refuse to offer disabled employees work or to treat them less favourably than other employees. They are entitled to additional training and time off for treatment during

working hours. If practicable, you may have to provide special or modified equipment.

If you have more than 20 employees, 3 per cent of the workforce must be registered disabled unless the work is dangerous.

Employees with criminal records

Apart from caring services and some professions, employees need not disclose some fines, court orders and custodial sentences of over six months 'spent' after periods of up to 10 years. Life imprisonment and preventive detention cannot be 'spent'. Dismissal for failure to disclose unspent convictions is fair.

Exposure to health risks

After working for four weeks employees can claim up to 26 weeks' pay if exposed to some health risks, unless they are unable to work or unreasonably refuse alternative work.

Guarantee and redundancy payments

Unless they are seasonal or casual workers, apprentices, over retirement age or have given written notice under a contract of at least two years, there is a trade dispute or they unreasonably refuse alternative work, employees with you for four weeks can claim guarantee payments after 12 weeks without work for every day without work. The maximum claim is £20.40 per day for a maximum of five days in a three-month period unless there is a collective agreement.

Redundancy payments can be claimed when lay-off or short-time work lasts for more than four weeks or more than 6 in 13 and employees have received less than half a week's pay. You can agree to pay or, by counter-notice in response to a request, state that you reasonably expect to be able to provide at least 13 weeks' continuous work and if there is then no work the employee is entitled to payments. Employees redundant after two years' continuous work

can claim even if they volunteer for redundancy or immediately find other employment. Claims must be made within six months and are as follows:

- half a week's pay for employees between 18 and 22 up to the age of 21;
- a week's pay for employees over 22 up to the age of 40;
- One-and-a-half week's pay for employees aged 42 and over;

for each year of employment.

Employees can also claim redundancy payments if:

- you cease, or intend to cease, carrying on business; or
- the work for which you took on the employee has ceased or diminished or is expected to cease or diminish; or
- the specific work for which the employee was engaged in the existing workplace has ceased or diminished or is expected to do so.

Pay includes overtime plus payment for one week's notice for every complete year worked to a maximum of 12 weeks. The maximum entitlement is for 20 years at £310 per week for 20 weeks. There is no liability to tax or NICs for payments up to £30,000. An employee given notice of redundancy by agreement still qualifies for payment but the notice period must have started by the date on which the employee leaves. Payment must be made when dismissal occurs or soon after.

If independent trade union members are affected, you must consult their representatives before dismissal, giving reasons and stating how many and which employees are to be made redundant. You must do all you can to comply with the requirements if there is insufficient time for full consultation.

Directors or shareholders can authorise additional payments for employees when a company is taken over or wound up.

Employees' obligations

The law assumes that employer and employees enjoy each other's trust and confidence. Employees must follow lawful and reasonable orders and take proper care of your property and must not disclose your industrial and trade secrets unless required to do so by the law.

These belong to the employer if made in the course of employment. Employees should sign agreements to protect you against disclosure of confidential information and from competition but the courts will not enforce one which effectively stops them making a living and you cannot stop disclosure to HMRC or FIMBRA. If you repudiate the agreement, you cannot enforce the restrictions put on the employee.

References

You do not have to supply references. An employee can sue on a bad reference, but there is no claim if it is true and made without malice (see also page 171, 'Data protection'). If the reference is too favourable, you may be liable to a new employer if the employee is unsatisfactory.

Inducing breach of the contract of employment

Persuading someone to leave a job is actionable by the ex-employer as an inducement to breach of contract.

Disciplinary powers of management

Some disciplinary powers are specified under the employment and earlier legislation. Procedures should be fair and worked out with the employees and their representatives. Employees should know who can take action and in what circumstances. They must have an opportunity to defend themselves and a right to appeal to a senior level of management or independent arbitration. Fines can only be imposed for breaches of discipline likely to cause loss and must be fair and reasonable. Deductions from pay can be made in connection with disciplinary proceedings under statute. Procedures should be set out in a rule book and employees should acknowledge agreement by signature. Details should also be included in contracts of employment or notices and, unless based on trade practice, in collective agreements.

Statutory grievance and disciplinary procedures must be written into all employment contracts; breach constitutes breach of contract and unfair

dismissal. The procedure can be found on the ACAS website, www.acas.org.uk.

Codes of practice

Some disciplinary powers and procedures are set out in codes of practice issued under the employment legislation. These codes under the health and safety legislation, the anti-discrimination legislation and TUC codes that cover trade disputes and payments to political funds can be obtained from the ACAS website on www.acas.org.uk/publications/pdf/cop.pdf and the Office of Public Sector Information on www.opsi.gov.uk. The codes do not have the force of law but are taken into consideration in the event of disputes.

Retirement

The national 'default retirement age' is now 65. Unless you have a legitimate business reason compulsory retirement before that age is unlawful. You can, however, agree on another age for retirement, provided it apples to *all* employees.

Employees are entitled to request to continue working after the statutory or agreed retirement age and if you do not follow the statutory procedure and are unable to show a fair reason for dismissal you may face a claim of age discrimination *and* unfair dismissal.

Fair procedure comprises giving employees:

- written notice and details of the right to ask to continue working six to 12 months before the intended retirement date;
- the opportunity to meet to discuss the request to continue working;
- written details of your decision and information of the right to appeal within 14 days of the meeting; and
- confirmation of the retirement date if the request to continue working is rejected.

Employees have 14 days to appeal. The appeal meeting must be called within 14 days of notice of appeal and they must be notified of the decision reached 14 days thereafter.

Provided you give six months' notice the employee's written request must be given at least six weeks before the retirement date. If you do not give six months' notice, they can ask to continue working at any time before the retirement date, thereby automatically extending their employment until you notify them of your decision.

There is a sliding scale of penalties for not following the procedure. If you miss or fail to comply with the six months' time limit employees can claim up to up to eight weeks' pay. But if you comply with the procedure there is a presumption of fair dismissal.

Dismissal

The unfair dismissal provisions apply to full-time and part-time employees who have worked for you for a year, except those working or residing abroad.

There is no one-year qualifying period and dismissal and redundancy is unfair for the following 'inadmissible' reasons:

- sex, race or other discrimination;
- using or attempting to exercise a statutory right, eg taking maternity leave;
- unjustified dismissal of an employee over retirement age;
- non-compliance with Sunday employment legislation;
- taking appropriate action on health or safety grounds – selection for redundancy on this ground is also unfair dismissal;
- TU membership, non-membership or TU activities.

You can fairly dismiss employees on strike on written notice stating that if they do not return to work within a specified time they will be dismissed and the dismissal is during the strike.

If disciplinary grievance procedures do not comply with statutory guidelines employees can claim unfair dismissal and the award can be increased by up to 50 per cent.

Employees employed for less than a year, or who suffer a detriment, eg demotion, whatever their age, or are dismissed or made redundant after jury service or after being summoned for jury service may also have a claim for unfair dismissal. *And* dismissal of employees employed for less than a year

whatever their age on a refusal of a flexible working hours application or other working parents' rights without following the statutory procedure is automatically unfair.

Retail shop employees must be given a written statement setting out their rights in connection with Sunday work within two months of engagement. They cannot be dismissed or penalised for refusing to work on Sundays if this was agreed at the outset or before 26 August 1994. Even if Sunday work is agreed, the employee can give later written notice of objection which is usually effective after three months.

Fair dismissal is based on one of the following:

- the employee's capabilities or qualifications (*if* required by the contract);
- misconduct – eg persistent drunkenness or dishonesty;
- redundancy – 'Last in first out' (LIFO) is usually safest and fairest;
- the employee cannot continue work without breaking the law – eg a driver loses his driving licence;
- some other substantial reason – eg going into business in competition with you;
- on transfer of the business: for economic, technical or organisational reasons (see page 207).

Putting an employee in an untenable position, thereby compelling him or her to resign – eg moving a senior executive into a very small office although paying the same salary – may be unfair and also wrongful dismissal.

You must act fairly and reasonably and the employee must have a chance to defend him- or herself. Instant dismissal is rarely justified and warnings, if possible written, should be given, with details of the complaint and stating that dismissal will follow if there is no improvement. Usually you must give a second written warning before you can consider suspension or dismissal. Reasons for dismissal must be sent to the employee within 14 days of dismissal.

If unfair, an industrial tribunal will, if practicable, order reinstatement in the same job or re-engagement in a similar job. If not practicable, employees can be awarded compensation of a basic award of half a week to one-and-a-half weeks' pay at a maximum of £330 per week for each year of employment, depending on age and length of service, for a maximum of 30 weeks, with a maximum of £9,900.

The minimum basic award for dismissal on trade union, health and safety, occupational pension scheme trustee, employee representative and working time grounds is £4,200. For employees excluded or expelled from a trade union and not admitted or re-admitted by the date of a tribunal application this is increased to £6,600.

The sum of £2,900 is awarded for unlawful inducement relating to trade union membership, activities or services and for unlawful inducement relating to collective bargaining.

The maximum compensatory award considered 'just and equitable' in the circumstances is £63,000, but there is no limit if the employee was unfairly dismissed or made redundant because of health and safety concerns or public interest disclosure ('whistleblowing').

If the tribunal's order for reinstatement or re-engagement is ignored or if dismissal is for sex, or racial or other discrimination, an additional award of between 26 and 52 weeks' pay at a maximum of £330 per week to a maximum of £17,160 may be ordered.

Part of the compensatory award in unfair dismissal cases compensates an employee for loss of earnings to the date of the tribunal hearing. The employee may, however, have already received unemployment benefit or income support for this period. The tribunal will therefore order the employer to pay a specified amount of the employee's award to the Jobcentre Plus to avoid 'double payment' to the employee.

The employee must mitigate his or her loss and seek alternative employment and the amount may be reduced if the employee unreasonably refuses reinstatement, has found other work, or conduct was a contributory factor.

If the employee loses, he or she does not have to pay your legal costs unless the tribunal decide the allegations were serious or unfounded, but you may be able to obtain payment of all or some of your costs if the dismissal was because of TU pressure.

The tribunal can also award damages for breach of the employment contract of up to £25,000.

E-mail and your employees

If your employees have agreed that you can monitor their e-mails, you can legally dismiss them for sending and receiving e-mails that do not relate to their work. You need their specific agreement, preferably under a clause in the statement or contract of employment that gives you the right to monitor

all messages created, sent, received and stored on your systems, or a clause stating they are not the employees' private property and there should be no expectation of privacy.

Your right to monitor employees' e-mails may conflict with the Data Protection Act 1998, and possibly also with the implied contractual relationship of mutual confidence and trust between employer and employee, and employees' right to privacy under the Human Rights Act 1998. Your best course therefore is to agree sensible guidelines on good business practice and guidelines to safeguard employees' privacy and your business interests, to include an appropriate consent clause in individual statements and contracts of employment, and to follow the Employment Practices Data Protection Code.

The code sets out helpful guidelines about complying with data protection provisions, and covers all 'electronic communications', that is, e-mails, faxes, telephone calls, internet access and CCTV and audio surveillance, but not records kept in response to specific queries, such as customer complaints. It assumes monitoring is intrusive and advises that advantage should be weighed against its impact on employees. Anyone with access to personal data should be aware of the data protection requirements and should be identified to employees, and third parties who contact employees should be told about monitoring.

Only the address and header information of e-mails should be checked unless it is essential to monitor content. Covert monitoring is only justified in exceptional circumstances, such as if fraud is suspected.

Employees should:

- be told when they will be monitored, the justification, how the information will be used and to whom it will be disclosed;
- have written details if the information is to be used in disciplinary procedures;
- be able to comment on the information before action is taken;
- know how long the information is kept.

Wrongful dismissal

If you break a term of the individual contract of employment the employee can claim damages for wrongful dismissal in the civil courts under the general

law which may amount to far more than compensation for unfair dismissal. Damages here are based on what the employee loses and expects to lose by instant unemployment and he or she must seek comparable alternative employment to minimise loss. If the employee instead chooses to take a claim to the employment tribunal, the maximum amount of an award for breach of contract is £25,000.

But whether the claim is unfair and/or wrongful dismissal, you cannot be forced to take an employee back and you always have the choice of paying compensation instead.

Offences and penalties

It is a criminal offence to refuse to pay the minimum wage, fail to keep proper records or to obstruct officers making enquiries under the legislation. There are fines of up to £5,000 for failing to pay and keep records of SMP and SSP, SAP and AP and for failing to provide information related to claims for SMP, SSP, SAP, AP, Incapacity Benefit, Maternity Allowance or Severe Disablement Allowance, plus a daily fine until you have put things right. A heavier fine or three months' imprisonment is the additional penalty for knowingly providing, or allowing to be provided, false documents or information relating to claims and compensation. Fines are also imposed for non-compliance with the anti-discrimination legislation.

Blowing the whistle

'Whistleblowers' who report a deliberate cover-up of any of the following are now protected against unfair dismissal and other sanctions:

- a crime or breach of a statutory obligation;
- a miscarriage of justice;
- danger to health and safety or the environment.

The self-employed and voluntary workers are not covered.

Protection only extends to:

- a reasonable, if not necessarily correct, belief at the time of disclosure;

- information passed to the employer or someone specified in the employer's internal procedure;
- information passed to a third party reasonably believed to be solely or mainly responsible for the wrongdoing;
- information passed to a legal adviser when obtaining legal advice.

To obtain protection for wider disclosures, such as to the police, media or MPs, the employee must either:

- give substantially the same information;
- reasonably believe he or she would be victimised if the disclosure were made internally;
- reasonably believe the evidence is likely to be suppressed or destroyed if disclosure is made internally.

Alternatively the wrongdoing must be exceptionally serious, the employee must not act for personal gain, and he or she must act reasonably, particularly in regard to:

- deciding to whom to disclose;
- the seriousness of the wrongdoing;
- whether the risk or danger continues;
- the reasonableness of the employer's response to a previous disclosure;
- whether the employee complied or should have complied with internal procedure;
- whether disclosure breaches the employee duty of confidentiality.

You cannot prohibit 'protected' disclosures by a clause in an employment contract or severance agreement.

Dismissal after whistleblowing is treated as automatically unfair, and a victimised employee can claim compensation for the loss suffered and expenses reasonably incurred. Protection extends to post-employment victimisation, eg denying a whistleblower a reference. You are therefore advised to have a whistleblowing policy that encourages confidential internal disclosure.

Human rights in the workplace

Individual rights protected by the Human Rights Act could be breached if:

- there is sexual or racial discrimination, or discrimination on the ground of sexual orientation;
- there is use of CCTV and monitoring of e-mail and phone calls;
- employees cannot practise their religion because of the demands of work;
- employees are bound by contractual confidentiality clauses.

An employer may be able to justify apparent breaches of these areas, but justification must be genuine and impingement of the right must go no further than is required to achieve the stated purpose.

Statutory references

Access to Medical Reports Act 1988
Adoption and Children Act 2002
Companies Act 1985
Contracts of Employment Act 1972
Copyright, Designs and Patents Act 1988
Data Protection Act 1998
Deregulation and Contracted Out Act 1994
Disability Discrimination Acts 1995 and 2005
Employment Acts 1980, 1982, 1989, 1990 and 2002
Employment Equality (Age) Regulations 2006
Employment of Children Act 1973
Employment Protection Act 1975
Employment Protection (Consolidation) Act 1978
Employment Relations Acts 1999 and 2004
Employment Rights Act 1996
Employment Subsidies Act 1978
Equal Pay Act 1970
Equality Act 2006
Factories Act 1961

Fixed Term Employees' Regulations (Prevention of Less Favourable Treatment) Regulations 2002
Health and Safety at Work Act 1974
Human Rights Act 1998
Industrial Tribunals Act 1996
National Minimum Wage (Enforcement Notices) Act 2003
Part-Time Workers (Prevention of Less Favourable Treatment) Regulations 2000
Public Interest Disclosure Act 1998
Race Relations Act 1976
Regulatory Investigative Powers Act 2000
Regulation of Investigatory Powers Act 2000
Rehabilitation of Offenders Act 1974
Sex Discrimination Acts 1975 and 1986
Social Security Acts 1975 and 1989
Social Security Contributions and Benefits Act 1992
Sunday Trading Act 1994
Trade Union and Labour Relations (Consolidation) Act 1992
Trade Union Reform and Employment Rights Act 1993
Wages Act 1986

9

Trading

This chapter covers the law of sale of goods and consumer credit, which affect the day-to-day search for profits. Like the law of landlord and tenant and insurance, they are based on contract law.

Contracts

Contracts are agreements between willing parties who exchange promises, eg a promise to deliver goods in return for a promise to pay. The promises *plus* implied terms make up the contract and contract law dictates the remedies for non-performance.

Theoretically, and with important exceptions, oral contracts are as good as written ones but it is better and safer to incorporate business arrangements into written contracts.

Some agreements, including some leases and business contracts, must be written and state that the document is intended to be a deed and both parties must sign (execute) it. One witness is sufficient unless signing on behalf of someone else (eg a company), when there must be two. Sealing, ie sticking a red seal at the foot of the document, is only necessary when required by a company's Articles but the deed must be delivered (handed over).

Only the parties are liable under the contract but agents can pass liability to a principal (as directors do with the company).

Third parties, however, can now claim the same rights and remedies as the contracting parties if the contract specifically gives them rights or if it

was made for their benefit. The third party must be identifiable by name or description, and may have to share rights and remedies with a contracting party. If they have rights, they cannot be deprived of them without their consent unless the contract provides for it. There are, however, no third party rights in employment contracts, contracts for the carriage of goods and contracts relating to negotiable instruments (that is, cheques, bills of exchange, etc – see pages 144–48).

Contracts for business abroad made via e-mail may be governed by foreign law. They should therefore state that they are governed by English law for convenience, speed and to save costs. Otherwise where the case is heard may have to be decided in accordance with the Rome Convention. And you may have to pursue judgment through foreign courts anyway, if there is no property here to satisfy the claim.

Arbitration

You can agree to have disputes settled by arbitration or mediation. There may be considerable savings in costs, particularly in landlord and tenant and commercial disputes. Information and an overview of the various UK schemes and how they work is available on the Advice Services Alliance's website, www.adrnow.org.uk. The organisation is independent of ADR providers and government.

Buying and selling for cash

If goods are sold for cash the transaction is governed by the sale of goods legislation and the custom of the trade.

Business buyers have partial protection. They can safely assume the seller owns the goods and the parties cannot be totally unreasonable – a seller with a monopoly will probably be unable to exclude the statutory quality guarantee.

Consumers have full protection: goods must be of satisfactory quality and fit for the purposes for which goods of that kind are commonly supplied, taking into account the price and other relevant circumstances. 'Quality' includes:

- the state and condition of the goods;

- appearance and finish;
- safety and durability;

and they must be free from minor defects except for defects:

- drawn to the buyer's attention;
- discoverable on inspection, if the buyer was given a chance to inspect them;
- apparent on reasonable inspection of a sample in sale by sample.

And they must correspond with samples, descriptions and display items. The protection covers some agreements to hire goods and contracts for services, including repairs and maintenance where work must be done in a reasonable time, with reasonable care and skill and, if no price is agreed, at a reasonable price.

Consumer contracts must be in 'plain intelligible language' and 'unfair' terms are unlawful and void, which here means contrary to good faith and significantly weighting the contract against the consumer. The consumer can now, for instance, sue directly on a penalty clause even if the contract states that he or she has no right to do so.

Selling to consumers can bring liability for others' mistakes, eg for inadequate manufacturer's instructions.

Liability for quality and quantity can be restricted or excluded but the law more readily permits a limitation of liability. Only specific wording excludes liability for negligence or non-performance and in dealing with consumers the clause or notice on your premises has no legal effect. Widely framed indemnity clauses are illegal and you are liable for accidents resulting in personal injury or death. But liability for financial loss and damage can be restricted if the contractual clause or notice is reasonable in the circumstances. Here the bargaining strength of the parties and the price are relevant in business transactions and consumers have more protection.

Importer, manufacturer, packager, carrier, installer, distributor, retailer, hirer and anyone putting names or labels on goods is strictly (automatically) liable to consumers for death, personal injury and loss or damage to property exceeding £275. Defences include compliance with the law or scientific and technical knowledge, and liability can be passed up and down the chain of supply. Personal injury claims must be made within three years of the date the claimant knew his or her rights; a six-year time limit applies to contractual

claims. No claim can be made after products have been circulated for 10 years.

A manufacturer's guarantee cannot limit liability for negligence or exclude or restrict the consumer's contractual rights.

In commercial transactions you can agree almost anything you like but there are legal limits. The following clauses are void:

- contravention of EU law;
- excluding or restricting liability for personal injury or death due to negligence;
- excluding or restricting implied terms as to title and in consumer contracts restricting implied terms as to description, quality and fitness;
- excluding or restricting liability in guarantees for loss or damage arising from defective consumer goods due to negligence in manufacture or distribution.

In deciding if a term is unfair to consumers, all the relevant circumstances at the time the contract was concluded are taken into account, including the nature of the goods and services. And the following clauses are subject to the 'reasonableness' test:

- attempts to exclude or restrict liability for negligence causing loss or damage;
- attempts to exclude or restrict liability for breach of contract;
- attempts to entitle a party to provide a contractual performance substantially different from that reasonably expected;
- attempts to provide no performance if one party is a consumer or contracts on the other party's standard terms;
- attempts to require a consumer to indemnify someone else for liability for negligence or breach of contract;
- negligence causing loss or damage.

Agreeing the contract

First comes the offer. When a firm offer is accepted, the contract is complete. Accepting a specific quantity of specific goods delivered over a fixed period at a fixed price is acceptance of the whole consignment, even if delivered

by instalments. A buyer can revoke a contract for a maximum quantity as and when demanded. It is basically a standing offer, each order being placed under a separate contract, but goods already ordered must be accepted.

Acceptance by post is received when posted even if not received. Oral, faxed and (presumably, there are no cases on it) e-mailed acceptance is received when heard or seen. Offers to sell can be cancelled any time before being accepted but should be confirmed before selling elsewhere. Acceptance varying an offer – eg by asking for a different quantity – may be a counter-offer, requiring the other side's acceptance. If you do not ask for formal acceptance, goods are accepted unless rejected within a reasonable time or they form part of a 'commercial unit' (see below) but not if a buyer asks for or has agreed to repair or has re-sold them.

Standard terms of business in consumer transactions must be intelligible and consumers can refer to the courts to assess fairness. Business customers are less protected and if both parties use standard terms – eg in order forms and delivery notes – each set may be a counter-offer. The contract may then incorporate the terms of the last document exchanged but unusual or onerous terms are incorporated only if specifically pointed out.

Payment and delivery

The law will not put a whole contract together. Terms of the trade or terms included in previous dealings may be incorporated, but if price, quality, size, style and design or content are not agreed, there may be no contract unless omissions are minor details. If price is not agreed, the buyer must pay a 'reasonable' price within a reasonable time. Deposits are usually lost if the buyer does not complete the transaction but part payments must be returned.

The right to claim (statutory) interest at 8 per cent above current bank base rate on debts for goods and services supplied to other traders is now automatically incorporated into business contracts. Interest becomes due the day after the specified date for payment, or the 30th day after delivery, or the 30th day after the purchaser is notified of the debt – whichever is the later.

A contractual term excluding statutory interest is void unless you have agreed a term allowing interest on late payments at a reasonable and substantial rate.

Unless otherwise agreed, you can take delivery when you pay. If nothing is agreed, the law spells out the details as follows:

- You can refuse delivery of more or less than ordered, unless the amount is negligible. If accepted you must pay, *pro rata*, at the contract price.
- If goods are mixed with goods not ordered, you can accept all the goods or only those ordered.
- You can reject all or part of a consignment, including goods under an instalment contract, which does not conform with the contract, *unless* part of a 'commercial unit' and division would impair the goods' value or character – eg parts of a machine – but you may be able to exclude this provision in business transactions.

And you do not have to return rejected goods, although you must notify the seller of rejection.

Payment, unless otherwise agreed, is not due until delivery, but if goods are lost or destroyed while at your risk, you may have to pay for them. When you pay, the seller must deliver or pay damages. If unique goods – eg antiques – are involved, the court will order delivery whatever the cost.

If the price is not paid or offered, the seller can retain goods, stop them in transit or sell them elsewhere. After delivery to a carrier, delivery can only be held up if the right has been expressly reserved, unless the carrier is an independent middleman. Delivery of instalment contracts cannot be held up to extract payment for earlier deliveries.

The owner takes the risk and a buyer may own goods before receiving and paying for them. A clause providing goods remain the seller's until paid for – a 'retention of title clause' – protects a seller if a buyer becomes insolvent. This is relatively straightforward for intact goods but provisions covering sale proceeds or materials to be mixed or processed with other goods should be professionally drafted. You may also have to register a charge on the buyer's assets in the Register of Bills of Sale or with the Companies Registry to preserve priority in insolvency.

Ownership passes from seller to buyer as stated expressly or by inference from the contract or surrounding circumstances. If the question is still open, ownership depends on whether goods are:

- 'specific' – identified and agreed at the time of the contract;
- 'unascertained' – bought from bulk or of a particular type – eg 12 clocks from stock or 12 clocks.

Goods can also be 'ascertained' by 'exhaustion', for example your purchase of 600 crates of beer sent to you by lorry carrying a consignment of 1,000 crates is yours as soon as the carrier offloads 400 crates.

Similarly, if you order a quarter of a bulk consignment, eg 8,000 litres of oil, brought to you by tanker, provided the contract of sale identifies your order, you own 2,000 litres of the oil as soon as you have paid for it.

The law then makes the following rules regarding ownership for specific goods:

- if finished and in a deliverable state – the buyer's when the offer is accepted;
- if put into a deliverable state – eg by weighing – the buyer's when notified they are ready to deliver;
- if in the process of construction/manufacture – the buyer's when materials are set aside and identified;
- if held on sale or return – when agreed or accepted, otherwise the buyer's within a reasonable time.

Future or unascertained goods in a deliverable state sold by description are the buyer's when handed to him or her or a carrier or put in storage.

These rules are contractual only and do not apply to negligence claims.

Misrepresentation

When you are deliberately misled you may be able to claim damages plus reimbursement from the seller, but you must prove that the misrepresentation persuaded you to close the deal. You can usually cancel if the seller is careless or genuinely mistaken, unless you have agreed to accept the goods or a third party is involved, but a specifically worded clause can restrict or exclude liability.

Unfair, aggressive and misleading trading

There is now a duty not to trade unfairly under the 2008 Protection from Unfair Trading Regulations. Detailed regulations about pricing, trade descriptions and misleading pricing have been replaced by a general ban on unfair trading,

considerably simplifying consumer protection in the United Kingdom and the EU. The Regulations aim to ensure traders act honestly and fairly with consumers, requiring them to stop aggressive selling and misinforming and misleading consumers about products or services, so that they can make free and informed decisions.

Businesses which fail to comply can be prosecuted and fined after investigations by the local authority's trading standards service and other organisations and traders and their staff are advised to read and understand the Regulations to ensure compliance.

Information is available from local authority trading standards offices and the following websites: www.businesslink.gov.uk/unfairtrading (England), www.bgateway.com/unfairtrading (Scotland), www.hiebusiness.co.uk/unfairtrading (Scottish Highlands & Islands), www.businesseye.org.uk (Wales) and www.nibusinessinfo.co.uk/unfairtrading (Northern Ireland).

Other criminal offences

The offences covered in the Protection from Unfair Trading Regulations which overlap with the Trade Descriptions Act (TDA) are to be repealed. Currently, however, it is also an offence under the TDA to apply false trade descriptions (FTDs) to goods, or to supply or offer to supply, goods to which one has been applied. This covers almost any oral or written statement as to quantity, size, manufacture, production, composition, fitness for the purpose, strength, performance and other physical characteristics, testing and approval; previous ownership and other history and dishonesty do not have to be proved. Liability can be disclaimed by an effective disclaimer specifically brought to the buyer's attention.

The provisions also cover a private seller's oral statements and descriptions of services and accommodating, unfair pricing and misleading indications of British origin. You can be vicariously liable for an employee's FTD if you knew it was false when made or read.

Sole traders, partnerships and directors can be convicted under the Fraud Act 2006 if they:

- make a dishonest false representation in words or conduct intending to make a gain or cause loss or risk;
- wrongfully fail to disclose information;

- dishonestly abuse a position – eg by disclosing confidential information;
- obtain services dishonestly; *or*
- possess something to be used in fraud.

Local weights and measures authorities can make test purchases, enter premises and seize goods, but usually issue proceedings only if there is a public need for protection. If you are trading for profit you can bring civil proceedings for injunctions to restrain a competitor's further wrongful acts, and you can claim damages and costs.

It is an offence to make, or not correct, uninformative or misleading bargain offers for foods, services, accommodation and facilities (other than investment business).

Protection for the business trader in the new fair trading framework is provided under the Business Protection from Misleading Marketing Regulations 2008. The Regulations specify what comparative advertising – advertising which identifies a competitor or a competitor's product – is permitted and makes misleading advertisements or 'indications' a criminal offence.

'Indications' are misleading if:

- they deceive or are likely to deceive; and
- are likely to affect a trader's economic behaviour or injure, or are likely to injure, a competitor.

Buying and selling on credit

The 1974 and 2006 Consumer Credit Acts and associated legislation apply to credit arrangements for amounts exceeding £50, excluding interest and including optional charges and insurance – other than life insurance premiums for loans secured on land. *But* existing credit agreements within the £25,000 previous statutory limit are unaffected.

The sum of £25,000 continues to be the limit for a loan entered into by an 'individual', ie a sole trader or partner in a partnership of less than four partners, if it is 'wholly or predominantly' for business purposes and the agreement includes a declaration to that effect. The declaration will, however,

be ineffective if the creditor, or someone acting on his or her behalf, eg a broker, knew or had reasonable cause to suspect that the agreement was not being entered into for business purposes.

Unless agreed otherwise, the agreement between lender and dealer is covered by the sale of goods legislation.

The £25,000 limit does not apply to company borrowings, or loans to partnerships with more than three partners. And credit arrangements with banks, exempt lenders and companies with a capital of over £250 million with a specialised banking service are not covered by the consumer credit legislation. Except for EU central banks and exempt lenders, banks must be licensed and comply with banking legislation. No statutory credit can be charged in connection with a credit or security agreement.

Debtors with a 'high net worth', ie with earnings or assets over a currently unidentified threshold can opt out of the legislation provided the creditor obtains a 'statement of high net worth' for the debtor from an appropriately qualified third party. As from 6 April 2007 new agreements with unfair or oppressive terms can be set aside by the court and the creditor, or his or her associate, may be ordered to vary the terms or repay some or all of the amounts paid.

Anyone advising on credit terms must have a licence, including debt administration and credit information service providers. Licences are valid indefinitely and cost £380 for sole traders and £725 for partnerships and companies. They are not transferable.

No fee is payable by registered loan and friendly societies, or credit unions, or debt counsellors and adjusters, unless they charge fees or commission.

Applications can be downloaded from the OFT website, www.oft.gov.uk, made online, or obtained from the Office of Fair Trading (OFT), Fleetbank House, 2–6 Salisbury Square, London EC4Y 9JX (Tel: 020 7211 8608).

Applicants must satisfy the OFT that they are, and continue to be, fit to engage in the specified credit activities, taking into account relevant circumstances, credit competence and current and intended business practice. Applicants for debt collection and debt management categories must complete a Credit Competence Plan and applicants involved in high-risk lending, broking, debt administration, and credit reference agencies a Credit Risk Profile. On-site visits by the Local Authority Trading Standards Services (LATSS) may also be required.

The OFT can:

- refuse applications;
- grant licences in accordance with an application or on different terms;
- suspend, vary or revoke existing licences;
- impose Requirements if not satisfied with the licencee's or applicant's conduct – if not complied with, the applicant or licensee can face fines of up to £50,000.

There is a right of appeal against decisions and Requirements.

The OFT must be notified within 21 days of changes affecting the licence. Some changes increase the licence fee, eg changes in business premises, trading names and categories. No extra fee is payable if there is a change in partners or directors.

Unlicensed lenders can face fines of up to £5,000 and/or imprisonment and will be unable to enforce the agreement, although the borrower can do so.

Borrowers can also challenge credit agreements in court if the overall relationship is unfair to the borrower and the court can:

- alter the terms of the credit or related agreement;
- reduce the amount payable; or
- impose requirements on the lender or an associate.

Appeals against OFT licensing decisions are made to the Consumer Credit Appeals Tribunal.

Disputes can be referred to the Financial Services Ombudsman (FSO). Information is available on www.financial-ombudsman.org.uk.

If an unfair relationship harms the general interests of consumers, enforcement action can be taken under Part 8 of the Enterprise Act 2002.

It is also an offence to send out unsolicited credit cards or circulars about credit to anyone under 18. Unsolicited cash loans can only be offered at the lender's business premises.

Copies of agreements and notices can be sent out electronically. Borrowers are entitled to have details of their credit references and regular information about the state of their account, including notice of arrears and notices of default. If two consecutive payments are unpaid, they must be sent an 'early warning' notice. Additional information is likely to be necessary in current

running-account statements, eg credit card statements, warning customers about the dangers of making minimum payments and missing payments.

The creditor is only entitled to simple, not compound, interest on amounts in default. No interest can be charged if the debtor has not received an annual statement for fixed-amount and fixed-term loans and hire purchase, conditional sale and credit sale agreements. This provision applies to existing as well as new agreements.

Borrowers are entitled to have details of their credit references. They must be kept informed of the state of their account and receive annual statements and regular notices if the account falls into arrears or they are liable for a default payment.

With hire purchase, you hire goods with an option to purchase. They remain the seller's until the option is exercised. Conditional sale and credit sale agreements are contracts for the sale of goods at a price paid in instalments. In conditional sales, the borrower owns the goods when all payments are made. In credit sales, he or she owns them as soon as the contract is made.

Hire purchase and conditional sales are covered by the 1974 Act. Sale of goods legislation applies to credit sales but the rules on acceptance and delivery are the same whether goods are sold on cash or credit.

Most sales on credit are three-cornered: the dealer sells for cash to the lender and the lender sells or hires to the borrower.

The borrower's signed application form is his or her offer to the lender to buy on credit. When the dealer completes it, the form becomes the dealer's offer to sell to the lender. The lender accepts or rejects both offers and is responsible for the quality guarantee because he or she sells directly to the borrower.

'Regulated' agreements under the 1974 Act must be signed by the borrower and by or on behalf of the lender and must contain details of:

- the transaction;
- the cost of the credit;
- the right to pay the debt before the agreed date;
- the right, if any, to cancel and to whom notice of cancellation is given – usually within 5 to 14 days of signing, depending on the type of agreement. This gives the borrower time to consider the transaction.

Cancellation also cancels linked agreements. Items traded in part exchange or their value are returnable within 10 days and if the borrower returns goods, he or she can claim repayment, plus fees or commissions over £1.

The borrower must be given copies of the agreement. If inaccurate the agreement and linked security agreements are enforceable only by court order. In some cases the lender may not be able to enforce it at all.

Special formalities apply to mortgages. The borrower has 14 days to consider the loan which is only enforceable by court order.

If the lender has a right to cancel, notice of cancellation must usually be served on the borrower. The notice must:

- identify the borrower's breach of the agreement, – eg failure to insure goods, so it can be put right;
- state that if it cannot be put right, he or she can pay specified compensation instead;
- set out the consequences of failing to comply with the notice.

And no further action can be taken by the lender for at least seven days.

No notice is required when the borrower is in arrears or exceeds a credit limit if the lender:

- sues for arrears; or
- restricts the borrower's right to draw on credit.

When over a third of the price is paid, the lender can in some cases only enforce the agreement by court order but the borrower can apply to the court for extra time to pay at any time.

Security for the loan should be included in the agreement or in a document to which it refers. If the borrower provides security, there must be a separate agreement in a prescribed form signed by or on behalf of the guarantor or indemnifier, otherwise it is unenforceable without a court order. If security is given by a third party, eg a recourse agreement between the lender and a dealer, it does not have to comply with the Acts. Special formalities apply to some security agreements, eg mortgages of goods and assignments of life assurance policies, which are usually only enforceable if the agreement is enforceable, unless an indemnity is for a borrower under the age of 18.

Security and linked agreements are cancelled with the regulated agreement.

Credit buyer's protection

Buyer protection is the same whether you buy for cash or credit but the quality guarantee is backed by the lender. Both dealer and manufacturer are responsible if goods are not checked before delivery.

Legislation is being considered to require credit agreements to use simple language, to enable consumers more readily to understand the cost of paying the debt and to remove financial penalties for paying the debt off early.

Consumer hire agreements

These are covered by the Acts if the credit is for more than three months and there are at least three instalment payments. If annual payments exceed £300, or the goods are specialised goods for the borrower's business, or they have been leased to someone else, the lender can repossess them without a court order but only if he or she has obtained consent to entry of the premises.

Hiring industrial plant and machinery

Some manufacturers offer their own financing if agreements are outside the financial limits and machinery is often leased. It then remains the manufacturer's or dealer's property and the borrower's cost of hiring is deductible for tax purposes. In credit sales, the borrower owns the goods and can take advantage of capital allowances.

Mortgages

Mortgages are outside the Acts and some other loans are specifically exempted but second mortgages on land obtained by private individuals are covered by the Acts, whatever the amount.

Consumer credit businesses dealing with first charge mortgage protection, payment protection or similar insurance may need permission from the Financial Services Authority (FSA) to sell or administer regulated mortgage and general insurance contracts. Information is available from the FSA, 25 The North Colonnade, Canary Wharf, London E14 5HS (Tel: 020 7066 1000) and on their website, www.fsa.gov.uk.

Doorstep selling

Consumers can refuse to pay for unsolicited goods or services delivered to their home address after an unsolicited visit or telephone call. There is a right to cancel within seven days of contracting and to return unsatisfactory goods within seven days of receipt. The trader must serve notice of the right to cancel within seven days of contracting, stating who must be notified, otherwise the agreement is unenforceable, although the consumer's rights are unaffected. Notice of cancellation must be in writing and given personally or by post. Consumers need not return goods until repaid unless a written request is received within 21 days but must take reasonable care of them in the interim. Perishable or consumable goods, goods incorporated into the consumer's property, eg double glazing, or supplied for an emergency need not be returned but the cash price must be paid.

The provisions also cover goods and services other than those discussed at the trader's premises if not usually supplied by him or her and contracts made while on trips organised by the trader away from business premises. Contracts for work and materials for house repair are covered unless linked to a mortgage but the following are excluded:

- contracts for time share, sale of land and house extensions;
- food, drink, household consumables;
- purchases from trade catalogues if there have been continuous dealings between customer and sales representative;
- some contracts of insurance;
- investment agreements;
- contracts for bank deposits.

Hire purchase, conditional sale agreements and credit exceeding £35 are excluded. The Acts cover credit of between £50 and £25,000 for business purposes to individuals and partnerships with fewer than three partners, but there is no protection for credit between £35 and £50.

Mail order

Mail order contracts often have a cancellation clause and buyer protection is the same as in cash sales. Unless goods are retained to compel repayment,

they must be handed over on written request but the customer does not have to arrange for their return.

Remedies for non-performance

If goods are unsatisfactory:

- Consumers under conditional sales agreements can reject them, even after delivery, unless the transaction has been confirmed.
- If covered by the 1974 Act you can cancel – if the cash price is between £100 and £30,000 supplier and lender are jointly liable to repay deposits.
- In retail sales for cash the customer can refuse credit notes and claim repayment.

A negligent carrier is liable to the owner of damaged goods, even if the owner is not consignor or consignee.

Take advice before claiming for non-delivery. Depending on whether goods have 'perished' (deteriorated), been destroyed or have disappeared, the buyer may be able to claim damages or repayment but may have to pay the seller's necessary expenses. If risk has passed to the buyer, the buyer must pay and claim separately for damages.

If goods do not belong to the seller, you may have to hand them to the owner and claim damages. Goods bought through agents can usually be retained but you should take legal advice before asserting your rights.

If a transaction becomes illegal or there was duress or misrepresentation, there may be a right to rescind (cancel) the contract.

In some circumstances a buyer can claim for consequential loss but reasonable steps must be taken to minimise the loss.

Fines and penalties

Traders whose advertisements mislead consumers about the total charge for credit are liable to fines of up to £2,000 and/or imprisonment.

Statutory references

Administration of Justice Act 1985
Arbitration Acts 1950, 1975 and 1979
Banking Act 1979
Bills of Exchange Act 1882
Bills of Sales Acts 1878 to 1882
Business Protection from Misleading Marketing Regulations 2008
Companies Acts 1985 and 2006
Competition Acts 1980 and 1988
Consumer Arbitration Agreements Act 1988
Consumer Credit Acts 1974 and 2006
Consumer Protection Act 1987
Consumer Safety Act 1978
Contracts (Applicable Law) Act 1990
Contracts (Rights of Third Parties) Act 1999
Deregulation and Contracting Out Act 1994
Fair Trading Act 1973
Fraud Act 2006
Late Payment of Commercial Debts (Interest) Act 1998
Latent Damage Act 1986
Law of Property Act 1925
Law of Property (Miscellaneous Provisions) Act 1989
Law Reform (Frustrated Contracts) Act 1943
Limitation Act 1980
Misrepresentation Act 1967
Protection from Unfair Trading Regulations 2008
Sale of Goods Act 1979
Sale of Goods (Amendment) Act 1995
Sale of Goods (Implied Terms) Act 1973
Sale and Supply of Goods Act 1994
Supply of Goods and Services Act 1982
Sunday Trading Act 1994
Supply of Goods (Amendment) Act 1994
Supreme Court Act 1981
Trade Descriptions Acts 1968 and 1972
Unfair Contract Terms Act 1977
Unfair Terms in Consumer Contracts Regulations 1999
Unsolicited Goods and Services Act 1974

10

Cash and credit at home and abroad

Most trading is for cash or credit and your books are debited and credited with money amounts even if you only deal in paper, with rights and a value varying with the content and creditworthiness of the signatories.

You and your bank

Your creditworthiness essentially depends on your bank, which must:

- take reasonable care in conducting your business – they are liable for payments on cheques if they are careless or suspect fraud;
- follow your instructions – they are not obliged to warn of any risks inherent in doing so;
- honour cheques to the limit of the account or overdraft – if they refuse, you may be able to claim damages;
- pay you in cash on request;
- not divulge information about you unless compelled by law or the public interest. If a court requires information, they do not have to inform you.

If asked for advice, their duty of care is very limited and can be further limited by disclaimers of liability.

And you must:

- draw cheques with reasonable care;
- notify the bank of forgeries.

Opening a bank account

When you open the account, the bank requires references. For partnerships, it requires details of the partners and their authority and involvement in the business and a copy of the partnership agreement. Usually, all the partners sign the mandate (agreement) which sets out assets and liabilities and gives instructions as to the conduct of the account – eg who signs cheques and requests advances – and they must confirm that securities to be held by the bank apply to existing and future liabilities and undertake to notify changes in the partners or the agreement. A sole trader's mandate stands until the account is closed or the business wound up. With partnerships it continues even if the partners or the partnership name changes, but incoming partners should confirm its terms and outgoing partners remain liable. Cheques drawn by deceased or bankrupt partners must be approved by the partnership, unless the mandate specifies otherwise.

Opening an LLP or company account is more complicated because of the protection of limited liability. The bank must see the Certificate of Incorporation and the Partnership Agreement or Memorandum and Articles of Association and the company's resolution appointing them. The Partnership Agreement or the resolution is the mandate with the bank and gives instructions about operating the bank account.

Usually the bank supplies a draft agreement for the LLP or resolution to be completed and passed at the first meeting after arrangements have been provisionally agreed. The bank may want a separate agreement or resolution covering overdraft facilities, incorporating the designated partners or directors' undertakings given on behalf of the LLP or company. The mandate is terminated by agreement with the LLP or resolution and ends if the account is closed, a receiver appointed or the LLP or company goes into liquidation.

Guarantees

A guarantee for a sole trader or partner in a partnership of fewer than four partners is covered by the Consumer Credit Acts if it is 'wholly or predominantly' for business purposes. The agreement must include a declaration to that effect, but will be ineffective if the creditor, or someone acting on his or her behalf, eg a broker, knew or had reasonable cause to suspect that it was not a business loan. The guarantees can be open or limited to a fixed amount and become operative when signed by the guarantors. If co-guarantors are insolvent, you can be liable for the whole amount.

Directors' guarantees are not covered by the Consumer Credit Acts.

Bank guarantees commit you to repay any money owed on all your bank accounts for an indefinite period. The guarantee continues until renegotiated, but a deceased guarantor's estate may not be liable, so co-guarantors should sign on behalf of 'their heirs, executors and administrators'.

Under other guarantees you can turn to the principal debtor and set off anything already paid and you are then entitled to any security given for the debt. Alternatively you or the creditor can sue the debtor or 'prove' – establish your claim – in his or her bankruptcy or liquidation.

The sole trader and partner are liable for all business debts, but when company debts are paid, directors are only liable if there are problems with floating charges, or fraudulent preferences, or there has been fraudulent or wrongful trading.

Payments

Your cash and paper are negotiable, ie they give rights and obligations which are transferable. If you hold a negotiable instrument you can sue on it. When you give value in good faith – becoming a 'holder in due course' – it becomes valid even if invalid initially, *provided* it is current, unconditional and appears to be properly completed, unless there is a forgery. Trading via bills of exchange and commercial credits is usually confined to larger businesses, although bills are fairly common in some manufacturing trades and heavy industry. Export business is usually done under letters of credit. Historically and currently a bill of exchange permits a seller to be paid when goods are shipped, although the buyer does not pay until they are received or sold elsewhere. The period (tenor) of the bill is usually at least three months,

a bank or finance house standing as intermediary for payment, and charging a commission for the advance during the period of transit by discounting the payment. Bills can also be accepted, ie by the acceptor's confirmation that the drawee will pay on the due date. The drawer pays the acceptor an agreed percentage of face value, acceptance is endorsed on the bill, the bill becomes freely negotiable and the acceptor becomes primarily liable to the holder.

The main types of negotiable instruments are:

- bills of exchange – a cheque is a bill;
- promissory notes – which include bank notes;
- bankers' drafts – which can be treated as bills or promissory notes.

Bills of lading – receipts for goods sent by sea – are semi-negotiable; once invalid, they remain invalid. Postal and money orders are not negotiable. Money orders are void 12 months after issue.

Negotiable instruments are promises to pay on a specified date. Banks must stop payment on request but you can be sued on the dishonoured promise to pay and your bank is liable if your cheque is wrongly dishonoured. A formal notice of dishonour is usually sufficient to enforce payment through the court at minimal cost. Defences are very limited and if there is a dispute, the debtor must usually pay up and sue in separate proceedings.

Cheques

A cheque is an unconditional order from you (the drawer) to another (your bank, the drawee) to pay a sum of money on demand to a specified person or 'to bearer':

- If 'to cash or order' it is valid but *not* a cheque because there is no payee.
- Post-dated cheques are valid but banks usually refuse to pay before the due date.
- It is not a continuing security but you remain liable for up to six years (although banks usually return cheques for re-issue after six months).

A cheque crossed 'a/c (or account) payee' with or without 'only' is non-transferable – the crossing can be deleted if you want to transfer it. If you add 'not negotiable' it cannot be negotiated. It can be transferred by endorsement but the endorser cannot pass better title than he or she has him- or herself – a stolen cheque is valueless – and the bank must give notice of dishonour to endorsers.

Unless post-dated, a cheque comes to life when handed over or the payee is told it is held on his or her behalf. The holder is the person to whom it is payable (the payee) or the named endorsee or anyone holding a cheque payable 'to bearer'. The holder can alter the crossing but other alterations without the drawer's consent usually invalidate the cheque. If endorsed after alteration, it is valid for the altered amount against the endorser.

Holders take cheques on the same terms as the payee. But if a cheque is not overdue, the holder gives value in good faith, the cheque is regular on its face and the previous holder was entitled to it, the holder becomes a 'holder in due course'. As a 'holder in due course', he or she is in a stronger position: the cheque can be freely negotiated, payment can be claimed through a non-existent payee and it may be claimable on an undated or stopped cheque, or one which the drawer was fraudulently induced to issue.

A bearer cheque is negotiated by handing over – if payable to order it must be endorsed by signing it, the signatory thereby becoming liable for the amount – *and* delivering it to another holder. If no endorsee is named, any name can be written above an endorsing signature. If you are signing or endorsing on behalf of someone else, limit or negate personal liability by signing 'for and on behalf of' your principal or the business *and* describing the capacity in which you sign. Company names must be on all negotiable instruments, endorsements and orders for money, and directors endorsing as guarantors are liable to both drawer and holder. One signatory can stop payment on joint company or partnership accounts but one partner's signature is normally sufficient on cheques paid by, or to, the business. Cheques made out to more than one payee must be endorsed by them all, unless one has authority to sign for the others. You can direct endorsees to be paid jointly on the cheque but the face value cannot thereafter be split.

Lending money on an accommodation cheque – by post-dating it and making it payable to someone who makes a loan to a third party – makes you liable to a holder for value.

Banker's drafts

A draft is an order for payment made by the payer's bank and the bank is the drawer and drawee. The amount, place of payment and the name of the beneficiary/payee appear on the draft, which when crossed works like a cheque.

Promissory notes

Promissory notes are conditional or unconditional promises to pay on demand, or on a fixed or determinable future date, a fixed sum to, or to the order of, a specified person or to bearer. They can be made payable with interest or in instalments and can provide that if an instalment is unpaid, the full amount becomes due.

A note need only be presented for payment if a place is specified and endorsers are only liable if it has been presented. With some exceptions a note-holder's legal rights and remedies are the same as those of a holder of a bill of exchange.

Bills of exchange

A bill is an unconditional order in writing addressed by one person (the drawer) to another (the drawee), signed by the drawer, requiring the drawee (who, when he or she signs, becomes the acceptor) to pay on demand or at a fixed or determinable future date, a fixed sum to, or to the order of, a specified person or bearer (the payee). Bills are more easily negotiated than cheques and notes; the right to future payment can be more flexible and is more saleable for immediate cash.

The differences between bills and cheques are as follows:

- Bills can be drawn on anyone, a cheque only on a bank.
- Bills can be payable on demand or in the future – cheques only on demand.
- Bills must be presented for payment, or the drawer and endorser are discharged; a cheque drawer is liable for six years.
- Cheques can be crossed, bills cannot.

- Paying and collecting banks are more exposed when dealing with bills than cheques.
- Unless payable on demand, bills are usually 'accepted'. A cheque is not usually accepted, so the drawer is primarily liable.
- A bill, but only rarely a cheque, can be 'backed' – ie endorsed by someone who is neither drawer nor acceptor and who is liable to a holder in due course. It is backed when sold at a discount for immediate payment, the extra credit cover increasing the discount value.

A bill can be an order to pay from a fund or account, or set out the transaction giving rise to the debt. The value given for payment does not appear on the bill and where it is drawn or payable need not be stated.

A bill can be payable on demand, at sight, on presentation, at a determinable future date, after a fixed period after date or sight, after a fixed period after a specified event *but not on a contingency*. If no time is specified, it is payable on demand.

Interest or payment by instalments can be included with a provision that if an instalment is unpaid the full amount becomes due. If payable in foreign currency the rate of exchange can be specified, otherwise it is calculated according to the rate for sight drafts at the place of payment on the due date.

Bills drawn and payable within the United Kingdom or drawn or accepted on a UK resident are inland bills; other bills are foreign. The main difference is that foreign bills must be 'protested' if dishonoured, otherwise protesting may be optional. And inland bills are usually 'sola', ie drawn up in one part. Foreign bills can be drawn in sets of two or three parts (copies), each referring to the others, to protect against loss. You should accept and endorse only one.

Bills must be presented for acceptance and payment on the due date. Strictly, this is only necessary if payable after sight (when acceptance fixes maturity date), if specifically required, or if payable anywhere except the drawee's business or residential address. But they should be presented to secure the drawee's liability and the bills can then be negotiated and discounted – if the drawee refuses acceptance, the holder can immediately turn to the drawer. If the drawee later accepts it, acceptance is backdated to the date on which the bill was first presented for payment.

Bills can be accepted before the drawer signs or when overdue after dishonour, except for bills payable after sight which are dishonoured if not accepted. Acceptance can be:

- general – unconditional affirming the drawer's order; or
- qualified – conditional and can be of a partial amount only. The holder can refuse this – unless it is partial acceptance of face value – and treat the bill as dishonoured. Drawer and endorsers are then discharged from liability. Partial acceptance can only be protested as to the balance.

Bills must be presented for payment and acceptance before overdue unless payable on demand, when they can be presented for payment any time. Presentment is usually at the acceptor's or drawer's address and, if agreed, can be by post. All joint acceptors or drawers must be presented with it, unless one has authority to accept for them all. If an acceptor or drawer is bankrupt or dead, the bill can be treated as dishonoured or can be accepted by the trustee in bankruptcy or personal representatives but must first be presented. Although drawer and endorsers are usually discharged from liability if a bill is not presented for payment on the due date, the acceptor remains liable unless he or she has stipulated it must be presented for payment. If not accepted within a reasonable time, notice of dishonour can be given to drawer and endorsers but if the bill is not 'noted' or 'protested' the right of recourse against them may be lost.

Drawer and endorsers are liable when bills are dishonoured on presentment for payment. Non-payment of accepted bills gives a right of immediate action against the drawer as acceptor without having to protest the bill or give notice of dishonour.

Generally, notice of dishonour must be given to all parties, in writing or in person, on the day of dishonour or the next working day. Foreign bills require proof of presentation and dishonour. The bill must be re-presented by a notary public and refusal of acceptance or payment is 'noted' on the bill – a declaration (the 'protest') is then made in a separate document. Although not required for inland bills it is safest to do both.

Overseas payments

Overseas business is usually done under letters of credit or documentary or acceptance credits issued by banks or accepting houses, who lend their name where a buyer or seller is unknown or there is doubt about the economic and/or political situation. Interest rates vary with the risk and the trader's credit-standing.

For importers some banks require partial cash cover. The bank issues a letter of credit in favour of the supplier, undertaking to accept his or her bill drawn on them if accompanied by shipping documents. The supplier's bank buys the bill for cash and sends it with the shipping documents for presentation and acceptance to the importer's bank, which releases the documents to the importer, so that he or she can take delivery.

Overseas customers can open irrevocable documentary acceptance credits in their favour at their foreign bank. Their London branch takes the bills for current shipments on the security of the shipping documents. When accepted they can be discounted.

Importers can also arrange acceptance credits with acceptance houses or banks that accept bills drawn on them subject to conditions, but again they may require partial cash cover. The proceeds then go to the bank's overseas agents, who pay the supplier when he or she hands over the shipping documents. Alternatively, an overseas supplier may arrange with a London bank to draw bills on the security of the shipping documents, which are released to you against payment. They may have a documentary credit with a London bank to negotiate bills drawn by you on them. The bills are presented to the London branch, which sends them to the overseas customer's bank, where they are surrendered for cash or against acceptance of the bills.

Overseas suppliers can also draw sight or time bills on UK customers. Sight bills are sent to the United Kingdom with the shipping documents and presented to the importer for payment against delivery of the documents. With time bills the importer arranges a credit with a foreign branch or correspondent of his or her bank, which buys it at the bank's buying rate of exchange for similar UK drafts. The importer accepts it on D/A terms (documents against acceptance) when the goods are delivered on arrival or are warehoused and insured at the importer's expense until the bill is paid at maturity, although he or she may be able to take earlier delivery by paying a premium.

Acceptance credits are often made on a revolving basis: when drafts mature, new drafts are drawn up to an agreed maximum. Raw materials are sometimes bought through London acceptance houses by acceptance credit. Drafts are accepted up to a specified amount drawn on the bank by a manufacturer, usually payable three months after date. The manufacturer must put the bank in funds at or before maturity date by way of cash or bills which can be discounted when accepted.

The Export Credits Guarantee Department (ECGD), PO Box 2200, 2 Exchange Tower, Harbour Exchange Square, London E14 9GS (Tel: 020 7512 7887), offers credit insurance by way of guarantees direct to exporters

and on goods and services sold on credit terms to the financing bank, as well as political risk insurance to UK investors in overseas markets. Information is available on their website, www.ecgd.gov.uk.

Different arrangements apply to ECGD support for UK exports to the EU and unconditional guarantees are available.

Cover on loans through foreign banks can also be arranged through the ECGD. Information and advice is available from your own bank and the government services, including the BERR.

Information about insurance for importers on credit purchases is obtainable through the Department for Business, Enterprise and Regulatory Reform. Similar schemes to the ECGD's are available if you are buying abroad and buyer credit guarantees from the supplying country may be available.

Selling debts

You can sell debts for cash under a factoring agreement, which sets out your undertakings as to the status of the debts, the factor's rights and the price paid for advance payment. The factor acts as a collection agent and is responsible for keeping accounts. You usually receive immediate payment of up to 80 per cent of the invoices accepted and the balance when the debt is paid, less the factor's charges, usually a percentage of turnover. The initial lump sum payment will also be discounted at a rate similar to bank charges on secured overdrafts, plus a flat monthly fee or a percentage of turnover. The agreement may attract stamp duty and should be registered as an assignment of book debts under the Bills of Sale Act or the Companies Act. Some banks offer a factoring service, buying debts at a discount on the security of invoices and interest is charged on the payment at a rate that is usually about the same as bank interest charged on secured overdraft facilities. You receive the balance of the face value of the invoice when the debt is paid. Other variations are *non-recourse factoring*, which provides 100 per cent credit cover on approved debts and *recourse factoring*, which usually provides more cash but no credit protection.

With invoice discounting, you retain control of the sales ledger and chase debts yourself. Again, you receive up to 80 per cent of accepted invoices and the balance less the discounter's charges when the debts are paid and, again, the charge is a discount on the initial lump sum payment plus a flat monthly fee or a percentage of turnover.

Statutory references

Banking Act 1979
Bank of England (Time of Noting) Act 1917
Bills of Exchange Act 1882
Cheques Act 1957 and 1992
Companies Acts 1985 and 2006
Consumer Credit Acts 1974 and 2006
European Communities Act 1972
Limited Liability Partnership Act 2000

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Intellectual property

Goods, services and anything manufactured, marketed or produced which depend for profitability and/or marketability on novelty or brand name are 'intellectual property' (IP). Like any other property, the law protects it.

Copyright works have automatic worldwide protection but other IP rights are only protected in the country where they are granted or registered. EC and worldwide design protection is obtainable, patent protection can be extended to the EC and some countries will extend UK protection after complying with local requirements.

Ownership

Ideas and inventions developed in the usual course of an employee's duties belong to the employer, unless entirely unrelated to the employee's usual work. It is therefore advisable to specify what inventions might fall within the course of their normal duties in employees' contracts. They will, however, retain a right to claim a fair share of the benefits of their invention.

Protection provided by the law

Protection varies but is principally aimed at stopping competitors exploiting your product or process without consent and covers:

- patent law – protecting 'uniqueness' of technological inventions;
- copyright – protecting literary, artistic and musical works, computer programs and databases, films, recordings, broadcasts and cable programmes;
- design right – protecting the appearance of mass-produced articles;
- trademarks – protecting commercial labels;
- protection against competitors disparaging your products maliciously and 'passing off' their products as yours;
- commercial exploitation of industrial secrets.

The UK Intellectual Property Office (IPO) has a mediation service team trained by the Centre for Effective Dispute Resolution (CEDR) which also deals with disputes referred from the courts and independent mediator. Hearings are at the IPO's offices in London and Newport. If already litigating, the parties can apply to a Hearing Officer to advise whether the dispute would be better dealt with through mediation. Information and Guidance notes are on the IPO's website, www.ipo.gov.uk.

Alternatively you can enforce your rights through the civil courts. Patent actions are the most lengthy, complicated and costly and often cease to be commercially important before trial. The award or decision is binding and litigating parties may be punished in costs if they refuse to mediate.

Copyright, trademark and passing off actions can be brought to trial within months and cost far less. Actions for infringing industrial design vary in cost and complexity, depending on the conduct of the action and the approach.

An interlocutory – pre-trial – injunction ordering a defendant not to continue or to embark on a course of action until trial is a fast and relatively cheap route but the plaintiff must in return undertake to compensate the defendant if the case is lost. If the plaintiff then wins, he or she can obtain a continuing injunction, delivery up or destruction of infringing items and compensation for financial loss. Trademark owners may also claim advertising costs for restoring their position, copyright and patent owners can claim compensation for forced reductions in price pending trial, and plaintiffs in passing off and slander of goods actions can claim compensation for damage to goodwill. Copyright owners can also claim damages for conversion, ie for work sold, or destroyed by, or as a result of, infringement. There may also be criminal liability and an offence under the Trade Descriptions Acts, bringing fines and penalties, including imprisonment and forfeiture or destruction of the offending goods and materials.

It is proposed to introduce voluntary Alternative Dispute Resolution (ADR) in the Patents County Courts to provide low-cost handling of intellectual property disputes to be heard by specialist single arbitrators whose award or decision will be binding. Mediation is part of the package which should offer a fast and relatively cheap route to a legally enforceable settlement.

Patents

Patent law gives temporary protection to unique articles and manufacturing processes superior to their predecessors and a properly drawn up patent gives a complete monopoly. Novelty is the basis of a patent and the product's importance decides whether competitors risk legal action or try to avoid your monopoly. The length of the protection may be decisive as to the practicability of competitors doing the necessary work to sidestep your patent.

Patent litigation is expensive but disputing parties can choose instead to ask the Patent Office for an opinion on patent validity and infringement.

Patent protection abroad is obtained through national applications in each country or a single application under the European Patent Convention (EPC) 2000 or the Patent Cooperation Treaty (PCT) 1970 as amended.

The UK 1977 Patents Act defines what is patentable in the United Kingdom and as from 13 December 2007:

- you can obtain an amendment to an existing patent after the date of the original grant or amend it by limitation with the European Patent Office (EPO);
- new methods of treatment or diagnosis can be patented, for instance a new medical use for a known drug;
- published European patent applications can be used to demonstrate that an invention is not new.

At the time of writing you cannot patent a computer program in the United Kingdom under the 1977 Patents Act, for instance, for an improved word processing program, but you can patent some inventions that include computer programs.

A successful application to the EPO under the 2000 EPC applies in every country in which the European patent is in force and limitations apply retrospectively to the date of grant. Applications can be made at any time after the grant, after opposition proceedings or after an earlier limitation.

If a claim invalidates the patent in an EU country, it can be amended separately in that country, or amended to overcome a specific prior art. If, however, the prior art is only valid in the UK, it can be amended the UK while maintaining broader protection in other EU countries.

You may also want to consider filing a single international patent application under the Patent Cooperation Treaty (PCT) as amended, which covers 138 countries including the United Kingdom. Applications by UK residents are made to a PCT Receiving Office, the EPO, or the International Bureau of the World Intellectual Property Organisation (WIPO) in Geneva. You must request permission to apply for a patent abroad if the application relates to military technology or could harm national security or public safety. Information about the procedure is available at www.ipo.gov.uk.

Agreements restricting competition

The following agreements should be drafted by specialists to ensure compliance with both British and EU law.

Patent licences

The manufacture, import, sale and use of patented articles or processes is only lawful with the consent of the patent holder, and with important exceptions you can agree any terms. When you license manufacture, it is implied you can use and sell the product/process yourself. Anyone knowing of restrictions must comply with them or risk infringement, but not every restriction is lawful. Under EU law you cannot limit inter-product competition which precludes granting an exclusive licence but there are some block exemptions. British law is also restrictive and you cannot usually force a licensee to buy unpatented materials, although you can agree preferential terms on unpatented goods if you comply with EU law.

Know-how licensing

These also restrict competition in breach of both British and EU law but there are individual and block exemptions.

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Research and development

Cooperation agreements for research and development are usually permitted under EU law and, although conditions are strictly defined, some agreements are specifically exempt.

Copyright

Copyright, design right, computer programs and e-commerce are protected under copyright law. E-commerce covers electronic transmission, digital broadcasting and 'on-demand' services; copy protection systems and digital watermarks are also protected. The European Copyright Directive, amending the Patents Act 1977, brings our patent system into line with the European Patent Convention and strengthens the enforcement of patent rights and the resolution of disputes. The amendments also restrict the type and scope of permitted exceptions to copyright and:

- grant performers exclusive right to control 'on-demand' transmissions of recordings of performances;
- permit some exceptions to reproduction right for some temporary, transient or incidental acts;
- grant increased protection to technological measures used by right holders, other than computer programmers, against unauthorised reproduction and copyright infringements;
- enable right holders of electronic right management information (RMI) to identify, track and assist with utilisation of works, including the conditions applying for the acts to be considered unlawful. The RMI must be associated with the copyright work. (This is entirely new in our copyright law.)

And there are increased sanctions and remedies.

Additional royalties are payable for some uses of copyright material, eg photocopying books and journals by businesses, that no longer fall within the scope of the fair dealing exception permitting fair dealing (see page 168). You should check with the Copyright Licensing Agency to see if you are covered by an existing industry licence for larger-scale business photocopying.

At the time of writing it is unclear what effect this provision has had on the licensing arrangements for royalties on sound recordings.

The Copyright Licensing Agency website on www.cla.co.uk has information about licences and guidance about changes in copyright law. Downloading or copying some online material, even for personal use, is a criminal offence, and any kind of technology that enables someone to play your legitimately acquired and copyright-protected CDs or DVDs on their PC is illegal.

Most industrial designs are copyright through initial drawings or prototype models, and copyright exists as soon as pen is put to paper or the model takes shape without registration or legal formalities. There is no copyright in an idea and others with the same idea have their own copyright, but your copyright stops exact copying.

Copyright gives the owner the right to stop others from doing something.

If recorded in writing (ie in notation or code, by hand or otherwise) copyright covers:

- original literary, dramatic works (including dance or mime) – no aesthetic merit or style is required, so lists, catalogues, etc are included;
- computer programs, databases and software products;
- original musical works – ie music excluding words or action;
- part or all the typographical arrangements of published editions of literary, dramatic and musical works;
- original artistic works comprising graphics (photographs, sculptures or collages irrespective of artistic quality), architecture (buildings or models for buildings) and works of artistic craftsmanship;
- original sound recordings, films, broadcasts, teletext, satellite and cable programmes.

The 'author' is usually the first owner. Otherwise the first owner is:

- the creator of literary, dramatic, musical and artistic works;
- the person responsible for undertaking arrangements for making computer programs;
- the person undertaking arrangements for making original sound recordings, films and cable programmes;
- the person making broadcasts;
- the employer for work done in the course of employment, though the creator may retain moral rights *and* the publisher is the owner of published works.

Both 'author' and country of first publication must qualify for protection. Broadly, protection covers British citizens, subjects and nationals, citizens of British dependent territories, British protected persons domiciled or resident in the United Kingdom and in countries covered by the Act and companies incorporated under British law for 70 years. For design right protection, qualifying countries extend to cover member states of the EU.

'Premier league' electronic and paper database creators are protected for the life of the 'author' plus 70 years whether or not the database is innovative. For 'first league' databases the period is life plus 15 years. 'Premier league' databases, eg *Yellow Pages*, indicate by their complex structure that some 'intellectual creativity' was involved, while 'first league' databases, eg telephone directories, are compiled through a basic mechanical arrangement of information. But the dividing line is unclear. Records of how a database was created using intellectual effort could help in obtaining maximum protection and unless created by employees, you should require creators to assign copyright to you or the business.

These apply to all and a substantial part of the works and there is infringement if any of the following are done without the owner's consent:

- copying, ie making a facsimile copy, including reduction or enlargement;
- issuing copies to the public, including renting out sound recordings, films and computer programs – but only when first issued;
- publicly performing literary and dramatic works, including audio and visual representations and publicly playing and showing recordings, films, broadcasts and cable programmes;
- broadcasting or including the work in cable service;
- adapting and translating literary, dramatic and musical works, and doing any of the above in relation to an adaptation.

Permitted acts include:

- 'Fair dealing' with a substantial part of a work – this allows use compatible with fair practice and justified in the circumstances, eg for criticism and reporting, *but* copying of literary, dramatic, musical and artistic works is only permitted for private study, research or educational purposes *and* reprographic copying, and a fee is payable to the author if the copying is done for commercial purposes. Copying some public documents is restricted.

- Performing, playing and showing works for educational purposes.
- Copying works in electronic form if purchased on terms that permit it.
- Rental of computer programs 70 years from the end of the year of first public issue.
- 'Reasonable extracts' of public readings in sound recordings, broadcasts or cable programmes unless expressly prohibited.
- Copying works other than broadcasts, cable programmes and typographical arrangements for use within 28 days by broadcasters and cable programme operators.

Not-for-profit and educational organisations do not need consent to produce large print, braille and audio editions of copyright works.

'Authors' of literary, dramatic, musical and artistic works and film directors have moral rights personal to them which cannot be assigned. Rights extend to adaptations and false attribution and essentially give rights to be given credit and have the creation respected. They cover:

- harm to reputation;
- 'paternity right' – to be identified (*but* not for computer programs or typeface design);
- 'right of integrity' – to object to derogatory treatment, ie additions, alterations and adaptations other than translation or change of musical key or register if there is distortion or mutilation, or honour or reputation is prejudiced (*but* computer programs and reports of current events are excluded);
- right to privacy of some photographs and films;
- the right not to have the work changed and possibly to have it maintained in good condition;
- exclusive right to authorise publication;
- right to withdraw and revise the work.

An employer owning copyright has no moral rights and they do not apply to fair dealing and incidental inclusion in sound recordings, films, broadcasts or cable programmes.

Rights are infringed by possession, sale, hire, rental or exhibition in the course of business or distribution which affects the author or director's honour or reputation.

Rights can be assigned in writing but only exclusive licences must be in writing. You can assign future rights and assignments for part of the copyright period.

The owner and exclusive licensee can stop infringement by injunction and obtain:

- search warrants and orders for delivery up and seizure of infringing copies – in some circumstances owners can seize copies themselves;
- accounts of profits;
- damages – *but* not if the infringer did not know or had no reason to believe copyright subsisted;
- an order restraining 'derogatory' treatment of moral rights of an author or director.

Devices for copy protection (software preventing unauthorised copying or use) are protected if the infringer knows or has reason to believe they are used for making infringing copies. They may also be protected under unfair competition law.

Broadly, these cover 'dealing', including importing and exhibiting, when the defendant knows or has reason to believe the articles are infringing copies and the 'consent or connivance' of a company's officers brings liability on them as well as the company.

Offences punishable with a fine and/or imprisonment are:

- playing or showing infringing works *but* not receiving infringing broadcasts or cable progammes unless intending to avoid payment;
- making or possessing articles designed or adapted for copying, knowing or having reasonable cause to believe they will be used to make infringing copies for sale, hire or use in business;
- gaining unauthorised access to a computer system;
- carrying out unauthorised modifications to, or erasing, a computer program.

The UK criminal courts can order search and seizure of infringing copies and HMRC will stop imports at the owners' request.

Copying, adapting, performing, broadcasting, recording, distributing or putting a protected work on the internet constitutes 'commercial' copying in breach of copyright, even if no money changes hands; copying for profit may increase penalties.

You can of course play your CDs and DVDs yourself and pass the originals on to someone else but you cannot pass on copies. Copying them from the internet effectively steals the copyright and persistently copying them leaves you open to legal action by the copyright owner(s).

Some countries permit a limited number of copies to be made for personal use, but there is no general right to copy before buying.

Internet service providers, the music industry and owners of copyright and related rights regularly remove illegal material from the internet. The music industry is pressing for increased action against copyright theft and internet infringers can face civil and/or criminal proceedings.

Performers' protection and performance rights

Rights last 70 years from the end of the calendar year of the performance. Infringement is by recording, live transmission and possessing, using, importing and dealing in illicit recordings. Performers and those with whom they have exclusive contracts can consent to breach of copyright – even though the performer is in breach of contract – or sue for infringement. The court can order search, seizure, delivery up and destruction of recordings, films and equipment adapted to produce them and it is a criminal offence to make, deal with or use illicit recordings. Defences are similar to those in other criminal copyright proceedings and penalties include fines and/or imprisonment.

Data protection

If you store data about living individuals who can be identified from your electronic or paper records, you must register with the Information Commissioner under the 1998 Data Protection Act. Forms and information are available from the Office of the Data Protection Registrar and an annual licence costs £35. Failure to comply with the Act can lead to prosecution, refusal of registration or service of enforcement transfer prohibition, or deregistration notices.

If requested, you must give data subjects details of the information stored, including its sources, uses, why it is held and to whom it is disclosed. You

can charge a fee for the service. You can be required to cease processing the data if it is causing or is likely to cause unwarranted and substantial damage to the data subject or anyone else, and the data subject can apply to court for compensation. If the data is incorrect or misleading, you can be required to rectify, block, erase or destroy it, and the data subject can refer to the Commissioner to assess whether you are contravening the Act.

Non-disclosure of some data is permitted, including management forecasts, management planning and information relating to national security, crime, taxation, health, education and social work.

Design right

'Design right' gives the following periods of protection to registered designs and artistic works:

- original non-commonplace designs of an article's shape or configuration – 10 years from first marketing with a 15-year limit from creation;
- registered designs – a maximum of 25 years;
- articles designed as artistic works exploited industrially – 25 years;
- artistic works not exploited industrially – 50 years.

There can be partial transmission of some rights and of part of the protected period. Assignments must be in writing and, unless otherwise agreed, registered design right includes design right.

Rights are slightly different from copyrights:

- Primary right is an exclusive right to reproduce commercially. There is primary infringement when articles are copied 'exactly or substantially to' the design. 'Kits' – 'complete or substantially complete' sets of component parts which infringe when made up – are included.
- Importing, possessing for commercial purposes, or dealing commercially with an infringing article knowing or having reason to believe it is such is secondary infringement.

There is a limited defence too of innocence and if the design is copyright and copyright is not infringed, there is no infringement of design right.

During the last five years of protection there is a 'licence of right' to perform restricted acts.

Design right owners and exclusive licensees have the same remedies as copyright owners and the court can also order forfeiture, destruction or other disposal of infringing articles. Unlike copyright, design right is effective only in the United Kingdom.

Non-functional designs, ie shapes, configurations or ornaments with eye appeal, applied to articles by an industrial process are protected by registration. The test of infringement is the eye of a customer interested in design. Registration is expensive but worthwhile if the design is an almost inevitable development in its field. It is then infringed by anyone using it, even if created entirely without reference to the design. The author is the original owner but the commissioner and employer are owners of commissioned designs and designs made in the course of employment.

The owner has exclusive rights to make, import for sale, hire or use for the purposes of trade and to sell, hire, offer or expose for sale or hire articles for which the design is registered and to which it, or one not substantially different, has been applied. Infringement is doing any of these without consent and making anything, or enabling anything to be made, to which the design is applied. Rights last for five years, extendable by five-year periods to a maximum of 25 years. There is a six months' grace period at the end of each period to permit late application and rights can be restored if registration lapses.

Applications for community-wide design right protection can now be made to the Office for Harmonisation in the Internal Market (OHIM), in Alicante, Spain.

Even without registration the appearance or configuration of your products is protected for ten years in the United Kingdom and three years in the EU but you must prove you hold the design and that it has been deliberately copied and it is difficult to establish a right to sell or license it.

Confidential information

Information, including trade and technological secrets, commercial records and marketing, and professional and managerial procedures, can be protected by obtaining undertakings to keep it confidential. This is only possible with those who receive information directly or indirectly and the law is reluctant

to impose obligations on ex-employees to stop them using their knowledge and skill.

Domain names

A domain name – your label on the internet – protects your business name from 'cybersquatters'. Check the availability of the name online at registration agents' or authorities' sites, such as www.123-reg.co.uk or www.UKreg.com. There is usually a small charge but you do not need to establish a website to register a domain name.

Trademarks and service marks

Trademarks are defined as signs capable of being represented graphically and which distinguish your goods or services. They can be words, names, designs, letters, numerals, the shape of goods or packaging, or distinctive sounds or smells, provided they can be graphically represented.

Service marks identify services and are registered and protected in the same way as trademarks.

Collective marks which distinguish goods and services of members of an association are also protected. A trademark search shows existing and pending registrations, but the search is technical and you are advised to use a trademark agent. Details can be found at www.itma.org.uk and www.cipa.org.uk. The agent can also check for rights of reputation or 'passing off' rights (see below).

Registration is refused if the mark:

- is not distinctive;
- consists of signs or indications designating the goods or services' characteristics, eg quality, quantity, purpose, geographical origin, *unless* the mark is distinctive through use.

In line with the Community Trade Mark (CTM) – see below – the IPO does not refuse applications because the same or a similar mark is already registered, but their owners will be notified of the application and it is up to them whether or not they file opposition. Opposition can be expensive but the IPO will give preliminary opinions on the outcome.

Registration is for 10 years, renewable for further 10-year periods.
When the mark is registered the owner can prevent the use of:

- an identical mark for identical and similar goods/services;
- a similar mark for similar or identical goods/services if there is a likelihood of confusion;
- an identical or similar mark for non-similar goods/services where the infringer would take unfair advantage of or damage the owner's established reputation.

The owner can require infringing articles to be handed over and claim damages and infringers may be fined or imprisoned.

If the mark is well known but unregistered, the owner can stop use of a similar or identical mark for similar or identical goods/services and require infringing articles to be handed over but cannot claim damages.

Applications are made in the member states and rights are enforceable against imports from outside the EU. Owners in an EU member state can, however, only stop imports of goods with the same mark from another member state if they were wrongfully marketed in the exporting state by the exporter or marketed without the owner's consent in the importing country and there must be no link between the two owners. The owner cannot stop marked goods sold in the EU from being resold, even if the marks in member states have different owners.

Alternatively you can register a Community Trade Mark (CTM) with the OHIM, in Alicante, Spain. The mark must be distinctive and the name must not mislead, or be contrary to EU public policy, or already be in use within the EU. Details are available on www.oami.europa.eu/mark.

Registration gives EU protection and the owner will be able to stop imitation or use of the mark for similar goods and services or exploitation of its commercial value, but infringement proceedings will be governed by national law. Rights are transferable and can be licensed. Registration is for 10 years, renewable for a further 10 years, but the owner must put the CTM to genuine use in the EU during the first five years.

The IPO and CTM Offices accept registrations with wide specifications for goods or services which can close out valid applications. Many registered marks are not in use for the full range of goods or services for which they are registered and some are not in use at all. It may therefore be worth subscribing to a private 'watching service' which monitors trademark publications worldwide and notifies subscribers when conflicting marks are published.

Owners of earlier marks are not precluded from applying at some point to have later registered marks declared invalid. You are therefore advised to seek advice from a trademark attorney before taking action.

Application for CTMs are made to OHIM, Alicante, Spain. Information is available on their website at www.uami.europa.eu/mark/. Owners of CTMs do not receive automatic notification but they can opt in to the notification system for a fee of £50, which covers notifications via up to two e-mail addresses for three years.

International trade marks registered with WIPO also give protection in the EU which administers international registration of marks under the Madrid Agreement Concerning the International Registration of Marks and the Madrid Protocol 1989 as amended. Anyone linked through nationality, domicile or establishment with a country party to one or both of the treaties may obtain an international registration through their country's trademark office having effect in some or all of the other countries of the Madrid Union. Registration is equivalent to registration in each country designated by the application and changes and renewals can be effected by a single procedural process.

CTMs and WIPO marks both give protection in the United Kingdom, even if the owner has no specific interest in the UK market. They are not examined in the same way as UK applications and are not blocked by earlier registrations unless formally opposed.

Certification trademarks

These show that the owner's goods have reached a certified standard. Certification requires compliance with standards and use approved by the BERR, details of which are obtainable from the Patent Office. Owners are usually trade or similar organisations and often manufacturers are authorised to apply the mark under the owner's supervision. The mark is not registered and ownership can only be transferred with the consent of the BERR.

Passing off

Passing off covers everything from dishonest trading to near infringement of trademarks, but actions are often concerned with business names because

registration of a name gives no right to exclusive use. Most actions involve applying a distinctive badge, sign, label or distinctive package or appearance to goods, thereby implying they are someone else's. The badge must be something used by another trader which deceives, misleads or confuses the customer. There must be a real likelihood of financial loss and it is irrelevant whether other traders or the general public are misled and whether the deception is a mistake, an accident or fraudulent. You are entitled to compensation and an order forbidding continuance of the deception, but full trials are rare because of the difficulty of proving deception.

Slander of goods

This is also called slander of title, trade libel and injurious falsehood, and consists of injury to someone's business by making a false and derogatory statement to a third party for an indirect or dishonest motive. The statement must be false and actual, or a genuine risk of financial loss must be proved.

Restrictive trade practices

Anti-competitive agreements between businesses, for instance cartels, are prohibited by UK and EC law and producers and suppliers of goods and services must register agreements where at least two parties restrict their conduct in one or more of the ways listed in the Competition Act (CA) 1998. The legislation is concerned with abuse of a dominant market position and unfair competition, particularly with terms relating to:

- prices and charges;
- terms and conditions of supply;
- quantities, descriptions and areas for the supply of goods and services;
- to and by whom goods and services are supplied;
- manufacturing processes.

For instance, it is unlawful – as being against the public interest – for manufacturers or suppliers exclusively to tie traders to one dealer for spares.

Patent, registered design and copyright licences are not registrable if the only restrictions concern the invention, the article for which the design is registered, or the copyright. But again, it must be registered if at least two parties accept restrictions.

Exchange of information agreements may be exempt if they relate to manufacturing processes. Trademark licences may be exempt if restrictions relate only to goods bearing the mark or to manufacturing processes. Once registered, agreements can only be modified through the Restrictive Trade Practices Court or the Director of Fair Trading. If they are not price-fixing agreements the Director can state they are 'non-notifiable' and will not refer them to the Restrictive Trade Practices Court. The Director also has a discretion to accept undertakings from monopoly traders involved in anti-competitive practices.

The system is to be replaced by a general prohibition on agreements and concerted practices which have or may have the object or effect of preventing, restricting or distorting competition. The wording is similar to provisions in EU law rendering such agreements illegal.

There is an unlimited fine and up to five years' imprisonment for anyone responsible for horizontal price fixing, limiting supply or production, market sharing and bid-rigging. Company directors and LLP designated members may also be disqualified from holding office for up to 15 years. 'Whistle-blowers' who cooperate in the investigation can obtain immunity from prosecution.

The Office of Fair Trading supplies information about registrable agreements and anti-competitive practices and further information may be available from your trade association.

This is, however, a complicated area, and if your contracts are likely to be affected, you should take legal advice.

Statutory references

Broadcasting Acts 1980 and 1996
Competition Acts 1980 and 1998
Computer Misuse Act 1990
Consumer Credit Act 1974
Copyright and Related Rights Regulations 2003
Copyright, Designs and Patents Act 1988

Copyright etc and Trademarks (Offences and Enforcement) Act 2002
Copyright (Visually Impaired Persons) Act 2002
Criminal Damage Act 1971
Data Protection Act 1988
Defamation Act 1952
Deregulation and Contracting Out Act 1994
Design Copyrights Act 1968
Enterprise Act 2002
European Communities Act 1972
European Patent Convention 2000
Fair Trading Act 1973
Legal Deposit Libraries Act 2003
Patent Cooperation Treaty 1970
Patents Acts 1977 and 2004
Patents (Amendment) Act 1978
Patents, Designs and Marks Act 1986
Registered Designs Act 1949
Trade Descriptions Acts 1968 and 1972
Trade Marks Act 1994
Video Recordings Acts 1984 and 1993

Main international copyright treaties

Berne Convention for the Protection of Literary and Artistic Works
Rome Convention (the International Convention for the Protection of Performers, Producers of Phonograms and Broadcasting Organisations)
Universal Copyright Convention
The World Intellectual Property Organisation Copyright Treaty and Performances and Phonograms Treaty cover copyright and related rights

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Debt collection and litigation

Delayed payment has a disastrous impact on cash flow and profits, especially if interest rates are high. Effective credit control backed up by efficient debt collection with a prompt resort to law can help.

Records

Your customer lists should record full names and addresses of the businesses and proprietors. Credit should be given personally to the proprietors of businesses using a trading name.

Terms and conditions of business

Terms and conditions, including interest on delayed payments, should be included in quotations, estimates, acknowledgements of orders, invoices and delivery notes. They can include a right to retain title to goods until payment, but the term should be professionally drawn. They should be legible and intelligible. If referred to court, you will have to show they have been understood, particularly if dealing with consumers. In dealing with businesses – but not consumers – a separate agreement confirming acceptance of your terms and conditions is useful.

If included in your terms and conditions, you can claim interest after the period and at the rate specified in the contract 30 days after the period has elapsed. You can also include a term entitling you to reasonable recovery costs.

The right to charge interest and recovery costs should be stated on all written communications, credit application forms, order confirmations, invoices and contracts.

If you have no interest provision in the contract you can claim (statutory) interest at 8 per cent above current bank base rate plus reasonable recovery costs from the moment goods are delivered or services are performed. There is no right to interest on advance payments, unless otherwise agreed. If the contract requires payment in full or by instalments before goods are delivered or services performed, statutory interest runs from the day following delivery or performance. The credit period ends on the last day of the month following the month in which the invoice is received if your payments are usually made at the end of the month following receipt of the invoice.

Debtors in default must be given notice that statutory interest is to be claimed plus recovery costs. It is best to give written notice, so that you have a record. It should state the amount owed, the total interest due and the rate at which it will continue to accrue and to whom, where and when it must be paid and whether by cheque, electronic transfer or other means.

'Small businesses' can turn to a 'representative body' – any organisation representing small business, eg your trade association – to object to grossly unfair contractual terms, which, for instance, remove the right to statutory interest.

The Better Payment Practice Campaign has details of the statutory interest provisions and an interest calculator at www.payontime.co.uk.

Internal procedures

Limits should be put on credit. Cheques should be backed by banker's cards and the number written on the back of the cheque by the payee. Most cards guarantee payment of £50 to £100 and the cheque must cover only one invoice up to the stated limit, otherwise the bank can refuse to honour the cheque. For a fee, your bank will expedite presentation of cheques to the payer's bank. Payment by credit card is a contract, with the card holder as the card company's agent – if the card company becomes insolvent, you cannot sue the card holder.

Weekly or monthly balances should be kept on running accounts, with a cut-off point for legal proceedings. Small amounts should be paid promptly on delivery, preferably by cash or cheque – even post-dated. Acceptance of part payment in 'full and final settlement' does not debar further demands or court proceedings for the balance unless the debtor has given fresh consideration – ie done something to his or her detriment not called for under your agreement – in return for your agreement to take no further action.

Your best cover is a personal guarantee from the debtor, and if the amount is substantial, a third party, but before allowing a substantial debt to accrue or suing a debtor, it is worthwhile carrying out checks through searches at:

- Companies House;
- The Land Charges and Land Registry;
- The High Court Registers of
  - Bills of Sale;
  - Bankruptcy Petitions and Orders;
  - Deeds and Arrangements;
  - The Register of County Court Judgments on www.registry-trust.org.uk;

  but registration is against an address, not an individual, so check the entries actually relate to your debtor.

When legal action is inevitable, letters of demand should be worded carefully, setting a time limit for payment. Before issuing proceedings, you should deliver a standard 'letter before (legal) action' on which you can take proceedings.

Settling disputes by arbitration

It may be worth considering arbitration. It can be flexible, fast, relatively cheap and specifically tailored to fit the dispute if heard by a specialist in the trade. Many trade organisations offer schemes, although some are thought to be biased in favour of their members.

Consumers have the right to refer instead to the court but legal advisers in civil proceedings are now required to explain ADR procedures to clients, including mediation, and to inform the Court that they have done so.

Other forms of ADR include:

- mediation, where a neutral trained mediator, who may be a lawyer, supervises without prejudice meetings leading to a legally binding agreement;
- conciliation – here the conciliator intervenes, suggesting possible solutions;
- med-arb, when mediation fails and the dispute is referred to arbitration, often before the mediator;
- arbitration conducted by an agreed independent third party, a lawyer or appropriate expert, whose 'award'(decision) is legally binding and enforceable through the courts.

It is also worth considering early neutral evaluation conducted by a professional, usually a lawyer, who hears a summary of the case and gives a non-binding decision on the merits; or neutral fact-finding, which is more suitable for technical disputes when an agreed neutral expert looks at the facts and gives an evaluation on the merits.

Information about the various procedures is obtainable on the Department of Constitutional Affairs' (DCA) websites, www.dca.gov.uk/civil/adr/index.htm and www.justice.gov.uk.

Civil litigation

Litigation is a last resort, to be taken only if you expect to obtain payment and/or compensation. Commercial litigation is dealt with by the civil courts – the High Court and the County Court. The courts have similar procedure and debt collection is relatively straightforward. Experienced legal practitioners are best equipped to deal with the finer points of High Court pleading and advocacy, and whatever the claim, you may face expensive opposition.

Civil legal aid dealing with commercial disputes is now only available to individuals with very low capital living on state benefits. Companies are not eligible for legal aid.

Litigation is expensive. Leading firms charge hourly rates of £750-plus, but unless you have a specialist and substantial claim, you are unlikely to need the constant attention of the most senior partner or a QC. However, even in a fairly straightforward County Court claim, the bill can be several thousand pounds and, win or lose, you pay for work done before litigation.

The Gaming Act forbids some types of betting, but solicitors can now gamble on litigation and you may be able to proceed through conditional

fee agreement. Your lawyers are entitled to a percentage of any winnings and insurance is available, but ensure all the terms of the contingency fee agreement are clearly spelt out. Alternatively, you may be able to obtain insurance cover for the litigation. Your solicitor will be able to give you details.

Your solicitor needs the facts, the documents (including a statement of account), relevant correspondence and details of a possible defence. If you are continuously referring debts to your solicitor, it is worth agreeing a standard referral procedure, with periodic summaries and settlement.

You can, however, litigate in person in any court and the small claims fast-track procedure in the County Court is specifically designed with this in mind. The emphasis here is therefore on suing in the County Court. If facts are in dispute or the claim is substantial, your best course is to instruct a solicitor.

Criminal proceedings

Crime is the business of the Magistrates' and Crown Courts and the police or responsible authority. It is no crime if debts are not paid or you carry on business at a loss unless fraud is involved. But you can be prosecuted under health and safety consumer protection, licensing, and road traffic legislation.

If you are prosecuted, whatever the circumstances, you need legal advice. Legal Aid is available but the decision to grant is for the court. The decision is based on a means test, whether the court would impose a custodial sentence and whether a conviction would lead to loss of livelihood or serious damage to reputation. Conviction can have serious repercussions in civil proceedings for compensation – conviction for a minor traffic offence linked to injury or property damage is automatically admissible, and negligence thereby proved in civil proceedings.

A prosecution in the Magistrates' Court is based on information stating that someone has, or is suspected of having, committed an offence. A summons or warrant to arrest is issued requiring the accused to appear in court. Warrants can only be obtained in specific circumstances, including for offences punishable with imprisonment and/or triable by jury.

More serious offences are heard in the Crown Court before a jury. The Crown Court also hears appeals from some civil decisions made in the Magistrates' Courts, eg decisions concerning licensing and recovery of unpaid income tax and NICs.

In police and in private prosecutions, an innocent party's costs may be paid if the accused is clearly innocent. But, as in any other litigation (unless there is full legal aid), innocent defendants pay part of the costs.

Civil actions

The High Court and the County Court deal with contractual, property and partnership disputes, business tenancies and tort claims. Contractual claims cover disputes about written or unwritten agreements. Claims in tort include claims in negligence, eg for compensation for injury or property damage caused in an accident. Straightforward cases are usually dealt with in the County Court. The High Court deals with more challenging cases and claims involving more substantial damages, professional negligence, fatal accidents, allegations of fraud or undue influence, defamation, malicious prosecution or false imprisonment and claims against the police.

County Courts are listed in the telephone directory and contact details and information about procedure is available on www.hmcourts-service.gov.uk. The County Court office will help you deal with forms and issue proceedings. District judges are used in cases involving up to £5,000. More important or complex cases and cases involving more than £5,000 are heard by a circuit or High Court judge.

Court fees are additional to your legal costs. You pay £15 to start an action claiming up to £300, increasing to a maximum of £1,530 for unlimited claims and claims for more than £300,000. Debt proceedings for up to £99,999.99 can be issued online on www.moneyclaim.gov.uk. Fees start at £20 and payments are made by debit or credit card.

A defendant putting in a counterclaim – a claim exceeding yours – pays the same fee and on the same basis as the claimant.

There is a fee of up to £1,000 for setting the case down for trial. You pay £40 when you apply for judgment if the claim is defended.

The judge is the case manager and management includes pre-action protocols. These aim to encourage cooperation between the parties at an early stage in an effort to narrow the issues and, if possible, to avoid taking the case to trial.

The court is required to encourage and facilitate the use of alternative dispute resolution and can stay proceedings to allow for this either at the parties' request or when it considers this appropriate.

Cases are allocated to one of three tracks, depending on the complexity and amount involved, and the judge must:

- encourage the parties to cooperate;
- identify the issues at an early stage;
- dispose of summary issues that do not require full investigation;
- help the parties to settle all or part of the case;
- fix timetables for the hearing and control the progress of the case;
- consider whether the benefit of a particular method of hearing justifies its cost.

Parties refusing to comply may have their case struck out or face sanctions, including costs sanctions.

The categories are:

- *Small claim track* for cases involving up to £5,000 in England and Wales and cases involving over £5,000 with the parties consent, claims for personal injury where damages claimed do not exceed £1,000 and some claims by residential tenants. There are different financial limits in Scotland and Northern Ireland. A date is fixed for a preliminary or final hearing and directions for case management ensure the trial proceeds quickly and efficiently. Procedure is aimed at keeping costs to a minimum by dispensing with formalities and is designed for the litigant in person in the cases of debt claims, consumer disputes, accident claims, disputes about ownership of goods and some landlord and tenant disputes. Trial fees range from £25 to £300.
- *Fast track* for cases involving over £5,000 and less than £15,000. There is a £500 trial fee, standard directions for trial preparation and a maximum of one day (five hours) for trial with, usually, no oral expert evidence and costs are fixed. Claims exceeding £15,000 are also allocated to fast track if the trial is likely to last for only one day and there is only one expert on each side in two areas of expertise.
- *Multi track* for more complex cases and those involving over £15,000. There is a £1,000 trial fee, no standard procedure and a range of case management provisions, including standard directions, conferences and pre-trial reviews.

You must usually sue in the court closest to where the defendant lives or carries on business, or where the incident on which the claim is based occurred.

On a contract, you sue where the contract was concluded. If you choose the wrong court, the case is transferred at extra cost.

Time limits are basic. The court serves the proceedings on the defendant. If there is no response, you can ask for bailiff service or serve proceedings yourself. You must file the other documents in the proceedings with the court and serve them on the defendant yourself. You must therefore ask for acknowledgement of service (receipt) of documents that are 'served' the day following postage to the appropriate address by first-class post.

The claimant starts the action and the person sued is the defendant. It is not usually difficult to identify your opponent unless there are several possibilities, eg in a road accident claim you may want to sue the driver, car owner and/or the driver's employer. Multiple defendants pay in proportion to their liability.

Proceedings must be filed with the court and served on (ie delivered to) the defendant or his or her solicitor.

Service on a limited company is to the registered office or on senior management. Companies cannot litigate 'in person', but you can apply for an order permitting a director or officer to appear for the company. The Articles may require the consent of the board or the shareholders before proceedings brought by a company can be continued.

If partners or the partnership are sued, service is on the partner or person controlling or managing the partnership's principal place of business.

Someone using a trade name is served by naming them or the business premises and serving proceedings at the principal business premises. Individuals are served at their usual or last known address.

The names of directors and of up to 20 partners are on business documents and filed at Companies House. Partners must disclose their names and addresses to the court, whether sued personally or in the partnership name, and can be served personally or at the principal place of business.

The first step is to complete a claim form with the names and addresses of the parties, concise details of the claim and why you are taking action, and a statement of value together with a statement of truth as to its contents. If you need to set out the facts at length, they must be contained in a separate document – the particulars of claim. If sent separately, it must be filed with the Court Office within 14 days of serving the claim form on the defendant, together with its own statement of truth.

The County Court is not strict about form and in a straightforward claim for debt, 'I claim £X the price of goods sold and delivered to Y on…', is sufficient, but usually pleadings refer to claimant *and* defendant: 'the

claimant claims £X'. Other claims require more details, eg road accident particulars must list the date, place and circumstances of the accident, say why the defendant was responsible and whether, as a result, you suffered pain, injury, loss or damage. If suing a driver's employer because the driver was working at the time of the accident, you must state that the driver was 'acting in the course of his/her employment'. Expenses and loss of earnings must also be listed; 'The claimant claims damages limited to £X' covers only general compensation assessed by the court. Interest may be awarded if included in the particulars.

A payment in or offer to settle made in writing 'and without prejudice except as to costs' by either party may dispose of the claim. An offer can be made at any time but payment in cannot be made before proceedings have issued. Thereafter, offer or payment in can be made any time before judgment, but, if not accepted, it must not be disclosed to the judge until after judgment but before costs are dealt with. If judgment exceeds the payment, the defendant pays the claimant's costs, but if he or she guessed right or judgment is for less, the defendant pays costs to the date of payment and the claimant pays both sides' costs thereafter.

You can apply for summary judgment even if the defendant has filed an acknowledgement of service or a defence. You must file written evidence with the court to support your claim, together with a statement of truth, file it with the court and serve it on the defendant. If no defence is served, you may have to wait until the hearing before you find out whether the defendant admits, defends and/or counterclaims, or whether there is a 'set-off' – eg for storage charges. If there is an arguable defence, the debtor may be permitted to defend on conditions – eg that all or part of the amount is paid into court pending trial. If there is a good defence, no conditions are imposed. If, however, the defendant admits the debt or you obtain judgment, the debt is entered on the Register of County Court Judgments and cancelled if paid within a month. Otherwise it stays on for six years and, when the court is notified of payment, it is noted against the entry.

The defendant may, however, make an offer to pay by instalments. If you reject instalment payments of a debt of less than £50,000, a court officer can decide without a hearing whether or not it should be accepted, taking into account the defendant's statement of means, other relevant information and your objections. If the officer does not make a decision, a judge will do so, with or without a hearing, and either party can apply to have the decision re-determined by a judge.

Judgment may be obtained without the defendant receiving notice of proceedings. The defendant must then immediately ask the court for details, producing the order for judgment. It is set aside if proceedings have not been properly served. Otherwise, it is set aside only if there is a reasonable defence and explanation for non-response and the defendant may have to pay costs to the date of judgment.

If you do not apply for summary judgment, the defence to a disputed claim must be filed with a statement of truth within 14 days. This can be extended to 28 days if the defendant instead files an acknowledgement of service within 14 days and files the defence 14 days thereafter.

Lists of relevant documents and other evidence are then exchanged and made available for inspection, including statements reports, photographs and sketch plans, unless otherwise ordered. 'Without prejudice' oral and written offers of settlement are excluded unless you choose to put them in evidence.

Agreement saves costs. For instance, you may be able to agree the cost of repairs instead of bringing witnesses to trial, leaving only liability for the trial.

The parties can ask for orders permitting them to act, or directing their opponent to do (or stop doing) something, pending the hearing. These applications are interlocutory and are made *inter partes* – on notice to the other side or, if urgent, *ex parte* – without notice –- at a cost of upto £75. Usually they must be served and filed, and the court office will tell you about time limits and restrictions. Some interlocutory orders, eg an injunction to stop someone trading, can be expensive because the court may require an undertaking to pay damages accruing until the hearing.

If costs are not agreed between the parties, the court will make 'detailed assessment' of costs at the end of the case. The court can, however, assess them on a summary basis at any stage and ask for estimates of accrued and future costs, and may order a payment on account of costs pending detailed assessment.

Costs are payable within 14 days of judgment unless the court orders otherwise and assessment is on a standard or indemnity basis.

Standard costs are those proportionate to the claim and reasonably incurred in the circumstances. Proportionality is not a factor in awarding costs on an indemnity basis. Whether standard or indemnity, the court takes into account the parties' conduct, the amount of money or property involved, its importance to the parties, the complexity of the case and the time, skill and specialised knowledge of those involved.

You may be able to appeal against a decision you think is wrong. The court office will inform you of time limits and explain procedures, but before appealing you should take legal advice.

Collecting debts after County Court litigation

When judgment is obtained, you can enlist the court's help in enforcing it at a cost of up to £95. County Court enforcement is confined to issue of:

- warrants;
- third party debt orders;
- charging orders;
- attachment of earnings orders;
- orders directing the transfer, delivery or recovery of possession of money or property.

Other enforcement proceedings must be taken in the High Court. This is often more successful because the County Court Bailiff's powers are more restricted than the High Court Sheriff's.

Unless stated to the contrary, stay of execution (delaying enforcement) is automatic for 14 days after money judgment is entered. An order to wind up a company stops execution on judgments against it.

A money judgment debtor can be ordered to attend court for examination as to property and means.

Warrants of execution are enforceable against goods. If located in several areas, concurrent warrants can issue in several courts. Costs are usually allowed and you should tell the court if you reach agreement with the debtor or withdraw from possession so the warrant can be suspended. If reissued, your priority is from the date of reissue.

Warrants are to enforce judgments or orders for recovery, or delivery of possession of land, and can issue 14 days after judgment or the day after a defendant is ordered to vacate. The court can suspend orders of possession for arrears of rent or under a mortgage and the warrant is cancelled on payment of arrears plus costs.

Delivery of goods is enforced by warrant of delivery or attachment. On assessed value, you can execute for the value, or judgment may permit

retaining goods pending payment. Injunctions and orders are enforced by warrant of attachment.

A judgment debtor may be committed to prison if he or she has persistently and wilfully disobeyed an order. On a money judgment, you must show the debtor had means to pay since judgment.

Charging orders on a debtor's land are made to enforce money judgments. The charge is registrable at the Land Registry or under the Land Charges Act, but not under the Companies Act. Charging orders on company shares and debentures are made on judgments for fixed amounts and can include dividends and interest. You can also obtain a 'stop notice' or injunction, which effectively invalidates dealings.

Attachment of earnings orders are available against anyone in employment, whatever the amount of the debt. You must identify the employer. The debtor must give details of the employment and current and future earnings, resources and needs, and the employer may have to file a statement of the debtor's earnings. The order directs the employer to make deductions from pay and pay them to the court, which must be notified if the employment ends.

Any unconditional debt, even if not immediately payable, can be garnished if it accrues solely to the debtor. Current bank accounts can be attached and (on conditions) deposit accounts, but you may lose priority to a third party if attachment is not completed by payment before a petition for bankruptcy or winding up is lodged.

A third party debt order stops defendants taking money out of their bank or building society account. The money is paid from their account. The order can also be sent to anyone who owes the defendant money.

If you cannot use any other method, the court may agree to appoint a receiver. The order covers the sale proceeds of land or a share of rents and property held jointly or subject to a *lien* or trust. It can include an injunction ancillary or incidental to appointment if the debtor might dispose of the property. The receiver may have to give undertakings to the court or you may be made personally liable for his or her actions. The order does not make you a secured creditor, so it should be registered as a charge or caution if made against land.

Judgment is enforceable against the partnership's and the partners' property and against partners who were served in the proceedings or admitted in the proceedings that they were partners. Charging orders against a partner charge his or her interest in the partnership property, plus the partner's share of profits.

By the same or a later order, a receiver can be appointed over other money due to the partner from the partnership and the court can make other orders and directions. The partner or his or her partners can redeem or purchase the charge if a sale is ordered.

The leave of the court is necessary before the partnership or a partner can enforce judgment against another partner.

Enforcement against a company is against the directors or other officers, but leave of the court is required before issue.

Non-compliance with a judgment or order is a ground for bankruptcy or winding up. But service of a statutory demand – which must be for at least £750 – often leads to payment of the amount due without recourse to litigation.

Statutory references

Arbitration Acts 1950, 1975, 1979 and 1996
Attachment of Earnings Act 1971
Civil Procedure Act 1997
Companies Acts 1985 and 1989
Consumer Credit Act 1974
County Courts Act 1984
Courts and Legal Services Act 1990
Criminal Justice Act 1982
Fair Trading Act 1973
Hire Purchase Act 1965
Insolvency Act 1986
Late Payment of Debts (Interest) Act 1998
Law Reform (Miscellaneous Provisions) Act 1934
Partnership Act 1890
Powers of the Criminal Court Act 1973
Supreme Court Act 1981

13

Bankruptcy and liquidation

Profit patterns fluctuate and projections are not always accurate. Before embarking on the sea of private enterprise, you should have some idea as to what happens if you run aground.

Insolvency

Insolvency is defined as:

- when debts and liabilities – including contingent and prospective – exceed assets;
- failure to pay a judgment debt (resulting from successful legal proceedings);
- failure to pay, compound or secure an undisputed debt of at least £750, within three weeks of formal demand, or if there is a serious possibility assets will be dissipated, forthwith;
- approval of a voluntary arrangement;
- the making of an administrative order;
- the appointment of an administrative receiver.

Contracts imposing unfair or oppressive rates of interest may be set aside by the court and onerous (oppressive) contracts for leaseholds can be disclaimed. If not registered under the Bills of Sale or Companies Act, general assignments of book debts are void, unless paid before presentation of a petition, the debts are due under specified contracts or were part of a transfer made in good faith and for value, or the transfer benefited the creditors.

Employees not given the proper period of notice of dismissal may be entitled to compensation from the BERR consisting of the following, at a maximum of £330 per week:

- up to 12 weeks' pay;
- up to 8 weeks' arrears of pay; and
- up to 6 weeks' holiday pay.

Only professionally qualified licensed insolvency practitioners who are members of the following professional bodies may act in LLP and company bankruptcies and liquidations:

- the Chartered Association of Certified Accountants;
- the Insolvency Practitioners' Association;
- the Institute of Chartered Accountants in England and Wales;
- the Institute of Chartered Accountants in Ireland;
- the Institute of Chartered Accountants in Scotland;
- the Law Society;
- the Law Society of Scotland; or
- the Secretary of State for Business, Enterprise and Regulatory Reform.

The liquidator, administrative receiver, administrator or official receiver has a duty to send a report to the Secretary of State on the conduct of members or directors who were in office in the last three years of trading and the Secretary of State has to decide whether it is in the public interest to seek a disqualification order against them.

Voidable transactions, preferences and transactions at an undervalue

Sole traders and partnerships

Transactions putting creditors, sureties or guarantors into a better position than other creditors can be set aside as 'preferences', including transactions:

- at an undervalue (ie gifts or transfers made for significantly less than market value or in consideration of marriage) – at risk if made less than five years before presentation of a petition for bankruptcy or an administrative order, *and* if intended to put assets beyond the reach or prejudice the interests of actual or potential creditors;
- at a proper price – at risk for six months but two years if made with an 'associate'.

LLPs and companies

Voidable periods vary, dating back from presentation of a petition for an administration order, the date the order is made, or the commencement of winding up or liquidation, but:

- Transactions at an undervalue are safe if made in good faith, for business purposes and for the LLP's or company's benefit, but are voidable in a company liquidation if with a 'connected person' (see page 24).
- Preferences made when the LLP or company was insolvent or that cause insolvency are at risk for six months to two years.
- Floating charges are at risk for one or two years.

Trading with an intent to defraud creditors – which may include paying cheques into the LLP's or company's account after it stops trading – imposes unlimited liability on the designated partners or directors. In insolvent winding up or liquidation, designated partners or directors, *de facto* and shadow directors may be criminally liable and subject to disqualification for wrongful trading. The only defence is that every step was taken to minimise loss.

The voluntary procedures

Insolvent individuals and undischarged bankrupts who have not applied for 12 months, their trustee or the official receiver (a member of staff of the BERR) can make arrangements with creditors through the court. Partnerships, LLPs and companies can also agree arrangements and compromises with creditors and apply for administration orders so business can be reorganised and insolvency avoided. There is an additional voluntary arrangement for LLPs and small companies, allowing them to seek a moratorium (a temporary bar on creditors' claims) to give management time to put together a rescue scheme for the creditors' consideration. Until formal approval or rejection no legal action can be taken against business assets, but agreements in satisfaction of debts or approved schemes of arrangement are legally binding. Details of the procedure are on www.insolvency.gov.uk.

With partnerships, these voluntary arrangements can be used even if an insolvency order is made against the partnership or a partner but there must be interlocking arrangements if the partnership and the partners both want to agree arrangements.

Partners, the LLP, directors, liquidators or administrators put proposals and a statement of (financial) affairs to creditors – and in a company, shareholders – nominating a supervisor. There may be creditors' meetings, secured and preferred creditors are protected as in bankruptcy and liquidation, and on application the court can stay (stop) the proceedings. Disadvantages are that:

- creditors cannot recover VAT bad debt relief;
- until the order is made partners and directors remain at risk.

Administration orders are mainly used if there are no standard fixed and floating charges and the court must be satisfied that:

- the business is, or is likely to become, unable to pay its debts; or
- all or part of the business would survive as a going concern; or
- creditors are likely to agree a satisfactory arrangement; or
- realising the assets is likely to be more advantageous than a winding up.

The administration order can be used in conjunction with other voluntary arrangements but not in a liquidation.

The partnership and/or the partners, and/or the directors and/or the company, and/or creditors, or if the business is already being wound up the liquidator, can petition. Secured creditors and debenture holders must be notified and the petition can only be withdrawn with leave of the court.

The administrator takes over management but cannot prevent an application for dissolution or appointment of an administrative receiver (under a company's floating charge). Partners' and directors' powers are restricted, creditors' and shareholders' meetings may be called and a more detailed statement of affairs must be prepared, confirmed on affidavit by current and former partners or directors and in some cases those involved in the company's formation, and employees. The Registrar must be notified and details of the appointment must appear on business documents and in the *Gazette* and in a newspaper that will bring it to the notice of creditors. Creditors and shareholders can apply to court if the business is, was, or will be, managed so they are unfairly prejudiced and the court can regulate the administration.

Administration ends on application to the court either because the purposes specified in the order cannot be carried out or because they have been completed.

Sole trader

Sole traders are personally liable for business debts and obligations. Personal assets, stock in trade and business assets can be sold. All you can keep are tools, books, vehicles and other equipment necessary for personal use in your business or employment and clothing, bedding, furniture and necessary provision for you and your family. But the trustee in bankruptcy can claim items he or she thinks will sell at more than replacement cost and you may have to pay over part of your earnings until discharge. The trustee, in whom some rights of (legal) action are vested, must be informed of increases in pay and estate (assets) but you can keep property held on trust for others and property payable under third party insurances.

Petitions in bankruptcy, bankruptcy orders and arrangements with creditors are registrable against real property and may bind a purchaser with unregistered title. They can be registered against registered property which stops dealings except through the official receiver or trustee.

Bankruptcy

The petition is presented by the debtor, creditor, supervisor, person acting in, or bound by, a voluntary arrangement, the official receiver, the Director of Public Prosecutions or person named in a Criminal Bankruptcy Order. Issue protects the debtor and his or her estate from legal proceedings and some legal processes. On a debtor's petition, the court may consider summary administration (for 'small' bankruptcies) and whether there should be a report.

An interim receiver or special manager takes over the debtor's estate pending appointment of a trustee, protecting assets and disposing of those liable to diminish in value. He or she continues to act in summary administration and criminal bankruptcy.

The debtor is then an undischarged bankrupt, deprived of ownership of most of his or her assets. He or she must cooperate with the receiver and hand over books and records. Except on the debtor's petition, a statement of affairs must be provided and there may be public examination in court and creditors' meetings.

Assets available include property acquired before and after the order, assets in voidable transactions and part of current income, but the right of occupation of a solvent spouse and dependants is protected. Debts and interest must be proved. Secured creditors can realise or value the security and prove for the balance or surrender it and prove for the full amount. The trustee may continue the business and make periodic payments (dividends).

It is an offence for a bankrupt:

- not to have kept proper accounts for two years prior to the order;
- to have materially contributed to his or her financial problems by gambling;
- to take assets outside the jurisdiction;
- to make a false statement of affairs;
- to enter into a transaction intending to defraud creditors;
- to go into business in a name other than that stated in the order;
- to act as a director or be involved in company management – anyone acting on the bankrupt's instructions in relation to a company also commits an offence.

And the bankruptcy must be disclosed when applying for credit and accepting payment in advance.

The order of distribution is:

- liquidation costs;
- preferential debts proportionately, ie 12 months' PAYE and NICs, contributions relating to subcontractors in the construction industry, six months' VAT, betting duty, pension scheme contributions, 12 weeks' wage arrears if no notice given, otherwise six weeks, to a maximum of £205, and payments under the employment legislation;
- secured creditors;
- unsecured creditors plus interest until distribution;
- provable debts plus interest due to the bankrupt's spouse.

Bankruptcy dates from the order and lasts until discharge but may be annulled if debts are paid off or secured. Discharge is automatic after three years for the first-time bankrupt, two years in summary administration. Otherwise it can be deferred for up to 15 years. The bankrupt can then go into business and, with some exceptions, is no longer liable for provable debts.

It is proposed that the period of disqualification be extended to 15 years if there was fraud or recklessness, and that if fraudsters seek a loan of more than £250 they will be required to tell the lender they are bankrupt, as well as their business contacts if they go into business under a new name.

Partnerships

Partners have complete financial commitment but commitment to co-partners ends by mutual agreement, dissolution, death or bankruptcy.

Dissolution by agreement is seldom straightforward and the agreement should set out terms applying to dissolution.

The partnership ends if business becomes illegal and unless the agreement states otherwise:

- on completion of the undertaking or end of the period for which it was formed;
- on a partner's bankruptcy, death, or resignation;
- if a partner's share is charged by the court for personal debt – but the other partners can buy it and continue in business.

You can rescind (cancel) the agreement if there is fraud by a potential partner. You are entitled to damages for deceit, a lien (right of retention for the price) on surplus assets equal to your capital contribution, plus interest and costs, an indemnity against partnership debts and repayment of anything paid towards liabilities, plus interest.

Payment for a retiring or deceased partner's share substitutes the agreement to pay for the final account and distribution of assets but you should agree a formal settlement. (An option to purchase limits liability by the terms of the option.) Executors of deceased partners should ask the court to appoint a manager or receiver.

If losses are due to a partner, you can apply to the court – or, with an arbitration clause, the arbitrator – for dissolution on the ground that it is 'just and equitable'.

The court appoints a receiver or receiver and manager who is usually required to take the 'usual accounts and enquiries' and complete the dissolution. Receivers take in income and pay outgoings. Managers continue the business, so receivers are usually appointed if the business is to be wound up.

Partners' responsibilities continue until winding up is concluded but only solvent or surviving partners are committed. When surviving partners of a deceased partner mortgage land, the deceased partner's estate may lose priority and the personal representatives should join in conveyances of land bought before 1926. If a partner is bankrupt, his trustee should be a party.

On dissolution, one partner sues in the partnership's name and distributes the assets. Goodwill must be sold unless otherwise agreed or it is personal and stays with the partners. If sold, they cannot solicit new business with existing connections. Except with a fixed-term partnership terminated by death, repayment of premiums can be ordered and when the assets are sold and the partnership dissolved a general account is made up in accordance with the partnership's usual practice.

Payments go first to preferential then secured creditors and then to pay other debts and liabilities. If there are insufficient partnership assets to pay off creditors, the shortfall ranks with the ordinary debts of the individual partners. Partners' advances come next, then winding up costs and initial capital contributions. If costs are not covered, they are paid proportionately by the partners. Losses, unless otherwise agreed, including capital losses, come from profits, then capital and then from the partners in accordance with their entitlement to share profits.

Insolvency

The law applying to sole traders applies with modifications to partners and partnerships but *not* to LLPs.

A petition served on a partner is served on the partnership, which can be wound up without involving their insolvency, but the adjudication order is made against the partners, not the partnership.

The partners (but not a limited partner), creditors or person acting in a voluntary arrangement can petition and the business is wound up as an unregistered company.

Partners, former partners and anyone who has or has had control or management is a director or officer under the insolvency and company directors' disqualification legislation with the liability of directors and management of a limited company.

If one or more partners as well as the partnership is insolvent there are two claims: first, between the partnership's and the partners' creditors if all partners are bankrupt; second, between a bankrupt partner's creditors and solvent co-partners.

If all the partners are bankrupt, creditors can claim against partnership assets and any unpaid balance comes from the partners' estates. Preferred creditors then rank with unsecured creditors but regain priority if payment is made into the joint estate from a partner's estate. Secured creditors can claim against the partnership or a partner without valuing the security. There are the following variations:

- If there are no partnership assets creditors can claim equally from each partner.
- Partners and the partnership are liable for their own fraudulent acts.
- Debts owed by the partnership and the partners can be claimed against the partnership and the partners.
- Creditors who put a partner into bankruptcy can usually also claim as partnership creditors.
- The trustees in bankruptcy of partners in business on their own account can claim against the partnership.
- Partnership creditors have priority over creditors of an insolvent corporate partner; the claims rank *pari passu* (proportionately) between themselves.

LLPs and companies

Receivership is when assets secured by a floating charge are realised and paid to the holder. Secured creditors can enforce the security without a winding up and without regard to anyone else's interests.

A company's outside investors' tax reliefs under the Enterprise Investment Scheme (EIS), Venture Capital Trust (VCT) or Corporate Venturing Scheme (CVS) are not put at risk if, except for the actions of the receiver, the company still qualifies under the schemes.

Administrative receivers are appointed by debenture-holders or the court in accordance with the debenture. Their powers are similar to those administrators. Floating charges usually include a charge over plant and machinery which may also be covered by a fixed charge. If the company is in default before a winding-up resolution, the charge becomes fixed, giving the lender priority over all the creditors. Notice of the appointment must be given to the company and creditors, and appear on company documents, in the *Gazette* and in a newspaper which will bring it to the creditors' notice. The administrative receiver prepares the fuller statement of affairs required in administration and reports to the Registrar and – unless he or she reports within three months – to secured creditors and their trustees and, if appointed, the liquidator. The appointment ends by court order or resignation.

Receivers are appointed under a fixed charge or by the court. They report to directors, shadow directors and the Registrar. If an administrator is appointed the security cannot be enforced without consent of the court or administrator but the fixed chargeholders retain priority if the security is sold. The appointment ends when the receiver has sufficient to pay his or her expenses and discharge the debt.

Voluntary liquidation

A member's (partner's or shareholders') voluntary liquidation is where a majority of the designated partners or directors produce a satisfactory declaration of solvency, setting out assets and liabilities and stating debts will be paid within 12 months. The partners or shareholders appoint a liquidator and the declaration is filed with the Registrar. If debts are not paid, the directors may be liable to a fine or imprisonment. Pending appointment of a liquidator, the directors cannot, without the consent of the court, do anything except what is necessary to protect company assets. Although the liquidator is

not appointed or supervised by creditors, most of his or her powers can only be exercised with the consent of the court until the creditors' meeting.

If there is no declaration, the liquidator disagrees with it or the debts are not paid, it becomes a creditors' voluntary liquidation. Creditors and company shareholders nominate liquidators but the creditors' choice takes precedence. A creditors' committee, which includes shareholders' representatives, may also be appointed to supervise the liquidator. Partners, directors, shareholders and creditors can nominate a joint or alternate liquidator through the court.

The liquidator realises the assets and distributes the proceeds but may need the consent of the court or the creditors' committee.

Outside investors' tax reliefs under the EIS or VCT Schemes are not put at risk in a liquidation.

Liquidation starts with the date of the winding up resolution and lasts until the liquidator vacates office after his or her final report to the partners or shareholders and the creditors, but he or she can resign on notice to the Registrar of the final meeting.

All debts, present, future, certain and contingent are provable, including quantified claims for damages, unless the LLP or company is insolvent. The first payment is under fixed charges, then liquidation expenses, preferential debts, floating charges and arrears of dividends, with remaining assets going equally to unsecured creditors.

Unquantified claims in tort – eg claims in damages for negligence – are provable debts in liquidation or administration proceedings if there is evidence of the claim at the date the business went into liquidation or entered administration.

The partners in an LLP are liable to contribute to an insolvent LLP's assets for at least five years or until the LLP is wound up. Their liability is limited to their investment, unless they accepted increased liability by agreement, but loans and guarantees to the LLP are treated by the Revenue as capital contributions. Undrawn profits are usually considered the LLP's debt and are not added to prescribed capital and a capital contribution to meet personal liability for negligence is taken into account for the purposes of tax relief. Shareholders, however, are only liable for the unpaid balance on their shares.

A private company's liquidator can be authorised by the shareholders to distribute all or part of the company's assets between them *in specie* – without converting them into cash. The liquidator can value and decide how to divide them or vest all or part in trust for the shareholders' benefit. They are not

compelled to accept assets burdened with debt or other liabilities. And the directors, shadow directors, and their 'connections' can acquire substantial non-cash company assets – property or non-cash interests in property worth over £2,000 exceeding 10 per cent of the company's net assets, or worth over £100,000 – without seeking the shareholders' approval if the company is in administration or being wound up, unless it is a shareholders' voluntary winding up.

LLPs and companies are dissolved three months from registration by the Registrar of the liquidator's final account and return.

Compulsory winding up

The LLP or a partner or partners can petition for compulsory winding up. In a company the company or contributories (ie shareholders who have held shares since incorporation or for 6 of the 18 months before liquidation) can lodge the petition. In both LLPs and companies the petition can also be lodged by creditors, the Secretary of State for Business, Enterprise and Regulatory Reform, the Financial Services Authority or the official receiver.

The court orders compulsory liquidation if:

- the LLP or company has not started trading within a year of incorporation or has stopped trading for 12 months;
- the LLP or company is insolvent;
- the Secretary of State for Business Enterprise and Regulatory Reform requests it.

And in a company if:

- a special resolution requests it;
- it is 'just and equitable' to do so;
- a director or seller of shares to the company for capital requests it on the ground that it cannot pay its debts;
- there is mismanagement or deadlock on the board, though this applies only if the court is satisfied that voluntary liquidation is not in the interest of creditors or shareholders.

On making the order the designated partners' or directors' powers cease and the official receiver or provisional liquidator is appointed pending appointment of the liquidator. Details must appear on company documents, be notified to the Registrar and be advertised in the *Gazette* and two local newspapers.

Liquidation starts from presentation of the petition unless there was a voluntary liquidation, when it dates from the date of the resolution. A full statement of affairs may be required and no proceedings can be taken by or against the company without the consent of the court. There may be creditors' and shareholders' meetings. Appointment of the liquidator is as in a creditors' winding up but the official receiver can apply for appointment and creditors and contributories may appoint a liquidation committee. The liquidator realises and distributes the assets and must keep the official receiver informed. The official receiver may report to the court and apply for public examination of anyone involved in the company's affairs. The court can also order examination of company officers.

Penalties

Sole traders and partners can now be convicted for fraudulent trading. Anyone involved in trading with an intent to defraud, incurring debts without a reasonable prospect of repayment, or convicted for an indictable offence (serious and triable by jury) relating to the LLP or company or their assets may be prosecuted and disqualified from participating directly or indirectly in the management of an LLP or company for up to 15 years. Gross incompetence and 'commercial immorality' (including failure to carry out statutory duties) also brings disqualification. Offenders may also be fined up to £5,000 and/or face up to seven years' imprisonment.

If the company bought shares within a year of the winding up and cannot meet debts and liabilities, management may share liability for loss with the holder of the shares.

A member of an LLP who is disqualified cannot be a company director, nor can a disqualified director be a member of an LLP. Directors and shadow directors cannot, without court consent within 12 months of insolvent liquidation act for, or be involved in the promotion, formation or management of, or be connected with, a company with the same name, or use a former name or trading name used during the previous 12 months, or one which suggests continuing association for five years.

Distribution is as in a voluntary liquidation except charges over distrained goods are paid after floating charges.

The official receiver can apply for early dissolution if expenses will not be paid. Otherwise the liquidator reports to creditors and the LLP or company is dissolved three months after dissolution is registered.

Statutory references

Attachment of Earnings Act 1971
Bills of Sale Act 1878
Companies Acts 1985 and 1989
Company Directors Disqualification Act 1986
Consumer Credit Acts 1979 and 2006
Employment Protection (Consolidation) Act 1978
Fraud Act 2006
Insolvency Act 1986
Insolvency Act (No. 2)1994
Land Charges Act 1972
Land Registration Act 1925
Limited Liability Partnership Act 2000
Limited Partnership Act 1907
Matrimonial Homes Act 1983
Partnership Act 1890
Powers of Criminal Courts Act 1973

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Takeovers and mergers

Business is good, profits are climbing, management is efficient – now is the time to consider expansion. But you may also be taking on:

- outstanding and transferred liability for VAT;
- employees' existing and continuing holiday entitlement;
- employees' accrued rights on unfair dismissal and redundancy *but* they lose their rights if they refuse to work for you.

If the first move on acquisition is to rationalise by dismissing employees, dismissal is automatically unfair if the reason or principal reason is the takeover. But you can fairly dismiss for 'an economic, technical or organisational reason entailing changes in the workforce'. Even on fair dismissal, there may be entitlement to redundancy payments. You should therefore obtain an indemnity from your seller to cover any claim which might arise on transfer of the business.

The sole trader and expansion

The route to expansion is to take on investors, partners or incorporating yourself as a limited company.

Mergers

If there is, or may be, a 'substantial lessening of competition' the merger may be prohibited by the Office of Fair Trading and the Competition Commission. Ministers are involved if there is a public interest issue, for instance national security.

Partnerships

When taking on additional partners or amalgamating with another firm, you must change the partnership name and the partnership agreement should be amended to reflect your extended liability for new partners. Existing and incoming partners should elect for continuance, thereby avoiding assessment to tax on the basis that the partnership stopped trading and started again when you took on new partners. Incoming partners should confirm the partnership's mandate with the bank and should be joined as co-sureties to the bank guarantee. You may also want to extend their liability to cover contracts with the partnership's existing creditors – by replacing the original contracts which include them – and if they should share in existing book debts.

LLPs

LLPs must in addition comply with the Limited Liability Partnership, Companies and Insolvency Acts, and before proceeding you should take legal and financial advice.

Companies

A takes over company B if A acquires sufficient shares in B to control B's decisions.

Takeovers of private companies usually require directors' approval because the Articles, and the draft model Articles, authorise them to refuse to register a transfer of shares. It is, however, usually impossible to control a private company unless you hold more than 50 per cent of the voting shares.

Takeovers and amalgamations must also comply with the Companies and Insolvency Acts and again you should obtain legal and financial advice before taking action.

Share for share and part cash offers

You can make a bid for a company in return for shares which are distributed to the selling company's shareholders in accordance with their rights. You can also make an offer extended generally to all the shareholders with part payment in your shares and the balance in cash. The offer is usually conditional on the acceptance of at least three-quarters of the shareholders, holding not less than 90 per cent of the shares – because you are usually bound to acquire the remaining 10 per cent on the same terms, unless the court orders otherwise on a shareholder's application. Bids can be confined to one class of shares, if your company already holds nine-tenths of that class of shares. If acceptances exceed the offer, you must take shares, *pro rata*, from all accepting shareholders.

You can transfer assets from one company to another on a tax neutral basis. Transfer is on a no gain/no loss basis and can consist of a disposal of the whole or part of a business to another company as part of a scheme of reconstruction or amalgamation, but the assets must remain within the scope of UK taxation.

There is a 0.5 per cent Stamp Duty on sales of shares and other securities, but there are reliefs for certain company reorganisations where there is no significant change of underlying ownership.

Straightforward exchange of shares between buying and selling companies, when you are not seeking further capital, is usually done by issuing your shares to the selling company's shareholders. If a majority of the selling company's shareholders accept, the selling company's shares are cancelled, except for any your company is to hold, and the selling company's shareholders receive your shares in payment for theirs. Payment can be in cash instead of shares if the reserve created by cancellation of the shares is capitalised. This is then applied to pay up further shares in the selling company, which are issued to you in place of the cancelled shares. The result is the same as a share-for-share takeover by compulsory acquisition but the majority necessary to approve the takeover is smaller and the court, creditors and shareholders must approve the arrangement.

Taking over while raising capital

If you are seeking more capital, the selling company must be wound up and its shareholders must make further contributions of capital. A new company is formed and the selling company sells its undertaking through its liquidator in return for shares in the new company. Shareholders receive your shares or they can be given partly paid-up shares in return for the fully paid shares they previously held, which means they take on a fresh liability for calls or give up their rights to the new shares.

Varying shareholders' and creditors' rights

Three-quarters of the shareholders or creditors – in number and value – must consent if their rights are to be varied. They can object within 21 days to the court, which can amend, vary, confirm or overrule the scheme. A selling company wanting to persuade its shareholders or creditors to agree to a sale must also apply to the court. The court monitors both these procedures and can order compensation for dissenting shareholders.

Directors' compensation for loss of office

Directors' compensation for loss of office must be approved by the selling company's shareholders or as specified in the Articles, otherwise the directors are liable to prosecution and the compensation belongs to shareholders, even if payment is made within a year before, or two years after, the takeover offer. The Company Directors' Performance and Compensation Bill currently before Parliament requires the board to take performance into account, whatever is in the service contract, and to disclose the payment on a shareholder's request, and if it exceeds the previous 12 months' basic salary, to include it in the annual report with an explanation of the amount.

The first £30,000 is not taxable and a reduced rate of tax applies up to £50,000. Tax is payable at the full rate on the balance. Payments for shares to directors exceeding the price paid to other shareholders are also considered to be compensation, unless the bid is only for *de facto* control by acquisition of less than a third of voting shares, when the directors are not accountable to shareholders, although they may be liable to the company. They can, however, keep genuine payments for premature determination of service contracts or as a pension for past services.

Statutory references

Companies Acts, 1985, 1989 and 2006
Employment Protection (Consolidation) Act 1978
Income and Corporation Taxes Act 1970 (as amended)
Insolvency Act 1986
Limited Liability Partnership Act 2002
Partnership Act 1890
Registration of Business Names Act 1916
Transfer of Undertakings Regulations 2006

Appendix: Useful addresses

Advice Services Alliance
12th Floor
New London Bridge House
New London Street
London SE1 9SG
Website: www.asa.org.uk

Advisory, Conciliation and Arbitration Service (ACAS)
Brandon House
180 Borough High Street
London SE1 1L1
Tel: 06457 47 47 47
Website: www.acas.org.uk

The Bar Council
289–293 High Holborn
London WC1V 7HZ
Tel: 020 7242 0082

British Franchise Association
172 Danebrook Court
Oxford Office Village
Langford Lane
Oxford OX5 1LQ
Tel: 01865 379892
Website: www.thebfa.org

British Insurance Brokers Association (BIBA)
BIBA House
14 Bevis Marks
London EC3A 7NT
Tel: 0844 770 0266
Fax: 020 7626 9687
Website: www.biba.org.uk

Business Link
A BERR service providing practical help and advice at local offices
Available online at www.businesslink.gov.uk
Tel: 0845 600 9006

Centre for Effective Dispute Resolution
Exchange Tower
1 Harbour Exchange
London E14 9GB
Tel: 020 7536 6000
Fax: 020 7536 6001
Website: www.cedr.co.uk

Chartered Institute of Arbitrators
International Arbitration and Mediation Centre
12 Bloomsbury Square
London WC1A 2LP
Tel: 020 7421 7444
Website: www.arbitrators.org

Companies House addresses
English/Welsh companies
Companies House
Crown Way
Cardiff CF14 3UZ
Website: www.companieshouse.org.uk

There are also offices in London, Birmingham, Leeds and Manchester

Scottish companies
Companies House
37 Castle Terrace
Edinburgh EH1 2EB

Central enquiries for all branches
Tel: 0870 333 3636
Fax: 029 2038 0801

Department for Business Enterprise and Regulatory Reform (BERR)
Ministerial Correspondence Unit
1 Victoria Street
London SW1H 0FT
Tel: 020 7215 6740
Website: www.berr.gov.uk

Export Credits Guarantee Department
2 Exchange Tower
PO Box 2200
Harbour Exchange Square
London E14 9GS
Tel: 020 7512 7000
Fax: 020 7512 7649
Website: www.ecgd.gov.uk

Health and Safety Executive
HSE infoline
Rose Court
2 Southwark Bridge
London SE1 9HS
Tel: 0845 345 0055
Website: www.hse.gov.uk

HM Courts Service
Customer Service Unit
5th Floor, Clive House
Petty France
London SW1H 9EX
Website: www.hmcourts-service.gov.uk

HPI Ltd (Hire purchase information – motor vehicles)
Dolphin House
New Street
Salisbury
Wiltshire SP1 2PH
Tel: 01722 422422
Website: www.hpicheck.com

Information Commissioner (data protection)
Head Office
Information Commissioner's Office
Wycliffe House
Water Lane
Wilmslow
Cheshire SK9 5AF
Tel: 01625 545740
Fax: 01625 524510
Website: www.sco.gov.uk

Institute of Directors
116 Pall Mall
London SW1Y 5ED
Tel: 020 7839 1233
Website: www.iod.com

Insurance Ombudsman (now part of the Financial Ombudsman Service)
South Quay Plaza
183 Marsh Wall
London E14 9SR
Tel: 0845 080 1800 and
020 7964 0500
Fax: 020 7964 1001
Website: www.financial-ombudsman.org.uk

Land Registry
Tel: 0870 010 8318
Website: www.landreg.gov.uk
Land registry searches online: www.landsearch.me.uk

The Law Society
113 Chancery Lane
London WC2A 1PL
Tel: 020 7242 1222
Website: www.lawsociety.org.uk

Register of Judgments, Orders and Fines
173–175 Cleveland Street
London W1S 6QR
Tel: 020 7380 0133
Website: www.registry-trust.org.uk
Website: www.hmcourts-service.gov.uk

Royal Institution of Chartered Surveyers (RICS)
RICS Contact Centre
Surveyor Court
Westwood Way
Coventry CV4 8JE
Tel: 0870 333 1600
Website: surveyline.com

The Stationery Office (TSO)
St Crispins
Duke Street
Norwich NR3 1PD
Tel: 0870 600 5522
Website: www.tso.co.uk

UK Intellectual Property Office
Concept House
Cardiff Road
Newport
South Wales NP10 8QQ
Central enquiries:
Tel: 0845 950 0505
Fax: 01633 817777
Website: www.ipo.gov.uk

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