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# Answers

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1 This question focuses on the fundamental human rights and freedoms afforded protection under Maltese law.

- (a) In the period running from Malta's ratification of the European Convention on Human Rights and Fundamental Freedoms to August 1987 when the European Convention Act entered into force, the Convention did not form part of Maltese ordinary law. Nonetheless, even throughout these years, its impact, even though minimal, could still be felt.

The human rights provisions in both the 1961 and 1964 Malta Constitutions were based on Commonwealth Constitutions which, in turn, were based on the wording of the Convention. As remarked by the main compiler of our Constitution, the inspiration of the European Convention on Human Rights on Chapter IV of the Constitution of Malta is, to say the least, 'very obvious'. Thus, if one takes the political rights which both the Convention and the Constitution adopt, one notes that they are very similar in wording. Article 2, guaranteeing the right to life, is identical to the local article 34, except for the words an unlawful act of war. Article 4 of the Convention, relating to the protection from forced labour, is also extremely similar to our article 36, as are the derogations to Article 5 and reproduced in article 35 of the Malta Constitution in relation to the right to liberty and personal security. This, however, does not mean that no differences exist between the two documents.

The first piece of legislation proposed by the Nationalist Government, on taking office in 1987, was an Act which rendered the European Convention on Human Rights an integral part of Maltese law. In view of the fact that our legal system is based on dualist principles, any international treaty cannot be said to form part of domestic law until it is domestically incorporated by an enabling law. This is, in fact, a legacy of British public law and an unwritten norm of Maltese law which will continue to hold water in terms of Section 11 of the Malta Independence Order, 1964, unless and until this is repealed by the local Parliament. This point was clearly expressed, although with reference to a treaty other than the Convention on Human Rights, in the case *Charles Spiteri v Ministru tal-Bini Pubbliku u Xoghlijiet u d-Direttur tax-Xoghlijiet*.

Incorporation of the Convention was therefore felt necessary, in that, it provided broader rights for the individual and also provided for the possibility that decisions awarded in Strasbourg be enforced locally, after satisfying the condition that prior to availing oneself of international recourse, all local remedies be exhausted. In order to place the Constitutional provisions and the Convention within their proper perspective it was submitted that the former contained the minimum, and not the maximum, of rights which should be enjoyed. Thus, if a right, as entrenched in the Constitution, had a more limited extension than as expressed in the Convention, it should be the latter which prevails once this has become part of Maltese law. However, if a provision was spelt out in greater detail in the Constitution, then the latter should prevail. The principle adhered to should always be that the provisions with the more extensive definition should prevail. Should, however, an inconsistency or incompatibility arise, then it is beyond all doubt that, as the supreme law of the land, it is the Constitution which should prevail. In this manner, protection of the individuals' rights was to be increased but not at the cost of detracting from any of the power enjoyed by the organs of the Maltese State, unless subjecting the local Executive to international scrutiny be considered so.

When the European Convention on Human Rights was incorporated into ordinary law, the Maltese judiciary was 'burdened' with the added role of interpreting this instrument. Maltese judges now have the task of interpreting another piece of ordinary legislation drafted and drawn up by Parliament. However, although in view of the fact that the Convention was transformed into Maltese law judges are bound to interpret and apply the enabling Act, they are nonetheless not bound by the decisions reached in other member States which have incorporated the Convention and neither by the decisions of the European Commission and Court.

On incorporation of the Convention into Maltese law, the local courts have been vested with the added task of interpreting an international instrument and keeping abreast with the decisions of the Strasbourg organs, especially as its decisions can now be challenged in Strasbourg. Whilst this possibility of petitioning a European court on the same merits, as would have already been decided upon locally, can serve as a means to monitor local decisions, as noted earlier, there is nothing to prohibit the local judiciary from going beyond decisions of its European counterpart or in interpreting the European Convention on Human Rights in a different manner.

- (b) The main rights afforded protection under the European Convention Act, 1987 are the following:

- protection of right to life;
- protection from arbitrary arrest or detention;
- protection from forced labour;
- protection from inhuman treatment;
- protection from deprivation of property without compensation;
- protection for privacy of family life, home or other property;
- right to a fair trial within a reasonable time by an independent and impartial court;
- protection of freedom of conscience and worship;
- protection of freedom of expression;
- protection of freedom of assembly and association;
- prohibition of deportation;
- protection of freedom of movement;
- protection of right to marry and found a family;
- protection from discrimination on the grounds of race etc; and
- other rights provided for in the European Convention for the 'Protection of Human Rights and Fundamental Freedoms'.

- 2 This question seeks to test the candidates' understanding of the doctrine of privity of contract. A fundamental principle is that a contract only binds the parties to it (and their heirs). Third parties, that is all those persons who are not parties to a contract, either personally or indirectly through an authorised representative, are not bound by it.

A principle of Roman Law, which is still applicable, is that an obligation is a strictly personal relationship which does not give rise to any relations except between the persons who take part in such obligation. Thus, with respect to third parties, a contract is a *res inter alios acta* and accordingly *tertio neque prodest nocet*. Contracts result from the consent given by the contracting parties and cannot therefore be deemed to produce any effects beyond the relations existing between those who gave their consent. This principle can be found under article 999 of the Civil Code which provides that a person cannot by a contract entered into in his own name, bind or stipulate for any one but himself. Furthermore, article 1001 provides that contracts shall only be operative as between the contracting parties, and shall not be of prejudice or advantage to third parties except in the cases established by law.

Accordingly, if a person does not act in his/her own name but as agent or representative of other persons, such person shall not be bound by such contract; only the persons he/she is representing shall be bound. Similarly, such person shall not stipulate for himself but in favour of the person whom he represents; the will of the latter is implicit in mandate or in lawful representation and is presumed in *negotiorum gestio*. The latter is a quasi-contract where the interested person finds himself bound without having done anything and the person who receives something which is not due certainly has no intention of binding himself to return it.

The principle described above does however suffer certain limitations, both with regards to promises of the performance of an obligation by a third party and to stipulations for the benefit of a third party.

Article 999(2) of the Civil Code provides that a person can bind himself in favour of another person, to the performance of an obligation by a third party; but in any such case if the third party refuses to perform the obligation, the person who bound himself or promised the ratification shall only be liable to the payment of an indemnity. This provision deals with the promise of performance of an obligation by a third party. However, the effect of such a promise is never that of binding the third party, who has not consented to the performance of an obligation, nor that of binding the promiser, who has not promised something to be done by him. The effect of this promise is of someone who promises *de rato* and assumes an obligation which must be fulfilled by him and which consists in effectively procuring what the third party is bound to perform. The latter is sufficient to render the contracting party liable for damages to the other party in the event that the third party refuses to perform the obligation. He shall be responsible in damages even if the defect of ratification is not due to his fault but to the fault of the third party because until he obtains the ratification he is considered not to have performed the obligation. Once the third party ratifies the obligation then the promiser is free from liability as the obligation undertaken shall be deemed performed.

The second limitation to the principle that an obligation is only binding on the contracting parties arises in the case of stipulations made for the benefit of third parties. Article 1000 provides that it shall also be lawful for a person to stipulate for the benefit of a third party, when such stipulation constitutes the mode or condition of a stipulation made by him for his own benefit, or of a donation or grant made by him to others; and the person who has made any such stipulation may not revoke it, if the third party has signified his intention to avail himself thereof. It can be held that there are two cases in which stipulations made for the benefit of a third party constitute the mode or condition of a stipulation made in one's favour.

The first case is when the promise to the benefit of a third party is a secondary object of the contract; where the principal object is the payment of a penalty to the person who stipulates, in case the obligation is not performed. An example of such a stipulation is where A and B agree that B give C a gift and in the event that B does not give C the gift, B will pay A a penalty of €100. The object of the stipulation is that B give A the €100 as compensation for non-fulfilment of the contract between A and B. The amount stipulated by A is a stipulation in his favour which he has an interest in receiving. The obligation that B give C a gift is only a condition and therefore a secondary object to the contract.

The second case when stipulations made for the benefit of a third party constitute the mode or condition of a stipulation made in one's favour, is when a contract has two considerations. In such a case, the person who stipulates adds to the obligation of the other party towards him another obligation in favour of a third party. Thus, if A agrees to transfer to B his business activity and A binds B to improve the working conditions of certain of his employees as part of the consideration for the transfer, the interest of A, as the party who stipulates, arises from the fact that he has agreed to a lesser consideration than he would have agreed to had he not imposed this obligation on the transferor.

Article 1000 also makes reference to a donation or grant made to others. This arises when there is an alienation of something or the payment of a sum of money by the person who stipulates to the promiser together with some condition imposed on such promiser in favour of a third party. Donations accompanied by burdens in favour of third parties are typical examples, as are all bilateral contracts by which the person who stipulates sells, exchanges, grants on lease or in any way transfers anything to the promiser by imposing, as a total or partial consideration of what he gives, the performance of some obligation for the benefit of a third party. A typical example of this is a life assurance made for the benefit of a third party.

The main effect of a stipulation made in favour of a third party is that of binding the promiser in favour of the party who stipulates. Until he accepts the stipulation made in his favour, the third party does not acquire any right and until he accepts the stipulation the person who stipulates has the right to revoke the obligation imposed on the promiser. Furthermore, as this is the implicit or explicit intention of the person who stipulates, the acceptance shall not deprive him of the right of revoking the stipulation in favour of the third party at any moment in time.

- 3 The Civil Code draws a distinction between contracts and quasi-contracts and between torts and quasi-torts. Candidates are required to explain the difference between each such institute.

An obligation is a bond as it binds one of the parties towards the other thus giving rise to the necessity of giving, doing, or not doing something. This necessity is a juridical one, in that, it is sanctioned by law and it attributes an action to the creditor in order to compel the debtor to fulfil that which he has bound himself to perform.

For the actual and concrete existence of an obligation, a cause, which gives rise to such obligation is necessary, in the same way as a mode of acquisition is necessary for the acquisition of any real right. It is held that there are five causes which give rise to obligations, namely the law, contracts, quasi-contracts, torts and quasi-torts.

The law is deemed to be the cause of every obligation, in that, if the law does not recognise an obligation which the parties want to create, the obligation would remain without effect. However, a distinction may here be made between those instances where the law is the immediate effect of a provision of the law, in that, the obligation is an immediate cause of the legal provision where the law imposes such obligation, or the mediate cause where an act is required to give rise to an obligation and the law merely recognises the effect of such act. Other than those obligations which are found in the law itself, those obligations arising out of a will for example, are also regarded as having the law for their immediate cause.

In terms of article 960 of the Civil Code, a contract is defined as an agreement or an accord between two or more persons by which an obligation is created, regulated or dissolved. A contract differs from other causes of obligations, in that, it is created by the free will of the contracting parties. On the other hand, a quasi-contract arises from a voluntary and lawful act of one of the parties, while a tort and quasi-tort arises from a voluntary but unlawful act of the debtor.

However, not every kind of agreement constitutes a contract but only that which constitutes, modifies or dissolves an obligation. Thus, even an agreement to dissolve an obligation is deemed to be a contract. Once two parties can agree to create an obligation they can also agree to dissolve such obligation.

A quasi-contract is defined under article 1012 of the Civil Code which provides that a quasi-contract is a lawful and voluntary act which creates an obligation towards a third party or a reciprocal obligation between the parties.

It has been contended that the above definition is the result of a misunderstanding. Quasi-contracts were often assimilated to contracts from the aspect of the agreement between the wills of the parties and therefore the obligations arising from quasi-contracts were based on the certain will of one of the parties and the presumed will of the other. However, this does not hold water, in that, in the case of *negotiorum gestio* the interested person finds himself bound without having done anything and the person who receives something which is not due certainly has no intention of binding himself to return it. It is therefore held that, in actual fact, the basis of the binding tie rather than a presumed intention is the utility or benefit which the person interested in the *negotiorum gestio* derives and the principles of equity in the erroneous payment of a debt as it would be unjust to allow a person to enrich himself to the detriment of another. Nonetheless, in regulating the two quasi-contracts the legislator refers to the now considered obsolete explanation of quasi-contracts.

There are two types of quasi-contracts, namely *negotiorum gestio* and *indebiti solutio*. *Negotiorum gestio* is the management of one or more affairs of another person assumed by a person without being bound to and without a mandate. On the other hand, *indebiti solutio* comes into being when a person, through a mistake, pays what is not due by him under any civil or natural obligation, either because there was never an obligation or because it was already extinguished or because he pays that which is due but not by him or because he pays that which is due but not to the person who receives it.

A tort and quasi-tort is an unlawful and unjust act, whether positive or negative, whether due to *dolus* or *culpa*, which causes damage to the person or to the property of another person. It is a cause of obligations as a person causing damage is bound to make good such damage to the injured party.

The concept of tort in civil law is different from that of crime. In crimes regard is had to the violation of the law and the consequent damage done to society, whilst in torts regard is had to the damage which is caused to the individual. Very often a crime is at the same time a tort or a quasi-tort but even then in such case the two actions are kept separate.

In dealing with torts and quasi-torts, a distinction is made between direct and indirect responsibility. The former is responsibility for one's own acts, which include both torts and quasi-torts according to whether the person causing the injury is in *dolus* or in *culpa*. Indirect responsibility, on the other hand, is responsibility for acts done by others or for damage caused by animals or any other object for which one is responsible.

- 4 The question relates to private companies set up in Malta in terms of the provisions of the Companies Act, 1995 and candidates are expected to distinguish between private companies and private exempt companies.

The Companies Act provides for the setting up, regulation and management of public and private companies. Unlike the situation on the Continent, and despite the fact that both type of structures are created to serve different purposes, public and private companies both in the UK and Malta are regulated by one set of rules. Under our system, it is the law itself through its specific schedules which renders a company a private one rather than a public company.

Under the Companies Act, the presumption is that when one forms a company, one is actually forming a public company, unless one complies with those specific requirements relative to private companies. Thus, unless the regulations of Part Two of the First Schedule are specifically adopted and unless it is stated that the company is to be a private company, then the presumption is that the company is to be a public company.

More specifically, within the body of the Companies Act, it is provided that a private company is one which, besides fulfilling the requirements of the said law for it to hold the status of a private company, the company must also, by its memorandum or articles restrict the right to transfer shares; limit the number of its members to 50; and prohibit any invitation to the public to subscribe for any shares or debentures in the company.

Thus, for a company to be an ordinary private company it must include all of the said three restrictions in its articles, either by adopting Part Two of the First Schedule or by including such restrictions within its own registered articles. Furthermore, the law provides that a private company shall not offer to the public, whether for cash or otherwise, any shares in or debentures of the company or allot or agree to allot, whether for cash or otherwise, any shares in or debentures of the company, with a view to all or any of those shares or debentures being offered for sale to the public by means of a prospectus.

A further distinction made locally is between a private company and a private exempt company. Once a company has been duly formed as a private company, it may comply with other requirements and come to be considered as an exempt company and consequently be entitled not to comply with certain legal requirements applicable in the case of all other private companies.

For a company to have a private exempt status, besides complying with the three restrictions mentioned above, it must also include within its memorandum or articles other conditions which can be split into four, namely, that the number of persons holding its debentures is not more than 50; that no body corporate is the holder of or has any interest in any shares or debentures of the company; that no body corporate is a director of the company; and that neither the company nor any of its directors is party or privy to an arrangement whereby the policy of the company is capable of being determined by persons, other than the directors, members or debenture holders thereof. In regard to the above conditions, it is to be noted that an exempt company which, in terms of law, is a private company, may hold shares (no mention is made of debentures) in another private exempt company without the latter ceasing to be considered a private exempt company, provided that the total number of individual persons holding shares in the companies does not exceed 50, the companies themselves and any interest thereof in any of their own shares or debentures being disregarded.

- 5 This question seeks to test the candidates' understanding of the institute of mandate by requesting candidates to explain the rights and duties of the parties to a mandate relationship.

The relationship between principal and agent are mainly regulated under Maltese law in virtue of the provisions found in the Civil Code on mandate. Mandate is a contract whereby a person gives to another the power to do something for him. The contract is not perfected until the mandatary has accepted the mandate. Every mandate must have for its object something lawful which the mandator could have done himself.

A mandate can be granted by a public deed, by a private writing, by letter, verbally, or even tacitly. The acceptance on the part of the mandatary may also be tacit, and may be inferred from acts. Mandate is gratuitous, unless there is a stipulation to the contrary. Furthermore, mandate may be either special, if it is for one matter or for certain matters, only; or general, if it relates to all the affairs of the mandator.

A mandatary cannot do anything beyond the limits of the mandate he has been given. A mandatary is vested with wide powers in order to carry out of the mandate. He may institute legal proceedings; make and prosecute appeals; make proof by reference to the oath of his adversary; take the oath *in litem* or the suppletory oath; enforce judgements both on movable and immovable property; make a demand for the issue of precautionary acts including those for the issue of which an application or declaration on oath is required; make demand for the personal arrest of the debtor of the mandator, where such demand is required; and do any other thing which the mandator might do personally, notwithstanding that such powers have not been expressly given in the mandate. The mandatary may also, in virtue of the said powers, be a defendant on behalf of the mandator, in any law-suit concerning the matter included in the mandate. A mandatary, however, may not sue or be sued, on behalf of the mandator, although the latter may have given him authority to do so, when the mandator himself is not absent from Malta in which the action is to be held.

However, where a person has been employed to do something in the ordinary course of his profession or calling, without any express limitation of power, such person shall be presumed to have been given power to do all that which he thinks to be necessary for the carrying out of the mandate, and which, according to the nature of the profession or calling aforesaid, may be done by him.

The mandator can, for the execution of a contract, act directly against the person with whom the mandatary in his capacity as such has contracted. When the mandatary has acted in his own name, the mandator cannot maintain an action against those with whom the mandatary has contracted, nor the latter against the mandator. In any such case, however, the mandatary is directly bound towards the person with whom he has contracted as if the matter were his own.

Insofar as the obligations of the mandatary are concerned, of essence is that a mandatary is bound to carry out the mandate so long as he is vested therewith, and in the case of non-performance he shall be answerable for damages and interest. He is also bound to conclude any matter, which he may have commenced before the death of the mandator, if delay might be prejudicial.

A mandatary is answerable not only for fraud, but also for negligence in carrying out the mandate. Nevertheless, such liability in respect of negligence is enforced less rigorously against a person whose mandate is gratuitous than against one receiving remuneration.

The mandatary, unless expressly exempted by the mandator, is bound to render to the latter an account of his management and of everything he has received by virtue of the mandate, even if what he has received was not due to the mandator.

Furthermore, mandate is deemed personal in that the mandatary cannot substitute another person for himself, if he has not been empowered to do so by the mandator. If such power has been conferred upon him but without naming the person to be substituted, the mandatary is answerable for the person he has substituted if he has selected a person notoriously incompetent or insolvent or whom he otherwise knew to be such. In all cases, the mandator may act directly against the person whom the mandatary has substituted.

Where there are several attorneys or mandataries appointed by the same instrument, there is no joint and several liability between them, unless it be expressly so agreed. Each of such mandataries may validly carry out the mandate independently of the consent of the other mandataries or notwithstanding their opposition, unless the mandator has expressly ordered that one shall not act without the other, or has otherwise expressly specified their duties. The limitation of powers of each of the aforesaid mandataries may not be set up against third parties, unless such limitation appears from the instrument of procuration, or unless it is shown that such third parties have otherwise had sufficient knowledge of such limitation.

Furthermore, a mandatary owes interest on the sums which, without the authority of the mandator, he has applied to his own use, from the day on which he has made such use, and on any other sum in which he shall remain a debtor, from the day on which he is put in default, saving, in both the aforesaid cases, the usages of trade.

A mandatary who has given to the party with whom he has contracted in such capacity sufficient information as to his powers, is not liable for any warranty in respect of what he has done beyond such powers, unless he has personally bound himself thereto.

A mandator, on the other hand, is also bound to carry out the obligations contracted by the mandatary in accordance with the powers which he has given him. Thus, he is not liable for what the mandatary has done beyond such powers, unless he has expressly or tacitly ratified it.

The mandator is obliged to repay to the mandatary the advances and expenses made or incurred by him in carrying out the mandate; and he must pay him the remuneration if promised to him, or if it is presumed to have been tacitly agreed upon, regard being had to the profession of the mandatary and to other circumstances. If no negligence be imputable to the mandatary, the mandator cannot refuse to make such reimbursement and payment, even though the matter has not been successful; nor can he have the amount of such expenses and advances *bona fide* incurred or made, reduced, on the ground that they might have been less.

Furthermore, the mandator must also indemnify the mandatary for the losses he has sustained by reason of the mandate, where no negligence is imputable to him. Interest is also due by the mandator to the mandatary on the advances and expenses from the day of the payment of such sums. Furthermore, the mandatary shall have the right of retention, so long as he is not paid what is due to him in consequence of the mandate.

Where the mandatary has been appointed by several persons for a common business, each of them is jointly and severally liable towards him for all the consequences resulting from the mandate.

Both parties also have a right to terminate the mandate. Thus, the mandator may revoke the mandate whenever he chooses and a mandatary may renounce the mandate by giving notice of his renunciation to the mandator.

- 6 (a)** A director is said to include any person occupying the position of director of a company by whatever name he may be called, carrying out substantially the same functions in relation to the direction of the company as those carried out by a director. In view of this definition being so vague, it is therefore possible to be a director in legal terms while being described as a manager or chief executive, for example, and equally companies may describe employees as technical directors, which does not make them directors in the legal sense.

It is to be noted that the law does not provide for a definition of a shadow director but only extends liability for certain offences to such persons in accordance with whose directions or instructions the directors are accustomed to act. It is to be noted that our law stopped short of describing such persons and omitted the qualification existing under the UK Insolvency Act whereby a person is not deemed to be a shadow director by reason only that the directors act on advice given by him in a professional capacity. Shadow directors therefore, as opposed to *de facto* directors, shall be held liable as directors in the case of criminal offences, fraud and other offences committed by officers of the company in the course of winding up and in the case of personal liability for wrongful trading.

According to a UK text writer, the reason for introducing this concept is to prevent the people who really exercise control from sheltering behind a puppet board, while according to another text writer this concept is designed to prevent the easy evasion of legal liabilities and responsibilities through such obvious manoeuvres. Shadow directors differ from *de facto* directors because they do not purport to act as directors but on the contrary claim not to be directors and hide behind those who are.

The absence of clarity and of a definition have given rise to uncertainty as to who is to be considered as a shadow director. In a 1994 UK case, *Re Hydrodam (Corby) Ltd*, the question arose as to whether two directors of a parent company could be regarded as shadow directors of a subsidiary. It was here held that for someone to be a shadow director, four things had to be shown, namely (i) those who are the proper directors of the company; (ii) that the person directed the directors how to act in relation to the company; (iii) that the directors acted in accordance with his instructions; and (iv) that they were accustomed so to act.

Similarly, as held by an English text writer, it is possible for a parent company to be considered a shadow director of its subsidiary when the level of control which it exercises is such that the directors of the subsidiary are accustomed to act in accordance with its directions. It shall therefore be a question of fact in each case to determine whether this level of control exists.

One offence where liability may be extended to a shadow director is that of wrongful trading. Thus, where it appears that a person who was a director (including a shadow director) and who knew or ought to have known prior to the dissolution that there was no reasonable prospect that the company would avoid being dissolved due to its insolvency, such person shall be held liable to make a payment towards the company's assets as the court thinks fit. Liability for wrongful trading shall, however, not be imposed where the director, knowing that there was no reasonable prospect that the company would avoid being dissolved due to insolvency, took every step he ought to minimise the potential loss of the creditors of the company.

What has often puzzled many is who in such circumstances may be considered as a shadow director, with particular problems met insofar as a holding company which dominates the company in question, or a bank working closely in the rescue of a company in financial difficulty. As to holding companies, it has been seen possible that they may be considered as shadow directors in extreme circumstances where the subsidiary has no separate existence, has no separate premises or personnel, and where the directors are those of the holding company. Here the holding company may be potentially liable for wrongful trading, as a subsidiary is accustomed to act through its board in accordance with the holding company's instructions. In many less extreme cases, liability will again be possible as in the case where a holding company decides to withdraw its support from a subsidiary in difficulty. At this point the holding company, through its directors, would know that the subsidiary is about to fail and withdraws from the picture to escape liability.

A bank is also particularly an attractive target for a liquidator seeking a wrongful trading order. However, here again the matter is not all that clear and it appears that to be held so liable the bank would have to be proven to have such a commanding position as to give directions or instructions to the board to the extent that the board be deprived of its own volition. In order to clarify matters it is suggested that local legislation be amended to specifically exclude banks from the definition of a shadow director so that they will not be inhibited from lending support to companies facing difficulties.

The Companies Act, 1995 provides for a whole chapter on offences antecedent to dissolution or in the course of winding up. Of importance are those which involve fraud. Thus, any past or present officer, including a shadow director, shall be guilty of fraud committed in anticipation of dissolution if, within the 12 months preceding the date of dissolution, he did any one of the various acts provided for, such as concealed or fraudulently removed or pledged or disposed of any property of the company unless the latter was done in the course of business; concealed or in any way destroyed any document relating to the company's property or affairs or made a false entry therein; or exercised false representation or fraud to obtain property for the company on credit or to obtain the consent of the creditors to an agreement relating to the affairs of the company or its dissolution.

- (b) An auditor may be removed from office at any time by means of a resolution taken at the general meeting consented to by more than 50% of the issued shares having voting rights. It should be noted that this is the same procedure which is to be adopted by a company which wishes to remove one or more of its directors.

Where a resolution removing an auditor is passed, the company is bound to inform the Registrar of Companies within 14 days thereof. Every officer in default shall be liable to a penalty and for every day during which such default continues, to a further penalty.

If removed, an auditor has every right to request compensation for damages in respect of the termination of appointment as auditor or for any other appointment terminating with that of the auditor.

Furthermore, an auditor who has been removed shall have, notwithstanding his removal, the right to receive notice, attend and speak at any general meeting:

- (i) at which his term of office would otherwise have expired; or
- (ii) at which it is proposed to fill the vacancy caused by his removal.

An auditor who is being removed or not being re-appointed is entitled to receive notice of the text of and reasons for the proposed resolution of the general meeting whereby it is intended to remove him. The auditor proposed to be removed may make, with respect to the intended resolution, representations in writing to the company, not exceeding a reasonable length and request their notification to members of the company. On receipt of such, the company, unless received too late, may include the fact that such representations have been received in the notice or may send a copy of such representations to every member to which notice has been sent. If the representations are not sent out, the auditors being removed may request that the representations be heard orally during the meeting.

Where an auditor ceases for any reason to hold office, he shall deposit at the company's registered office a statement of any circumstances connected with his ceasing to hold office which he considers should be brought to the attention of the members or creditors of the company or, if he considers that there are no such circumstances, a statement that there are none. The statement shall be deposited not later than 14 days beginning with the date on which the auditor ceases to hold office.

Where the statement is of circumstances which the auditor requests to be brought to the attention of the members or creditors of the company, the company shall within 14 days of the deposit of the statement either:

- (i) send a copy of it to every person entitled to receive copies of the annual accounts; or
- (ii) submit an application to the Court for an order that there are grounds of sufficient gravity to warrant that the statement should not be circulated and the Court shall decide upon the matter accordingly.

Where the company submits an application to court, the court must notify the auditor of this application and must hear both parties before deciding on the matter. Unless the auditor receives such notice of the application before the end of the 21 day period beginning with the day on which the notice is deposited, he shall within a further seven days send a copy of the statement to the Registrar of Companies.

If the court deems that the auditor is using the statement to secure needless publicity for defamatory matter, costs for the application may be awarded to be paid by the auditor and the company shall be obliged to send a statement setting out the effects of the court order to every person entitled to receive copies of the annual accounts of a company. In any other case, on reaching a decision the company shall notify the auditor of the court's decision and send a copy of the auditor's statement to every person entitled to receive the annual accounts of a company. The auditor must also send a copy of the statement to the Registrar of Companies.

- 7** A form of security which a shareholder may give to a creditor is a pledge over shares which he is a subscriber of. The question requires candidates to detail the procedure which is to be followed in order for shares in a company to be pledged in favour of a third party.

Shares may, unless otherwise provided in the memorandum or articles of the company or under the conditions of issue of those shares, be pledged by their holder in favour of any person as security for any obligation. The pledge of shares must be done by means of an instrument in writing entered into between the pledgor and the pledgee. However, in the case of a private company, shares may not be pledged unless the memorandum or articles of the company specifically so provide. Therefore, unless already provided, prior to registering a pledge over shares, the statutory documents of the company must be amended to so provide for the pledging of its shares.

In order to place the pledge into effect, notice thereof must be delivered by the pledgor or the pledgee, to the Registrar of Companies for registration within 14 days of the granting of the pledge. The company whose shares have been pledged, shall also be notified of the pledge in writing within the said period and the company shall record that fact in the register of holders of the respective shares. The pledge shall be effective in relation to a third party only after the registration by the Registrar.

During the existence of a pledge of shares, any transfer or other assignment made by the pledgor, whether by onerous or gratuitous title, of the pledged shares shall be null and void, unless it is made with the consent of the pledgee.

In the event of a default under the agreement of pledge and upon giving notice by judicial act to the pledgor and the company, the pledgee shall be entitled to do any of the following: (i) dispose of the shares which are pledged in his favour; or (ii) appropriate and acquire the shares himself, in settlement of the debt due to him or of part thereof.

The value of the shares may be established by agreement between the pledgor and the pledgee. In case of disagreement, the fair value for the sale or appropriation of the shares shall be determined by a certified public accountant appointed by the Civil Court, First Hall, on the application of the pledgee.

The pledgee shall, in selling the shares, be obliged to seek the best price being not less than their fair value. In the event that a buyer cannot be found for the sale of the shares at their fair value, the pledgee shall apply to the court for the shares to be sold at less than their fair value as aforesaid, subject to such conditions as the court may deem fit to impose.

Furthermore, in the case of a pledge of shares in a private company, the pledgee shall be obliged, prior to the exercise of the right to dispose of the shares or to appropriate them, to offer the shares to other shareholders of the company in accordance with any pre-emption rights relating to the transfer of shares as laid down in the memorandum or articles of that company, and, failing such pre-emption rights, to all the other shareholders of the company in proportion to their respective holdings. In either case the shareholders shall be entitled to purchase the shares at the fair value. Such offer shall be kept open for at least ten working days. In the exercise of these rights, the pledgee shall only sell or appropriate such number of shares as are needed to raise sufficient proceeds to repay the debt due. All remaining shares shall be released to the pledgor.

In the pledge agreement, the parties may agree on the person or persons who shall exercise all the rights belonging to the holder of shares including voting rights and the right to receive dividends and interest payments. If the agreement does not make provision for such matters, all rights pertaining to a holder of shares shall, for the duration of the pledge, be exercised by the pledgor.

Furthermore, unless the pledgor and the pledgee have otherwise agreed in the pledge agreement and notice thereof has been given to the company, dividends or interests payments due on shares which are pledged shall, during such time as the pledge is registered in the register of holders of the respective shares, be paid by the company to the pledgee.

Notice of termination of the pledge must also be delivered by the pledgee to the Registrar within 14 days of the termination of the pledge. The company, shares in which have been pledged, shall also be notified in writing of the termination of the pledge within the said period and the company shall record that fact in the register of members of the respective shares.

- 8** Contracts of employment for an indefinite period may be terminated on grounds of redundancy provided that the notice stipulated at law is given by the employer to the employees whose employment is being so terminated.

- (a)** Redundancy is not defined in our law. Industrial practice has interpreted it to include: (i) excess of supply and (ii) lack of profitability. Excess of supply is when the firm is producing more than the market can absorb and lack of profitability may be encountered where an entity is producing and has to sell at prices higher than the consumer is willing to pay.

An employee whose employment is terminated on grounds of redundancy shall be entitled to re-employment if the post formerly occupied by him is again available within a period of one year from the date of termination of employment, in which case he cannot be re-employed at conditions which are less favourable than those to which he would have been entitled if his contract had not been terminated. Furthermore, any person so re-employed shall be considered to have continued in his employment notwithstanding the termination on grounds of redundancy.



Of importance to note is that where an employer intends to terminate the employment of an employee on grounds of redundancy, he would have to terminate the employment of that person who was last engaged in the class of employment effected by such redundancy (last in first out). The only exception lies in the case of the last employee being engaged being related to the employer by consanguinity or affinity up to the third degree, where the employer may, instead of terminating the employment of such person, terminate that of the person next in turn.

Furthermore, redundancy must be genuine and not fictitious (the employer cannot bring about a situation leading to redundancy).

- (b) In the event of a collective redundancy, the provisions of the Collective Redundancies (Protection of Employment) Regulations, 2002 (L.N. 428 of 2002) must also be analysed. The purpose of these regulations is to regulate the protection of the employment of employees in the case of collective redundancies. 'Collective redundancy' means the termination of the employment by an employer on grounds of redundancy, over a period of 30 days, of:

- (i) 10 or more employees in establishments normally employing between 20 and 100 employees;
- (ii) 10% or more of the number of employees in establishments between 100 and 300 employees. The case under consideration falls within this bracket and therefore the proposed redundancies in Xejn Limited can be deemed a collective redundancy; or
- (iii) 30 employees or more in establishments employing more than 300 employees.

For the purposes of calculating the number of redundancies, termination of an employment contract which occurs on the employer's initiative for one or more reasons which are beyond the control of the individual employees shall be assimilated to redundancies, provided that there are at least five redundancies. The reduction in orders and the reason causing the same cannot be imputed to the management of Xejn Limited and is hence beyond the control of the same.

Furthermore, article 37 of the Employment and Industrial Relations Act, 2002 (which provides that prior to terminating the employment of any employee on grounds of collective redundancy, the employer must notify, in writing, the employees' representatives recognised by him of the termination of employment contemplated by him and shall provide the said representatives with an opportunity to consult with him) and these Regulations (L.N. 428 of 2002) shall not apply to terminations of employment effected under definite contracts of employment (except where such terminations take place prior to the date of expiry or the completion of such tasks) and the reason for such prior termination is the redundancy of the employees so terminated or to the terminations of employment of crews of sea-going vessels.

An employer proposing to declare a collective redundancy must, before terminating such employment, notify the employees' representatives in writing of the termination of employment contemplated by him. Furthermore, he must provide the said representatives with an opportunity to consult with him. Such consultations must begin within seven working days from the day on which the employees' representatives have been notified of the intended collective redundancies and such consultations shall cover ways and means:

- (i) to avoid the collective redundancies;
- (ii) to reduce the number of employees affected by such redundancies; or
- (iii) to mitigate the consequences thereof.

Within this seven day period, the employer shall be bound to supply the employees' representatives with a written statement giving all relevant information, including:

- (i) the reasons for the redundancies;
- (ii) the number of employees he intends to make redundant;
- (iii) the number of employees normally employed by him;
- (iv) the criteria proposed for the selection of the employees to be made redundant;
- (v) details regarding any redundancy payments which are due; and
- (vi) the period over which redundancies are to be effected.

The above obligations of the employer shall apply irrespective of whether the decision regarding the collective redundancies is taken by the employer or the undertaking controlling the employer.

Furthermore, the employer shall forward to the Director responsible for Employment and Industrial Relations (hereinafter the Director), a copy of the above-mentioned notification and statement on the same day that these are notified to the employees' representatives.

Saving the right of employees regarding notice of dismissal, any projected collective redundancies notified to the Director shall only take effect on the lapse of 30 days after the said notification, unless the Director feels that there exist exceptional circumstances warranting a shorter period of notification.

On the other hand, the Director may extend the period by a further 30 days if it appears to him that such extension may provide further opportunity for the resolution of the reasons for the redundancies or for the identification of solutions to the benefit of those employees who are being declared redundant. In such a case, the Director shall inform the employer of such extension in writing before the lapse of the initial period.

What is therefore important is that the management follow the procedure which is stipulated in the regulations.

- 9 (a) In the same way in which a company is registered and can commence to trade and undertake the activities for which it was registered, a company shall continue to exist until struck off the Register of Companies. Liquidation proceedings normally lead to such striking off, which proceedings can be brought into motion by various modes.

In terms of article 214 Companies Act, a company shall be dissolved and consequently wound up either if (i) the company has by extraordinary resolution resolved that the company be dissolved and consequently wound up by the court; or if (ii) the company has by extraordinary resolution resolved that the company be dissolved and consequently wound up voluntarily.

In the case under consideration, given that the financial situation warrants attention, the shareholders have decided to convene a meeting. At such meeting, the current financial situation of the company as well as its future prospects should be looked into. If following such a review they consider that the company is not in a viable situation to continue operating, they should resolve in terms of article 214(a) to place the company into liquidation.

- (b) In the event that the shareholders choose not to place the company into liquidation and the company continues to trade despite its precarious financial situation, creditors may commence action to place the company into involuntary liquidation. Furthermore, action may be taken by the creditors against the management for continuing to operate and incur further losses despite the fact that the company is unable to pay its debts.

Offences under the Companies Act, such as fraudulent and wrongful trading, also give rise to situations where the culprits are held personally and unlimitedly responsible for their acts. Fraudulent trading arises where, in the course of the winding up of a company, it appears that business was carried on with the intent to defraud the creditors of the company or any other third party or for any other fraudulent purpose, in which case the court may, upon the application of either the official receiver, liquidator, creditor or member, impose personal liability without any limitation of liability on those who have been a party to the fraud. This provision can be said to be very wide for a number of reasons.

Thus, the courts may impose unlimited liability on the persons it holds responsible, with no prescribed limitation on the quantum of the compensation that would have to be paid, in that, this may be set at a higher amount than that which was actually involved in the fraud, and with no limitations as to the persons who may be held so responsible, as the court can impose liability on any person who has been involved in the fraudulent trading. Also the list of persons who may bring forward a claim is wide, in that, this may be done not only by the creditors who have been defrauded but by all the creditors of the company. Finally, the said provision does not only impose civil liability and personal liability but also criminal liability, in creating an offence punishable with a fine and/or imprisonment. On the other hand, the provision on fraudulent trading may not be seen as effective, in that, in the first place this can only be invoked when the company is in the course of winding up, and secondly, this can only be invoked in cases of fraud which require a heavy onus of proof to be satisfied by the plaintiff alleging the fraud.

Wrongful trading applies in the case of an individual who, before the winding up, was a director of the company, and knew or ought to have known that there was no reasonable prospect that the company could not avoid being declared insolvent; provided that liability is avoided where the person concerned took every step to minimise the potential loss of the creditors on the assumption that he is a reasonably diligent person having the general knowledge, skill and experience expected of a person occupying his same post. One notes that personal and unlimited liability can, in the case of both fraudulent and wrongful trading, be imposed upon those persons on whose directions or instructions the board of directors act or are accustomed to act, in other words, the shadow director.

Personal, joint and several liability is also assumed by persons who were directors (or shadow directors) of a company in the twelve months preceding its winding up and who are prohibited, up to two years from the date when its name is struck off the register, from doing any of the following: (a) to be a director of a company that is known by a name which is the same or similar to that which was placed into insolvent dissolution and of which they were a director; (b) to in any way, whether directly or indirectly, be concerned or take part in the promotion, formation or management of any such company; or (c) to in any way, whether directly or indirectly, be concerned or take part in the carrying on of a business carried on under such a prohibited name.

In addition, the law mentions those instances where a company may be or shall be dissolved and wound up by the court. A company may be dissolved and wound up by the court:

- (i) if the business of a company is suspended for an uninterrupted period of 12 months;
- (ii) the company is unable to pay its debts. A company shall be deemed to be unable to pay its debts (a) if a debt due by the company has remained unsatisfied in whole or in part after 24 weeks from the enforcement of an executive title against the company by any of the executive acts specified in article 273 of the Code of Organisation and Civil Procedure; or (b) if it is proved to the satisfaction of the court that the company is unable to pay its debts, account being taken also of contingent and prospective liabilities of the company.

Therefore, if the shareholders of ABC Limited do not place the company into voluntary liquidation, the company may be dissolved and wound up by the court in terms of (b) above through an action instigated by the creditors.

- 10 One of the internal requisites which must be present for a contract to be deemed valid, is consent. The consent of the parties entering into a contract is of essence, without which a contract cannot be said to be concluded validly.

Consent is the will between the contracting parties to create, regulate or dissolve an obligation. For consent to exist two acts of volition must exist, namely the promise of one party and the acceptance of the other. If only one exists then there is no consent. One must also distinguish promise and acceptance from proposal and answer. The latter are two moments of consent, of which proposal is that part of consent which precedes the answer. On the contrary, promise need not precede acceptance nor need acceptance precede the promise. Thus, consent is the concurrence of the identical wills of the parties, duly formed and made known.

Consent is said to be manifested in four modes, namely by an internal and an external act, by the identity of the acts of volition of the parties and in the concurrence of these acts of volition. Consent as an internal act must be serious (not a joke), definitive (not still being negotiated) and free (not given by mistake or fraud); and externally the consent must be manifest, whether express or implied.

When consent is made known this must conform with the internal act of volition; otherwise there is deformity in consent. Such a defect may be either voluntary or involuntary. It is voluntary when one of the parties deliberately declares an intention which actually does not correspond to their true intention, that is, simulation. Involuntary deformity may be due to duress.

Furthermore, both parties must be agreeing to the same thing for consent to be valid. Thus, there must be identity between the acts of volition of the contracting parties. Disagreement is therefore always an obstacle to consent when this refers to some substantial element which is important with regards to the benefit or burden which the parties intend to derive or assume by the contract. If the disagreement does not affect the burden or benefit then it is indifferent and does not affect consent.

Finally, there must be concurrence between these wills. Therefore, a proposal does not bind the person making it but can be withdrawn unless accepted by the other party.

The parties in the case under consideration appear to have negotiated the purchase and sale of a particular thing. There was the volition of both parties to enter into the transaction which volition existed both internally and externally. However, we note that while Mark was under the impression that he was to acquire a particular famous painting, the latter consciously sold Mark another painting. Therefore in actual fact there was no unison of wills, in that, both parties were not agreeing on the same thing. Mark can therefore claim that his consent was vitiated on the basis of an error.

The defects of an act of volition, whether with reference to a contract or to any other voluntary act, are error, fraud and violence.

Error is the deformity between an idea and its object; it is a false notion of a thing. In order that error may be deemed to vitiate consent, it must be determining and excusable. It is determining and substantial when the person who gives his consent would not have given it had he known the truth, that is, had he a correct idea of the thing. Otherwise, that is if he would have equally consented even if he had a correct idea of the thing, the error would be indifferent, since the person who consents cannot say that he would not have done so had he known the truth. The error in the case under consideration can be said to be both determining and substantial, in that, had Mark realised the painting was a fake he would not have accepted to purchase it.

Moreover, the error must be excusable, otherwise Mark would simply have to blame himself, and it should not be lawful for him to evade the execution of the contract and to deprive the other party of the advantages acquired by means of the contract. Of essence is that even error of law may vitiate consent if it is determining, that is, if it is the sole and principal cause.

The most important kind of error is error of fact. Error of fact is any error which does not refer to a provision of the law and includes errors with regard to the nature of the contract, with regard to the object of the contract, to the motives which induce a person to enter into a contract and to the person of the contracting party.

In the case under consideration, Mark can claim that there was an error which referred to the object of the contract, in that, in his mind he agreed to purchase one particular painting and this was made clear to the art dealer.

The error could, however, also have been an error which referred to the quality of the thing. In this regard, one can distinguish between substantial error and accidental error, that is, according to whether the error refers to a substantial or to an accidental quality of the object. The latter distinction existed under Roman law. Thus, by error in *substantia*, the Romans meant a mistake as to the physical nature of the object, such as if copper were bought instead of gold. Error *concomitans* included any error with regard to all other qualities of the thing. This distinction is accepted under our law in terms of article 976 of the Civil Code which provides that an error of fact shall not void the contract unless it affects the substance itself of the thing which is the subject matter of the agreement. This provision is particularly relevant to the case under consideration as the error was such that it affected the substance of the contract, in that, in view of such error Mark no longer wanted to purchase the thing which the art dealer gave him. It is interesting to note that the criterion upon which we distinguish between substantial and accidental qualities is not that of Roman law, because we now adopt a subjective criterion which depends upon the way in which the parties, and especially that party who has been deceived, have considered such quality. The reason is that a quality which is not important for one person may be for another, and may also be important with regards to the purpose for which such person has acquired the thing.

Fraud is another defect of consent and is fundamental to the case under consideration. Mark can claim that the art dealer knew exactly what he wished to purchase and he deceived him in agreeing to sell him something which was different. The certificate which the art dealer gave him further reiterated the fraudulent intent of the same.

Fraud is deemed to be that artifice, deceit or simulation which is made use of by one of the contracting parties in order to deceive the other and to induce him to enter into the contract. In order that it may be deemed to invalidate consent, the fraud (i) must consist in fraudulent artifices or machinations; (ii) must be grave and (iii) must be determining and practised by the other party.

Fraudulent artifices are all those means which are made use of with the knowledge that they are false and which are apt to make an individual mistake one thing for another.

*Dolus* is grave when the machinations are such as to operate on a reasonable person, and they must exceed that sort of simulation which is usual in commerce and which is therefore allowed. *Dolus* is determining when it has such an influence on the mind of the contracting party as to deceive him and induce him to consent, when, without these artifices he would not have consented. If the *dolus* is not apt to have such an effect, it is known as accidental *dolus*.

However, what is essential is that as is provided under article 981 of the Civil Code, in order to bring forward such a claim the fraud must be proved and not presumed. In the case under consideration, Mark can provide the same with the certificate issued by the art dealer.

This marking scheme is given as a guide to markers in the context of the suggested answer. Scope is given to markers to award marks for alternative approaches to a question, including relevant comment, and where well reasoned conclusions are provided. This is particularly the case for essay based questions where there will often be more than one definitive solution.

- 1** The question asks candidates to demonstrate their knowledge on the manner in which the protection of human rights has developed under Maltese law principally with the adoption of the European Convention Act. Marks will be awarded depending on the level of knowledge evidenced by the candidates in their answers.
- 2** This question requires candidates to explain the doctrine of privity of contract.

  - 6–10 Thorough explanation of the meaning of the doctrine.
  - 0–5 Weaker answers showing little or a scanty explanation of the doctrine.
- 3** This question requires candidates to explain and distinguish between contracts, quasi-contracts, torts and quasi-torts.

  - 6–10 Detailed explanation of the meaning of the different concepts.
  - 0–5 Weaker answers showing little or a brief explanation of the subject-matter of the question.
- 4** The question deals with private limited liability companies registered in Malta under the Companies Act and requires candidates to distinguish between private companies and private exempt companies.

  - 7–10 Candidates earning these marks will clearly explain the criteria to be met in order for a company to be deemed private and for a company to be deemed private exempt.
  - 4–6 Good treatment of the information required.
  - 0–3 Poor answers given.
- 5** This question seeks to test the candidates' knowledge on the institute of mandate and the rights and obligations of the parties to such a contract.

  - 8–10 Candidates will earn such marks by clearly explaining the rights and obligations of both parties.
  - 4–7 Answers provide reasonable treatment of the subject matter of the question but providing less detail than the upper band.
  - 0–3 No or very little knowledge on the institute is given.
- 6** This question is divided into two parts with the first part dealing with the concept of a shadow director and the second part with the procedure for the removal of a company auditor.

  - 6–10 A clear explanation given in the replies to both parts of the question.
  - 0–5 Little to less detail than will be provided in answers falling in the upper band.
- 7** This question seeks to test the candidates' knowledge on the pledging of shares.

  - 7–10 Answers will give a detailed overview of the procedure to be followed in order for the shares in a company to be pledged in favour of a third party.
  - 4–6 A sound understanding of the area, although perhaps lacking in detail.
  - 0–3 No or very little knowledge of the subject area.
- 8** In answering this question candidates are expected to detail and explain the termination of employment on grounds of redundancy and the rules applicable thereto, as well as refer to the regulations issued in respect thereto. Marks will be awarded depending upon the level of detail given in the answers.

- 9** This question seeks to test the candidates' knowledge on the dissolution of companies with the first part dealing with shareholders placing the company into liquidation and the second part with action that creditors may take in the event that the shareholders do not take such action.
- 7–10 Answers will give a detailed overview of the liquidation procedure and the manner in which a company may be placed into liquidation and the action which creditors may take.
- 4–6 A sound understanding of both subject areas giving sufficient detail.
- 0–3 Insufficient coverage of the subject areas.
- 10** This question tests the candidates' knowledge on contract law, in particular on consent being an essential characteristic for a valid contract.
- 7–10 Candidates awarded such marks will have a sound knowledge of the subject matter covered by the question and be able to answer the question giving sufficient detail.
- 4–6 Candidates show that they are aware of the relative legal requirements but providing little detail on the scope.
- 0–3 Candidates demonstrate poor knowledge of the subject matter.