



Association of Accounting Technicians of Sri Lanka

AA2 Examination - January 2020

**Questions and Suggested Answers
Subject No : AA25**

**BUSINESS LAW AND ETHICS
(BLE)**

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THE ASSOCIATION OF ACCOUNTING TECHNICIANS OF SRI LANKA
EDUCATION AND TRAINING DIVISION

**AA2 Examination - January 2020
(AA25) Business Law and Ethics**

SUGGESTED ANSWERS

SECTION – A

Objective Test Questions (OTQs)

Ten (10) compulsory questions

(Total 20 marks)

Suggested Answers to Question One:

<i>Question</i>	<i>Answer</i>
1.1	(2)
1.2	(4)
1.3	(1)
1.4	(4)
1.5	(2)
1.6	(1)
1.7	(3)
1.8	<p><i>Any two (2) of the followings</i></p> <ul style="list-style-type: none">- The seller that in the case of a sale he has a right to sell goods, and that in the case of an agreement to sell he will have a right to sell goods at the time when the property is to so pass. (Sec 13)- Where there is a contract for the sale of goods by description, tht the goods shall correspond with the description. And where there is a sale of goods by sample as well as description goods must correspond not only with the description but also with the sample. (Sec 14)- If buyer expressly or impliedly makes known the seller the particular purpose for which the good is required, Goods must be reasonably fit for such purpose. (Sec 15(1))- Goods must be of “Merchantable Quality”.- Where the contract of a sale by sample, the bulk shall correspond with the sample in quality.

1.9

Any two (2) of the followings

- To advise the government on the development of the securities market.
- To regulate listing and issue of securities in a licensed stock exchange.
- To direct a licensed stock exchange to reject any application made to it for listing.
- To inquire and conduct investigations into any activity of a licensed stock exchange, broker, dealer, company or trustee of unit trust, a registered market intermediary or any listed public company.
- To implement the policies and programmes of the government with respect to the market in securities.

1.10

Any two (2) of the followings

- Bills of Exchange
- Collection Agreements
- Letters of Credit
- Payment on Open Account
- Payment in Advance
- Electronic Commerce

(Total 20 marks)

End of Section A

Five (05) compulsory questions.
(Total 25 marks)

Suggested Answers to Question Two:

Chapter 06 – Basic Corporate Law and Basic Partnership Law

In relation to the given scenario, where **Soysa** sold, purchased discounted stationaries to the partnership business at the market price and without the knowledge of his partner **Perera**. **Soysa** had breached following obligations imposed by law to comply with the following duties towards

- Render true accounts and full information on all things affecting the partnership, in this instance details of the discounted price of the material purchased.
- To disclose full information with regard to all benefits derived by him from all transactions concerning the partnership.

Principle laid down in the following cases, applies to the given scenario.

Bentley v Craven (1853)

In this matter Bentley (B) and Craven (C) were partners. C was employed to buy sugar for the firm. C bought sugar at a discount and sold to the firm at the market price, and made a profit. B was not informed of this. Court held that C must account to the firm the profit made from this transaction.

Pathirana v Pathirana (1967)

In this matter Pathirana (P1) and Pathirana (P2) were partners in a service station. The service station belonged to a company. The company appointed the partnership as the agent of the company. P2 gave 3 months' notice to P1 of the termination of the partnership. P2 also without knowledge of P1 negotiated a new agreement with the company to obtain the agency in P2's name only. Subsequently P2 continued to trade in the same way at the same premises of the now dissolved partnership. Court held that P2 must share the profit he had made from this agency with P1 as the agency was a partnership asset.

These two principles are applying to all partnerships irrespectively the existence of partnership agreement.

In applying the above principles to the given scenario, it seems clear that **Soysa** has breached all of the above principles. As mentioned in the case law above, the **Partnership** is entitled to recover part of its profit from **Soysa**.

(05 marks)

Suggested Answers to Question Three:

Chapter 08 – Introduction to ethics and Development
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Issues faced by an accountant in an organization

- Pressure from management
- Reporting discovered violations
- The need to earn a better living
- Omission of financial Records
- Lack of ethical sensitivity

(05 marks)

Suggested Answers to Question Four:

<i>Chapter 08 – International Trade</i>
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The Bill of Lading

A bill of lading is issued to the exporter of the goods by the owner of the ship by acknowledging to transport of specific goods from one port to another port by ship. A bill of lading performs following functions.

- i) It acts as the receipt to the goods from the shipping company to the exporter. Generally, it contains quantity , quality and remarks to identify the goods. Accordingly, the shipping company is obliged to ship same quantity in same quality.
- ii) It is an evidence of the contract of carriage between the exporter and the shipping company. Generally, the parties enter into the contract prior to issuing the bills. Therefore, the bill of lading is only an evidence of the contract of carriage between shipper and carrier. The terms of the contract are usually stated on the back of the documents.
- iii) It acts as the document of title for the goods which are being shipped. The goods will be released at the port of destination, only presentation of an original copy of the bill of lading. Moreover, evenbefore the carriage reaches the importer’s port, importer transfer goods by endorsing Bill of Lading.
- iv) It is used to claim insurance compensation in the case of any damages caused to the imported goods.

(Expected to explain three functions only)

(05 marks)

Suggested Answers to Question Five:

Chapter 06 – Introduction, Creation of Agency and Types of Agents
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The principal agent relationship comes in to existence in following ways.

- **Creation of agency by expression**

Under the creation of agency by expression, the principal gives expressly the authority to the agent who contracts with a third party on behalf of the principal. Hence, there is no formality in appointing an agent the express authority could be given in orally or in writing.

- **Creation of agency by implication**

In agency, the principal places his agent in a position such as Manager, Managing Director, Broker, Auctioneer, etc such an agent require some form of authority incidental to act in that position. But in practice part of that authority is given by expression and then balance authority is received by implication.

Agency by implication arise where, an agent acts within such ‘implied authority’.

Case Law

Hely-Hutchinson V Brayhead Ltd

- **Creation of agency by estoppel**

The agency arises owing to the rule of estoppel is called ‘the agency by estoppel’. The rule of estoppel means once you have represented expressly or impliedly something you are subsequently prevented from denying it. Accordingly, If one person represented another as an agent of him to a third party, later, that person is not allowing to deny the relationship of agency to the third party eventhough there is no such relationship exists actually.

Case Law

Freeman & Lockyer V Buckhurt Park Properties Ltd

- **Creation of agency by ratification**

As a general rule, when an agent acts without the express authority previously given principal agent relationship will not come in to existence. However, if the principal subsequently approve the beyond the power activities of agent, the agency by ratification arises. Ratification may be in the form of literal, oral or implied. However, several requirements to be fulfilled to create agency by ratification. Mere subsequent approval is not sufficient.

- **Creation of agency by Necessity**

Where, somebody acts for another in emergency situation, the principal agent relationship by necessity arises. It is mandatory to satisfy the following factors to rise such agency relationship.

- There should be an emergency situation which breaks communication between the parties.
- There should be an actual commercial necessity to act so.
- The person so acted should have good faith.

-
- Actions taken by the agent should be reasonable and prudent.
 - Actions taken should not be conflict with previous instructions of the principal.

Case Law

G.N.Railway V Swa field

(Expected to explain three ways only)

(05 marks)

Suggested Answers to Question Six:

Chapter 04 – Negotiable Instruments
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In terms of section 29 (1) of bills of exchange act following requirements should be fulfilled to become a holder in due course of a bill.

- **The bill should be complete and regular on the face of it**
If the bill is undated or does not contain the amount, lack of the signature or the endorsement then it will not be a complete bill and thus, there cannot be a valid holder in due course.
- **The holder must have taken the bill before it was overdue**
After the maturity date a term bill becomes overdue. After a reasonable time a demand bill becomes overdue. And after six months a cheque. No holder can hold the bill after it becomes overdue.
- **The holder must have no notice of previous dishonor, if there has been one**
A bill could be dishonored by non-payment or by non-acceptance. A valid holder in due course must have no notice of such previous dishonor of the bill.
- **The holder must have taken the bill in good faith**
If the holder of the bill is aware of the fact that the bill is a stolen one, then the holder cannot become a holder in due course.
- **The holder himself must have given value for the bill**
As English law applies to the bills of exchange in Sri Lanka, The consideration for a bill is a must. Accordingly a holder of a gifted cheque, stolen cheque or picked up cheque cannot be a holder in due course.
- **At the time bill was negotiated to the holder he had no notice of any defect in the title of the person who negotiated it.**

(Expected to explain three requirements only)

(Total 05 marks)

End of Section B

Three (03) compulsory questions.
(Total 30 marks)

Suggested Answers to Question Seven:

Chapter 08 – Law of Insurance, Leasing and Hire Purchase and Loans

- a) An insurance agreement should be confirmed by an Insurable interest. Insurable interest is the legal right of the insurer to insure the subject matter. Where, the insurance contract is not supported by the insurable interest, no valid insurance agreement exists. In order to have an insurable interest that person should have financial benefit by the existence of the subject matter and incur financial loss by the destruction of the subject matter.

In this case, Maya, Who owes one million from Kasun, is considering to obtain insurance policy covering Kasun's Life. Accordingly, Maya is the insuree and Kasun's life would be the subject matter of the Insurance agreement. Therefore it is important to seek, whether Maya has the insurable interest over Kasun's life according to the relationship between them.

In *Dalby V India and London Life Assurance Company* Court held that, a creditor has an Insurable interest in the life of a debtor. Accordingly, Maya is able to obtain an insurance coverage over the life of her debtor, Kasun.

- b) Contracts of Insurance are contracts of utmost good faith (Uberrimae fidei). Accordingly, All parties are obliged to reveal others all information that might influence the others' decision to enter into the insurance contract or enter in to the contract at what premium. This doctrine provides general assurance that the parties involved in an insurance transaction are truthful. The failure to disclose a material fact is caused the insurance contract voidable. Misrepresentation on material fact leads the contact to breach of good faith. It can result in a denial of benefits by the insurer.

As per the given facts, It Seems that, Maya and Sena did not disclose any fact regarding Sena's medical situation and the surgery to the Insurance company at the time of obtaining Insurance policy. The misrepresentation of facts amounts to a breach of the principle of uberrimae fidei by Sena and Amara. Therefore liability could be repudiated by insurers on ground of mis-statement and it can be justified according to the insurance law. Accordingly,

Case Law

Looker V Law Union Insurance Company

(Total 10 marks)

Suggested Answers to Question Eight:

Chapter 07 – Labour Law

a) Explain any three of the following

- **Control Test**

According to the control test, where, the employer has the right to tell the other party to the contract not only, what to do but also how to do. Moreover, if he has disciplinary control over the work to be done by the employee. Such person who is subject to be controlled is an employee. If the employer doesn't control the work done by the other party to the contract, then such party will be an independent contractor.

- **Test of Equipment**

Where, the person employed brings all the equipment required to work then such person is an independent contractor. Where, all the equipment are provided by the employer then he will be an employee.

- **Integral Test**

Integral test suggests that the individual is "part and parcel" of the organization. That is if the person is wholly a regular unit of the entity and not a casual, temporary employee then such person will be an employee.

- **Economic Reality Test**

Economic reality test indicates that if a person works for another then he is an employee. But if a person work for himself then, such person will be an independent employee.

- **Multiple Test**

A test where, all the aforementioned tests used concurrently.

Case Law

Sri Lanka Insurance Corporation V A.C.R. Wijesundara

(06 marks)

b) Every employee who is not expressly excluded by Payment of Gratuity Act, Act No 12 of 1983 are entitled for gratuity upon his or her cessation of employment. An employee should complete five(5) year of service with same employer to be entitled for gratuity payment.

The Value arrival by multiplying half of the last month salary drawn by the employee from the number of completed years of service with the employer could be received as gratuity.

$$\begin{aligned} \text{Gratuity} &= \frac{\text{Last month salary}}{2} \times \text{Completed number of years} \\ 4,500,000 &= \frac{500,000}{2} \times 18 \end{aligned}$$

Accordingly, Chanmugam can claim a gratuity of Rs 4,500,000/-

(04 marks)

(Total 10 marks)

Suggested Answers to Question Nine:

Chapter 10 – Offences related to the Business Environment and New Regulations
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- a) Offences under any of the following are constructed as unlawful activities as per the Money Laundering Act.
- Offences in relation to drugs
 - Trafficking of persons
 - Bribery
 - Exchange control violations
 - Terrorism
 - Transnational organized crimes
 - Cyber - crimes, offences under fire arms ordinance , explosives
 - Offences against children
 - Offences punishable by death or imprisonment
 - Pyramid scams

(05 marks)

b) i) **Marks**

A mark is any visible sign that serves to distinguish goods or services of one enterprise from another. It could be a word, slogan, name and group of letters, symbol, design and picture, any combination of above sound or shape of a product or packaging. A mark used in connection with goods is known as a “Trade Mark” and a mark used in connection with services is known as a “service mark”

Owner of a mark can obtain exclusive right to the mark by registering the mark under the act No 36 of 2003, Intellectual Property Act.

ii) **Trade Names**

Trade names are defined as the name or designation identifying the enterprise of a natural or a legal person. They too can be registered and protected. However, certain trade names including trade names which are contrary to morality or public order, likely to offend religious or racial feelings of any community or are likely to mislead the public cannot be registered.

(05 marks)

(Total 10 marks)

End of Section C

A compulsory question.

(Total 25 marks)

Suggested Answers to Question Ten:

Chapter 04 – Contract Law

Part (A)

- (a) This is based on the law of contract. A contract could be defined as an agreement between parties with an intention to create a legal relationship. Offer is a basic element of a contract and there is no valid contract where there is no valid offer.

Offer must be distinguished from an ‘invitation to treat’ because acceptance of the invitation to treat doesn’t create any valid contract.

An expression of willingness to negotiate is known as invitation to treat.

Series of decided cases held that followings are instances of invitation to treat

- An advertisement (*Harris V Nikerson , Partridge v Crittenden*)
- Auction sales (*Payne v Cave*)
- Tenders (*Spencer v Harding*)
- Goods display in a shop to sell (*Fisher V Bell , Crawly v Rex*)
- Prospectus
- Displaying notice

Accordingly the advertisement of antique seller for selling antique pots through an auction was not offering to sell them. Therefore, a binding contract has not been created between Dasun and Auctioneer and Dasun cannot claim damages caused due to cancellation of planned trip and cost of travelling from Galle to Colombo from the Auctioneer since there is no legally enforceable contract between parties.

(08 marks)

- b) This is based on the law of contract. Sara and the Travel Company have entered into a contract for a tour in Europe.

However, the air facility provided by the travel company was not corresponded with Sara’s requirement of business class seating and the accommodations were not matched with her requirement of star category within 500 meters from the city center which was mentioned in the contract.

These omissions by the travel company amounts to a breach of contract because the Travel Company has not obliged the “expressed terms” specifically mentioned and agreed between Sara

and the company at the time of entering into the contract

On this basis, Sara is entitled to remedy for breach of contract by the company. The following remedies are available to innocent party under the contract law.

- Damage
- Specific performance
- Injunction
- Rescission

When considering the given facts, As Sara already completed her tour, the best available remedy for Sara is asking for damages from the company as a remedy for the breach. **Sara could ask court to calculate damages considering additional expenses incurred by her due to the breach of contract and damages due to non-providing business class seating and agreed accommodation facilities.**

(10 marks)

Part (B)

Chapter 03 – Sale of Goods

This is based on the implied conditions of the sale of goods ordinance.

In terms of Section 13 of the sale of goods ordinance, the seller that in the case of a sale he has a right to sell goods, and that in the case of an agreement to sell he will have a right to sell goods at the time when the property is to so pass. If, seller is unbaled to comply with this implied term imposed by the statutory, it leads to a breach of the sales contract by the seller.

in ***Rowland V Divall***,

Divall bought a motor car in good faith from a thief. He sold it to Rowland, a car dealer. Rowland then put it in his showroom, and duly sold it to a third party. A couple of months later, the police seized the car and returned it to the true owner. Rowland paid the third party and sued Divall for the price he had paid. It was held by the court that as the seller did not have the right to sell the car, Rowland was entitled to recover the money from Divall.

As per the given facts it is almost similar to the aforesaid case, It seems that David had breached an implied conditions of the sale of goods ordinance since he has no proper right over the stolen car at the time of sale. Therefore David is obliged to pay back all the sum paid by Ronaldo.

(06 marks)

(Total 25 marks)

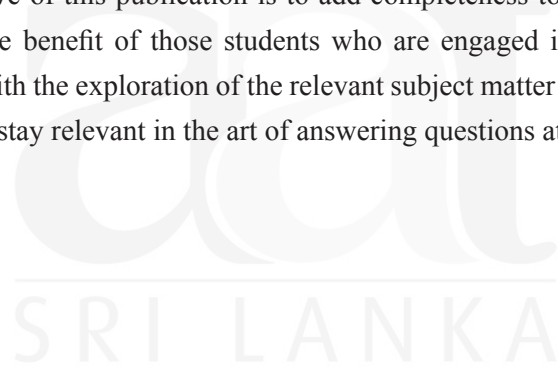
End of Section D

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