

Company Directors Should be Well Regulated

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The relative ease with which limited liability companies may be set up in Malta has made the protection of limited liability accessible to a large number of people. In reality, they may be unable or unprepared to assume the duties and responsibilities expected from company directors, fail to exercise adequate management skills, and lack proper regard to the financial interests of the company's creditors.

Limited liability should strictly serve as a legitimate stimulus to generating entrepreneurial activity and in order to protect business people from their honest commercial mistakes and failures. But unfortunately, it is being abused by some of the directors of companies who deliberately or recklessly

cause their companies to run up unsustainable debts through overtrading, lack of planning or even fraudulent objectives.

These insolvent companies will consequently end up in a liquidation process and finally be struck off the Company Registry. The net result is losses of thousands, and in some cases millions, of euro to unsecured creditors.

If we truly expect transparency and honesty in the local business environment, companies and company directors should be well regulated. I strongly believe that a person who wants to assume the role of a company director (irrespective of the size, industry sector and type of company), should apply for some sort of 'licence', which would be obtained only after rigorous due diligence and training.

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This due diligence should include the past involvement/s and any history related to the person's business/trade experience, while training is necessary to make sure that the prospective company director is skilled and competent enough to assume this role. I don't expect that a director should read an MBA programme, but every director should be aware of the very basic skills in doing business.

Does it make sense for every company director to be familiar with pertinent business legislation and skilled in good business practices?

Should every company director know his or her obligations and responsibilities as articulated in the Companies Act?

Should every company director know the proper employment process and the obligations and

responsibilities towards his/her employees, emanating from Employment Law?

Should every company director know his responsibilities and obligations vis-à-vis VAT and tax legislation?

Should every company director know his/her obligations and responsibilities with regard to data protection legislation?

Should every company director be aware of some basic business ethics, fair trading and competition in order to have a better business environment for the benefit of our economy at large?

One of the main concerns in doing business in today's business world is customers' payment defaults, extending credit, late payments and bad debts, which can

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Importance of appropriate gearing

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have serious consequences on the local business environment and the economy.

The Maltese business environment lacks the necessary skills and awareness of the importance of maintaining appropriate gearing in order to sustain sound cash flow, which is the lifeblood of any business. Very often, Maltese trade creditors are being faced with customers who overtrade and who do not request and utilise credit responsibly. Hence, a company director should be well skilled in how to grant and manage credit to ensure sound cash flow and secure profitable sales. The way forward would be an obligatory basic business training programme.

What about directors who lack the required skills, integrity or honesty in their commercial dealings? Are these directors managing other companies – or, even worse, continuing to occupy the role of directors in them? Are these directors establishing new companies of their own, hiding behind different company names?

The Maltese Companies Act contemplates the disqualification of directors or company secretaries to combat this commercial abuse. The disqualification of directors aims at preventing new companies being deliberately established to avoid the debts of insolvent predecessors, thus maintaining the integrity of the business environment.

This act clearly states that upon an application of the Attorney General or the Registrar of Companies, the court may issue a disqualification order against any person if it is satisfied

"that such person is or has been a director of a company which at any time has become insolvent, whether while he was a director or subsequently; and that his conduct as a director of that company, either taken alone or taken together with his conduct as a director of any other company or companies, makes him unfit to be involved in the management of a company."



The law also stipulates that a disqualification order is an order whereby a person shall not, without the leave of the court, be

"a director or company secretary of a company; or
a liquidator or provisional administrator of a company; or
a special manager of the estate or business of a company; or
concerned in any way, whether directly or indirectly, or take part in the promotion, formation or management of a company, for a specified period beginning with the date of the order."

Additionally, any person who, while being subject to a disqualification order, acts in contravention of it, shall be guilty of an offence and liable on conviction to a fine or imprisonment or to both.

Knowing this piece of legislation is in place is one thing, but is there the appropriate enforcement system to protect the local market and to deter improper conduct in the management of limited companies? If such a system exists, is it effective and efficiently implemented? Are all the directors of insolvent companies actually being

"Is there the right enforcement system to protect the local market and deter improper conduct?"

reported and investigated? Are liquidators giving the necessary information to the Registrar, so that an application would be made in court? Are the creditors of insolvent companies being asked to produce the necessary documents for investigation purposes?

In the UK, a Disqualification Unit within the Department of Trade and Industry operates with success. Insolvency practitioners in the UK have a statutory duty to report any directors of a failed company who they believe to be unfit. Although it

is not easy to prove 'unfitness' and bring up a case, according to the UK government figures there have been an average of 1,195 disqualifications a year.

The common criteria used to determine whether a director is unfit are

- continuing to trade at the time when the company was insolvent;
- failure to keep proper accounting records;
- failure to prepare and file accounts or make returns to Companies House as required;
- failure to submit or pay over to the Crown any tax which may be due.

The unit decides whether or not there exists a *prima facie* case of unfitness that justifies a case being brought. Once the court orders a disqualification, the UK Registrar of Companies is notified of the order, and the information is put onto the Register of Disqualified Directors, which is open to the public for inspection and is also posted online.

It is time local authorities give adequate thought to ways of effectively enforcing this legislation. EF

icient means should be developed by which the commercial public, companies' liquidators and possibly auditors, who are in direct contact with these insolvent companies and their respective directors, can report these people to the authorities.

It is also time that the police or the Registrar of Companies develop a team of forensic accountants. This team is needed to investigate insolvent companies and to take the necessary legal action against directors who have contributed to the collapse by their negligence, misconduct or misappropriation of company assets, to the detriment of their creditors.

A director disqualification tribunal should also be considered to hear all applications for disqualification on the grounds of unfitness. Besides offering a fairer trial and better access to justice, a tribunal would also serve to promote the policy behind the legislation.

I would also refer to the number of local registered companies which are not filing their accounts as obliged by law. Comparing once again our scenario with that of the UK, there are financial penalties for late filing and the penalties are doubled if a company files accounts late in two consecutive years. Ultimately, a company can be struck off the public record. Additionally, failure to file annual returns or accounts is a criminal offence which can result in directors being fined personally in the criminal courts.

The honest directors of various Maltese companies need the legal protection their competitors in other countries already enjoy – to secure better business practice in the local economy and to enhance profitability. It is all well and good to enact legislation to help our economy improve, but what is the use of having legislation in place without implementing it with a proper enforcement system?

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