

# The Business OBSERVER

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## Urgent changes needed to Companies Act

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A number of changes are needed to make the Companies Act more effective at protecting stakeholders – particularly creditors – when things go wrong in a company, the Malta Association of Credit Management believes.

The Malta Association of Credit Management (MACM) has long been highlighting the shortcomings that have emerged over the past 20 years since the Act was introduced, particularly those relating to the penalties and administrative sanctions applicable. It therefore commissioned a comparative overview of the local law with relevant UK legislation.

The MACM's preliminary analysis of the overview identified both definitions that needed to be tightened up as well as changes to the remedies.

The weaknesses emerge at every stage of a company's operation, from the requirement to submit documentation to the Company registrar, to what happens when a company fails.

Company registrar Joe Caruana recently told *The Business*

*Observer* that a new system is being put into place which will proactively remind companies when their documentation like annual accounts is due. In parallel, his team is going through the list of companies which fail to file, in an effort to identify which are active and which are not.

One option would be for the registrar to have more powers to set the wheels in motion to declare a company defunct if it is not filing accounts – even if it is actually still operating – as happens in the UK, for example.

Over the years, the courts have handed down judgments which clarified the difference between wrongful trading and fraudulent behaviour, but this is not the ideal way to tighten up definitions.

When the decision to wind up a company is being taken by its directors, more clarity is also required on what constitutes an "intent to defraud creditors" and hence the associated liabilities.

"The fraudulent director may be held legally responsible not only for contractual obligations assumed by the company, but also for any other types of obligation, including any statutory claims

made against the company (such as claims under planning legislation or tax legislation, among others, and liability in tort)," the report said, adding that this also covers debts and liabilities incurred prior to the fraud.

However, while the article is "rather wide in scope", the report's authors felt that the need to prove "intent" has "definitely both weakened and also created great complications in the potential applicability".

"The 'intent test' will certainly be complete when directors tolerate a company to incur credit when it is understood that the creditors can never be paid..." it wrote.

The concept of wrongful trading is also in need of a rethink.

"Various authors have attempted to list certain measures that should be taken in order to minimise exposure to liability for wrongful trading since the law, under article 316, does not give any form of direction as to what precautions are to be taken by a director in order to avoid this liability," it said.

When compared to the fraudulent trading provisions under Maltese law, the provisions relating to

wrongful trading are easily undermined, they felt.

"This is because there isn't the requirement to ascertain the element of fraud or dishonesty; in fact, what is required is simply unreasonable behaviour or negligence," the report said.

The problem is that this could be counterproductive and discourage business, it warned: "Indeed, there does appear to be a tendency towards judicial restraint in the imposition of liability for wrongful trading, a fear which stems from the fact that the imposition of such liability (other than in the most obvious of cases) might impede reasonable business decisions and cripple entrepreneurial activity."

The director general of the MACM, Josef Busuttill, is lobbying for the law to be fine-tuned as part of a campaign to improve decision-making when it comes to extending credit.

"Things have improved. When the association started 15 years ago, only a handful of our members had a credit application form. Now it is standard practice. We believe that credit is the lifeblood of business – but those who extend credit need to feel secure about being paid," he said.