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SOLICITORS

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Legal and Ethical Aspects

- **How is the company registered?**
  - The completion of a Form A1 (approximately two pages), together with submission of a copy of Memorandum and Articles of Association of the company and payment of the appropriate fee to the Companies Registration Office (presently €100.00 or €50 on CRODisk); Note: no identity requirements of CRO.
  - CRO check the documents and on the assumption that the same are in order will incorporate the company by the issue of a Certificate of Incorporation together with company number.

- **What do the CRO principally check?**
  - The CRO no longer accept Memorandum and Articles of Association which provide for objects of a company which are universal i.e. allow for any form of trade whatsoever by the company. The CRO require the company to have a principal object e.g. trade as a public house or hotel.
  - The CRO will check if there is share capital and if so what the authorised share capital is to be.
  - The CRO, otherwise, will not generally query the documents other than ensuring that they have been properly signed and executed.
  - Traditionally it has been efficient to use a good company formation agent and there are still benefits to doing so.

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- **What type of company might you want to incorporate?**
  - There are principally four types of companies which are incorporated in Ireland namely:
  - Private company limited by shares.
  - Private unlimited company.
  - Company limited by guarantee not having a share capital.
  - Public limited company.

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- **Private Company Limited by Shares**
  - Most common form of company in Ireland. What is it?
  - Section 33(1) of the Companies Act 1963 defines that company as follows:
  - There is a share capital set out its Articles of Association:
  - Restricts the right to transfer shares
  - Limits the number of its members to fifty
  - Prohibits any invitation to the public to subscribe for any shares or debentures in the Company.
  - Key Feature is that the liability of the members towards the company is limited generally to the amount, if any, of unpaid on the shares respectively held by them. Whilst the company is liable for its obligations to its creditors and said third parties, it is entitled to look to its members for a contribution to enable it to discharge its obligations. The amount that it can look to its members for is the stated member’s liability. The principle generally is considered only in winding up of the company.

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- **Private Unlimited Company**
  - This type of company has all the key features of a private limited company however the liability which its members have to the company is an unlimited liability.
  - Section 5(2)(c) of the 1963 Acts defines it "as a company not having any limit on the liability of its members".
  - On winding up, the members of an unlimited company are liable to contribute to the assets of the company in an amount sufficient for the payment of its debts and liabilities, and the costs, charges and expenses of the winding up, and for the adjustment of the rights of the contributories amongst themselves
  - It is not common to see unlimited companies as trading companies however they are a number of instances where you will see that now occurring.
  - Why incorporate as an unlimited Company?
  - An unlimited company does not have the same reporting requirements regarding financial information to the Companies Registration Office as other companies. Whilst an unlimited company still has to file an annual return and certain abridged financial information, it is able to limit public notice of the state of its finances.

- **Companies Limited by Guarantee not having Share Capital**
  - A minimum of seven members but no maximum number of members.
  - Is public in nature in that it can invite the public to subscribe for membership of it.
  - It has no share capital.
  - Typically used as management companies in managed estates or in club set up arrangements.
- **Public Limited Company**
  - Does not have any of the restrictions set out in Section 33(1) of a private limited company.
  - There is no maximum number of members.
  - It may invite the public to subscribe for shares in it.
  - Has a share capital.
  - Does not have to be stock exchange listed.

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- **How is the company registered?**
  - Four main ways of forming a company namely;
  - Lodging forms with the CRO on the ordinary list.
  - The company incorporation scheme.
  - CRO Disk Method
  - Company Formations Agent
  - The consequences of a company being incorporated: a company's life continues and can only be discontinued through dissolution. Dissolution takes place by way of a winding up (either in a solvent or insolvent winding up or through being struck off the register).

- **How the company is wound up?**
  - If the company is insolvent, it may be wound up voluntarily by its members known as a creditors voluntary winding up in which a liquidator is appointed without Court process through the passing of certain resolutions amongst other procedures. Alternatively, if insolvent, a creditor can petition the High Court to have the company wound up and, if an Order is granted, the matter proceeds by way of Court liquidation.
  - If the company is solvent, it proceeds by way of a member's voluntary winding up meaning that the members resolve to wind up the company and follow certain procedures and appoint a liquidator who will pay the liabilities from the assets and thereafter dissolve the company.
  - If the company is struck off from the register of companies, invariably this is for failure to file annual returns or accounts. Whilst previously this was treated as a convenient way for a company to end its life (whether having traded or not) this is highly inadvisable in this day and age.

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Consequences of Incorporation

- **Separate legal personality:**
  - The company has its own personality and is known as a legal person.
  - "It is possible to pierce the corporate veil".
  - The company is capable of earning and holding assets and property in its own right.
  - The company is capable of suing and being sued.
- **Limited Liability**
- **Transferability of Interests:**
  - Members interests may be transferred e.g. such as shares.
- **Perpetual succession:**
  - it only ceases upon one of the dissolving events referred to above and is not affected by other human frailties.
- It acts by way of affixing its common seal.
- It can grant security for its obligations to others over it assets e.g. fixed and floating charges.
- It enables the people to form organisations larger than twenty persons which otherwise cannot be formed for purposes of a common goal of profit if not incorporated.
- Taxation – different tax treatment.

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- **Corporate governance requirements :**
  - Must continue to have two directors and a secretary. A director mat also be the secretary.
  - Must display certain information.
  - Must make annual returns to the CRO and file accounts where appropriate.
  - Must maintain certain registers e.g. register of members.
  - Must carry on activity within the state.
  - Must deliver certain particulars to the Revenue Commissioners from time to time.

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- **Issues in dealing with a life of a trading company.:**
  - Section 31 – no granting of loans to director or giving of security or guarantees for debts of directors. Think whther teh company is doing something for you or you for the company?
  - Section 60 – no financial assistance permitted by a company in assisting somebody purchasing their shares in the company eg no giving security for money borrowed by that person, save in certain permitted circumstances .
  - Failure to file annual returns or accounts.
  - Duty on auditors to report breaches to the ODCE
  - Articles of association don’t capture what you are trying to do eh borrowing or securing

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- Corporate governance was in the Celtic Tiger times considered to be a smaller topic of very little interest. The almost daily appearance of Anglo Irish Bank in the newspapers has become one example of a case of failure of corporate governance and the consequences thereof.

- As the economic tide has receded, failures of corporate governance have tended to surface and the consequences of companies having turned a blind eye to good practice or required procedure are now all too apparent as our economy has suffered.

- Corporate governance refers in reality not to ownership of the company and issues arising out of that but to corporate management.

- When considering governance one considers the difference between ownership and management thereof.

- Much of management of companies is delegated to the officers of the company, namely directors and secretary.

- In many instances, the owners / shareholders of a company and directors are one in the same people however the obligations of management remain. However when differences of opinion arise in companies, particularly in small companies, the corporate governance requirements of management more often than not tend to become the focus of one party against another, particularly when crying over spilt milk on the history of the company or looking to lay blame for acts of the company at the foot of another.
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Delegation of management to directors

- The Companies Acts recognise that ultimate authority in the company rests with the members who are expected to be capable of exercising all of the functions of the company.
- However, in the overwhelming majority of cases, the articles of association of a company refer to the business of the company being managed by the directors of the company (model regulation 80 in Part 1 of Table A).
- The effect of articles of association incorporating articles similar to model regulation 80 is to vest management in the directors of the company exclusively.
- When management of the Companies affairs rest within the sole remit of the directors, it may be necessary to change the articles of association (which can only be done by way of special resolution) wherein the members will delegate certain powers. This is not commonly done. Where the members try to exercise powers of the company as members and not as a board of directors, such acts are generally invalid where those powers vest in the directors.
- Directors act by sitting on a board and pass resolutions by way of majority.
- Where permitted by the articles of association, directors may in turn delegate powers to managers, employees or other committees who may be authorised to act in a particular way or fashion however ultimately decisions made on behalf of the company rest with the Board of Directors and the Directors will be accountable for decisions made in the name of the company.
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When is the discretion of the board limited?

- When the Companies Acts 1963 – 2009 expressly or implicitly vary those
- When the Articles of Association expressly or impliedly vary those.
- When the members in general meeting, where not offending the Companies Acts or Articles of Association, give directions to the company. In this case, members giving directions to directors will have serious implications for directors and indeed serious implications for members who might be considered shadow directors. One of the implications of being a shadow director is personal liability.

- **Directors**

  - Section 2(1) of the 1963 Act refers to a director as including "any person occupying the position of director by word of the name called".
  - Every company must have two directors, one of which must be resident in the EEA. Where not resident in the EEA, a bond may be lodged.

Disqualification and restriction on becoming a director:

- Certain persons are debarred from being directors – undischarged bankrupts, persons convicted of certain offences involving company offences or for dishonesty can be prevented by Court Order.

- Qualification shares – whilst rare, it may be that the Articles of Association of a company require that for a person to be director they must maintain and hold a certain minimum number of shares as may be determined by a resolution of the members. In such circumstances directors must obtain a hold of such share qualification in order to maintain a position on the board. As stated, this is unusual in the context of most companies.

- Restricted directors – Section 150 of the Companies Acts 1990.

- Restriction arises in the course of winding up only.

- Disqualified directors – Section 160 of the Companies Acts 1990 – arises in the course of winding up only.

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Maximum number of directorships that a person may hold at any one time:

- Section 45(1) of the 1999 Act. A person may not be a director or shadow director of more than 25 companies at any one time.
- Any appointment of a person as director to a company in breach of this rule is void – think of the consequences of this.

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Types of Directors who may be appointed

- **Managing Director**
- **Chairperson**
- **Executive Director**
- **Non Executive Director**
- **Nominee Director**
- **Caretaker Director**
- **Alternate Director**
- **Assignee Director**
- **Associate Director**

It is important to note, all directors share the same duty of care and have the same responsibilities. There is no distinction.

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Types of directors who may be appointed

- **Managing Director** – power still vests in the board of directors however the managing director is given further delegated responsibility in relation to the day to day operation of the board and the company. Third parties are entitled to rely on a person being described as a managing director as having ostensible authority.

- **Chairperson** – although still referred to in company law as a chairman, the function of such person is largely confined to directing board meetings.

- **Executive Directors** – there is no definition. This would be a director who is also employed by the company in its day to day management.

- **Non-Executive Directors** – Again no statutory definition and generally is somebody who is paid to sit from time to time on board meetings but is not involved in the day to day management of the company.

- **Nominee Directors** – Typically this is a director who is expected to act in accordance with some understanding which creates an obligation or mutual expectation of loyalty to some other person other than the company as a whole. Potential conflicts of interests.

- **Caretaker Directors** – Very rare in Ireland. These are typically directors who agreed to act as directors of the company pending appointment of a new board by new shareholders.

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Types of directors who may be appointed

- **Alternate Directors** – This may be a person who is appointed as an alternate to any particular director (with the consent of the board) for a particular function only and usually for a particular period of time e.g. for a day or two days.

- **De Facto Directors** – a De Facto Director is a person who occupies the position of director but he has not been formally appointed as a director, whether by accident or intentionally.

- **Shadow Directors** – A shadow director is a person who is neither formally appointed nor necessarily held out as a director but to him certain sanctions and regulations normally reserved for directors can be applicable. Typically that person is a person, as described in the Companies Acts 1990 in accordance with whose directions or instructions the directors of a company are accustomed to act… unless the directors are accustomed so to act by reason only that they do so and advice given is by him in a professional capacity.

- **Remuneration of Directors :**

  - There is no requirement for a director to be remunerated.

  - There is also no entitlement to remuneration. To be entitled to be paid, the Articles of Association must provide that the Directors are entitled to remuneration and this is usually done by way of being determined by members in general meeting. Usually that authority is delegated to the board who in turn will enter into a contract for services or contract of employment fixing remuneration.

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- **A person will cease to be a director upon:**
  - Resignation or
  - Retirement by rotation or
  - Removal by a member.

- **Resignation** – this should be done in writing.

- **Retirement by rotation :**
  - The articles of association may make provision whereby directors shall retire by way of rotation. If that is the case, it is usual to find in the Articles of Association something to the effect that at the annual general meeting of the company in each year, the particular number of the board shall retire from office and shall be replaced by the members in general meeting.
  - It is common to exclude this sort of provision in Articles of Association.

- **Removal of directors –**
  - This may be done by the board itself (where the Articles of Association provide) or automatically (through being deemed to be removed on certain defined events e.g. unsound mind) or where removed by the members under section 182 of the 1963 Act.

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- **Meetings:**
  - Meetings of Directors – There is no specific requirement as to how many meetings of directors should occur in a year or a minimum notice period.
  - It is accepted that notice should be fair notice and generally communicated to each director.
- **Meetings of members:**
  - Annual General Meeting.
  - Extraordinary General Meeting.
  - Notice of Members Meetings.
  - Notice of Business.
  - Quorum.
  - Postponing and adjourning meetings.
  - Voting at members meetings.
  - Resolutions.

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Directors Duties

The General rule is that directors stand in a fiduciary relationship to their company and as a result of that owe duties to the company.

Recent developments have extended the directors duties to include duties towards creditors (Re Frederick Inns Limited [1994]) 1 ILRM and by statute to its employees and members.

<u>Duties to creditors.</u> Common law in Ireland holds that directors of a company have a duty to the companies creditors. What does this mean?

- Pay debts in the ordinary course and not prefer one creditor over another.
- Attend to the winding up of an insolvent company when appropriate and do not leave things too long.
- Do not dispose of the assets of the company at undervalue or to others prior to liquidation, safe in the best interests of the creditors.
- The phoenix syndrome – this would be the most common case of an abuse of creditors interests in Ireland today
- Difficulties in proving liability for breach of duty

Duties to Shareholders

Continued developments in the Sean Fitzpatrick / Anglo Irish Bank case is anticipated to become one of the contemporary cases in Ireland dealing with duties owed by a director to shareholders. One of the key questions in any consideration of the duty to shareholders is whether there is owed a fiduciary duty, ie, one which gives rise to a relationship of trust and confidence. It has been said that the distinguishing obligation of a fiduciary is the obligation of loyalty.

There are conflicting views in relation to fiduciary duties owed by directors to shareholders.

Each case will rest on the facts and there is no black and white answer. The facts must determine the relationship of trust and confidence and whether there is a relationship of loyalty. The duty to shareholders should not be confused with the duty to the company.

Duties of directors are commonly considered under the context of:

Exercise of directors powers
Conflicts of interests
Competition with the company
Duty of skill, care and diligence
Statutory duty to keep proper books and records and prepare accounts and financial statements

Duties incorporate considerations in the interest of the company as a whole, good faith, the exercise of discretion and the fettering of discretion (i.e. agreement to act in a particular way into the future).

A director cannot be considered to have gained from a fiduciary position and this particularly arises in the context of conflict of interest.

This does not mean that a director or shareholder in a company cannot be in competition with that company. Any breach in competing circumstances does ultimately come back to the issue of conflict of interest.

In considering the fiduciary relationship between directors and the company, the directors can be said to owe duty of care skill and diligence to the company and should not act negligently or conduct the business in a manner which is reckless or unreasonable.

It is very difficult, in common law and in particularly the law of tort, to establish liability of directors to said party.

Because of difficulties in common law, the companies acts has sought to provide remedies which arise particularly when a company is insolvent. These are considered under the headings as follows;

- **Reckless trading** - arises during the context of an examinership or during the course of a winding up when a liquidator or examiner must consider whether proceedings for reckless trading can be taken against directors.

The insolvency practitioner must show that the directors were <u>knowingly</u> reckless and, the liquidator or insolvency practitioner may bring proceedings to have the director declared personally liable.

Section 297A(2) is a deeming clause which provides that where a person ought to have known that his actions would have caused loss to the creditors of the company or was a party to contracting of a debt that he knew the company could honestly not pay the action should be deemed to be reckless.

- There are many practical difficulties in pursuing directors for reckless conduct for reckless trading and in the history of the Irish state there are very few cases which have been successful.

Criminal Fraudulent trading – Section 297 provides that if any person is knowingly a party to the carrying on of the business of a company with intent to defraud creditors of the company that person shall be guilty of an offence.

Civil Fraudulent trading – this is similar to reckless trading and the requirements are almost identical save that there must be an intention to commit fraud and to defraud the creditors. It is difficult to prove fraudulent trading in the Irish context. Personal liability may be imposed where fraudulent trading is established.

What if a company is not being wound up?

Misfeasance personal liability may be imposed under section 298 of the 1963 Act for the mis-application or retention of money by directors however again this should arise on the course of a winding up only.

There are practical difficulties in many windings up where there are insufficient funds to pursue these remedies.

Contracts for Work

Typically, the company and its directors, when engaging in contracts work should think practically. It is unlikely that a company or its directors will be considered to have acted recklessly where contracts for work are reduced to writing and a few basic checks are undertaken.

Practical tips

- Enter into a written contract. Written contract should include-
- Scope of the work
- The fees – how much and when are they due to be paid. VAT inclusive?
- Conditions for entering into the works
- Is there an intended limitation on liability of the company for the work it has done e.g. is liability to be limited to professional indemnity insurance levels

- Does it contain an indemnity and if so should this be taken out
- What are the conditions for any additional works to be carried out
- Is there any security registered in the company registration office over the company. Usually by a bank or other creditor.
- What is the known ability of the company to pay? Should you consider personal guarantees from the employer in the contract for works or some other form of security such as a bond or letter of credit from a bank?
- Is the person signing the letter of engagement/ contract duly authorised to do so? In this context who is that person?
- How is the company or entity that your contracting with supposed to sign e.g. by common seal? No.

Responsibilities relating to an office – see below regarding employment where the principal duties arise. Other requirements relating to offices chiefly lie in companies being tenants and what the Lease might say in relation to the obligations under their Leases.

Insurance – there is no requirement in company law that the company retains a minimum level of employer liability insurance, public liability insurance or professional indemnity insurance. Typically, however, when contracting with other parties, those parties require minimum levels of such insurance.

It is prudent to retain a minimum level of such insurance and indeed in relation to professional indemnity insurance it is often a requirement of most professions that they have such insurance at a minimum level to be able to practise.

In relation to insurance generally, but in particular to professional indemnity insurance, the following practical tips might be considered when considering insurance proposals for your business:

- Risk management – what risk management strategy can you self impose and demonstrate to insurers you have in order to show that you have a culture of risk management.
- Insure that your proposal form is not late.
- Make sure that the proposal form is not incomplete.
- Notify any claim to insurers early.
- Sell yourself. This is an important point that underwriters take note of but people tend to forget.
- Be positive in telling insurers why, in your proposal, that they should insure you at best rates and in particular highlight, where you have previously notified a claim, what you have done to be able to minimise risk of some error arising again in the future. Don't assume that the insurer will know this.

- Type the proposal form or send it as a PDF.
- Do not handwrite the proposal form.
- Give yourself plenty of time to prepare the proposal form.
- Check that attachments are numbered.
- Check that financial statements if submitted correctly add up.
- Don’t forget to sign and date the proposal form. Many proposals are received unsigned or undated and create a bad impression.
- Common areas include eligible handwriting, unanswered questions, incorrect financial information and late submission. All of these do have a bearing on your premium.
- Make a good first impression.
- Don’t be liberal with the truth. Proposal forms are extremely important in acceptance of an insured for cover.
- Read the policy. If you are not sure about cover and what it entails – ASK early!