

Goal 3 – Prosecuting Detected Breaches of the Companies Acts

Introduction

2004 was a year of increased enforcement activity levels across a number of fronts, with successful outcomes for the ODCE in virtually all proceedings in which it was involved. For the third year running, there was a substantial increase in the number of criminal convictions secured, with the figure rising to 66 (compared to 43 in 2003 and 14 in 2002). The Office also secured a number of disqualifications, restrictions and orders in compliance proceedings.

In October 2004, the Director also submitted to the Director of Public Prosecutions his first case relating a number of parties in breach of various company law obligations. A decision by the DPP on the case was awaited at year-end.

Legal Proceedings

2004 also saw the Director broaden the scope of the civil and criminal proceedings successfully concluded. The following sanctions were secured for the first time:

- a conviction for fraudulent trading;
- a conviction for acting as a director while restricted without complying with the statutory conditions;
- the restriction of a director of an unliquidated insolvent company;
- the disqualification and restriction of the directors of a company which had been struck off the Register of Companies for failing to submit annual returns.

In addition to his enforcement work, the Director also participated, directly and indirectly, in a number of other significant or novel cases. These included:

- High Court proceedings relating to publication of the Inspectors' Report on National Irish Bank Ltd.

and National Irish Bank Financial Services Ltd. (see previous Sub-Goal 2.3 material);

- High Court and Supreme Court proceedings involving the liquidation of Eurofood IFSC Ltd., a subsidiary of Parmalat SpA;
- High Court proceedings for relief from disqualification by a person who had been disqualified in England and Wales some years earlier;
- High Court proceedings for relief by persons who had recently been restricted by the High Court. As indicated later under Goal 4.1, this application was withdrawn following the ODCE indicating that it would be opposing the application for relief;
- High Court proceedings for relief by a number of persons whose exercise of their shareholding rights had been frozen, because the company had not been informed in time of their purchase of the shareholding. ODCE enquiries in these cases led us to indicate to the applicants for relief that we had no objection to their applications for relief being granted by the High Court, and we understand that a number of the applicants were subsequently successful in securing relief.

Overall, the Director directly participated in 61 proceedings, of which 19 were in the High Court and 42 were in the District Court. Of the 61 proceedings in 2004, 42 were concluded, and 19 remain ongoing at year-end. All but three of the concluded proceedings were successful in terms of progressing criminal investigations or achieving criminal convictions, rectifications of unlawful behaviour or some other satisfactory outcome. An overview of the outcome of these proceedings by type is provided in **Appendix 3.1**.

The table below summarises the nature of the Court decisions made in the successful proceedings in which the Director participated in 2004 (relative to 2003).

Number/Nature of Successful Court Decisions	2003	2004
Bankers' books orders	13	2
Charges on which convictions were secured	43	66
Charges taken into account on conviction	9	9
Charges thought proven	16	24
Disqualifications	1	3
Judicial review	1	-
Orders made in compliance proceedings	14	2
Property disposal order	1	-
Restrictions	-	2
Retention of Seized Documents	-	5
Search Warrants	10	4
Other decisions	1	5
Total	109	122

Appendix 3.2 outlines the nature of the 19 High and Supreme Court proceedings and the 42 District Court proceedings in which the Director was involved in 2004, together with the status and summary result of each type of proceedings.

Insofar as the completed civil and criminal proceedings are concerned, **Appendix 3.3** identifies the parties who were held by the High Court and the District Court to have breached their obligations under the Companies Acts. For the first time in relation to ODCE prosecutions, the District Court indicated a willingness to contemplate custodial sentences. In March, two suspended sentences of six months were imposed relating to convictions for fraudulent trading and failing to keep proper books of account. Later in the year, a further suspended sentence of three months

was imposed in conjunction with a conviction for acting as an auditor while unqualified.

Substantial penalties were also imposed in a number of individual cases. In one case, the District Court imposed fines and costs totalling over €6,500 on an individual.

The handing down of suspended custodial sentences and heavy fines and costs on a number of those convicted reflected the fact that more serious company law offences are increasingly being brought before the Courts by the ODCE. The results of ODCE enforcement actions are regularly included on the ODCE website at www.odce.ie/ shortly after the Court has made its judgement.

Enforcement Cases

In conjunction with the significant enforcement developments which occurred in the Courts in 2004, the volume of cases for possible enforcement being dealt with within the Office continued to increase dramatically last year. In all, some 469 new cases were received in 2004, a significant increase on the 269 received in 2003.

At year-end, about 474 cases for possible enforcement were on hands, representing a near doubling of the end-2003 figure of 241. This increase occurred notwithstanding the fact that 209 of these cases were closed in 2004 compared with 51 in 2003. The details on the throughput of these cases are contained in **Appendix 3.4**.

As **Appendix 3.5** shows clearly, the character of the cases on hands is currently dominated by two offence categories:

- excessive directors' loans and
- the failure to keep proper books of account.

While it has been investigating these case types, the Office also has many other priorities which it continues to pursue. In concrete terms, this has involved us in 2004 in continuing to employ a rolling system of case prioritisation which has proved to be effective in extracting the optimum outputs for the Office in enforcement terms.

The kind of substantial case volume growth which the Office is experiencing, together with an ongoing increase in successful prosecution activity (which draws on many of the same personnel) and a virtually static staffing complement, obliges the Office to ensure absolutely that scarce resources are applied effectively and proportionately to the processing of cases. It is clear at the same time that the Office will not be able to address properly its current level of enforcement work without a significant increase in staffing resources.

Sub-Goal 3.1: Developing a Balanced Enforcement Policy

As indicated above, case volume growth demands that the Office's enforcement policy be flexible and that the full range of available enforcement actions be employed in a pragmatic way.

Accordingly taking account inter alia of the character of the offence, the circumstances of the default and the quality of the available evidence, we continued in 2004 to employ one or more of the following options to rectify, deter or sanction misconduct under the Companies Acts:

- acceptance of actual remediation or an offer of voluntary rectification of the default;
- the issue of a warning letter indicating that any repeat of the default will be treated seriously;
- the issue of a warning letter urging early rectification of the default, failing which High Court proceedings will be undertaken to seek to compel compliance;
- the initiation of High Court restriction or disqualification proceedings to sanction past non-compliance;
- the taking of summary criminal proceedings for a suspected company law offence;
- the referral of an indictable offence case to the Director of Public Prosecutions for decision.

It will be clear from the statistics in this Report that the majority of cases of indicated non-compliance are dealt with on an administrative basis. In closing many

of these cases, the individuals in question have been acquainted with their obligations and have thereby been fixed with definitive knowledge of their duties in the event of their re-offending.

Where enforcement action was deemed to be warranted in 2004, the initiation of criminal proceedings on a summary basis was, as in previous years, selected most frequently. However, the Office made more use in 2004 of restriction and/or disqualification proceedings as a means of sanctioning misconduct. Some initial success in this area was reported this year with the Office's first restrictions and disqualifications. A number of other disqualification proceedings were also initiated before the end of the year, and further applications are in the pipeline.

The following three sub-sections, covering the three main offence areas, provide more detail of the matters pursued by the Office in 2004.

Sub-Goal 3.2: Upholding Disclosure Requirements

The production and dissemination of adequate information on the status and performance of a company is essential for its proper management and future development. Companies, particularly those operating with limited liability, have a relationship of mutual dependence with their stakeholders, including their employees, creditors and investors. Because each of these interests is committed in financial or other terms to the success of the enterprise, it is important that they have available reliable and timely information on the status of the entity so that they can judge its future prospects and assess the risks of continuing to engage with the enterprise.

The Companies Registration Office is the primary means by which the State seeks to ensure that the commercial market operates on a reasonably transparent basis. Every limited company formed in Ireland must regularly make available reliable information on its present status. This includes the identity of its registered office and directors and information on its current financial position.

Failure to Keep Proper Books of Account⁸

Where a company and its directors fail to record properly the transactions of the business, they are denying their stakeholders the right to make a fair assessment of the risk of their continuing to support the enterprise. The failure of a business without prior warning can disrupt the trading prospects of other companies as well as having adverse effects on company employees and investors.

This is why the Companies Acts require directors to maintain proper books of account and to prepare annual financial statements. Most of them are also required to file those statements in some form in the Companies Registration Office. Furthermore, the auditor of the company is required to give an independent opinion on the validity of the company's financial statements as prepared by the directors and to report publicly to the Companies Registration Office on any adverse opinion which s/he may have formed.

Consistent with the emphasis given by the Acts to maintaining a 'level playing field' for commercial relations, the ODCE continued in 2004 to treat seriously any reported failure to keep proper books of account. Some 15 summary proceedings were concluded by the Office arising from a suspected failure of the companies and their directors to comply with their legal obligations in this area. As will be clear from **Appendix 3.3**, the Office was successful in convicting the company and/or one or more of the directors in 14 of these cases – only one prosecution was dismissed for insufficient evidence. In one of the successful cases, the Office also secured a fraudulent trading conviction against the primary director. The circumstances of this case were outlined in **Illustration 3.3.1** in the ODCE's Annual Report for 2003.

Failure to Submit Annual Returns to the CRO⁹

This requirement is fundamental to achieving a reasonably transparent environment of commercial relations in the State. Although it is the offence which is most frequently reported to the Office, it is primarily a matter for the Registrar of Companies to enforce this obligation. Nevertheless, the ODCE does prosecute suspected offenders for this offence in conjunction with other indicated breaches of the Companies Acts.

In 2004, we secured three convictions in two cases for breaches of this statutory obligation.

Failure by Director/Secretary to notify Interest in Company Shares/Debentures¹⁰

The Companies Acts require every company to maintain a register of directors' and secretaries' interests. In order for companies to fulfil this obligation and maintain an up-to-date register, directors and secretaries must arrange for the prompt notification of their purchases and disposals of shares and debentures in the company or in any related company.

Where a director or secretary fails to comply with the disclosure requirements, their right or interest in the shares or debentures is not enforceable. This means, for instance, that shares cannot be sold or the shareholder may not exercise any voting rights as a result of his holding of the shares.

This 'freezing' of the shares or debentures may be lifted by the High Court, and in 2004, the ODCE became aware of applications to the Court by the holders of shares seeking relief from this disability. The ODCE's enquiries in two cases led us to believe that the default with respect to disclosure was accidental or caused by inadvertence on the part of the director or secretary concerned. We indicated to the Court in two proceedings that we had no objection to relief being granted, and both applications led to relief being granted by the Court.

Provision of False Information¹¹

The ODCE continues to support the CRO in its ongoing efforts to maintain a public register of company information which is both accurate and up-to-date. In our 2003 Annual Report, we warned that the provision of false information of a material character to the CRO would be treated seriously.

In 2004 in only the second such prosecution, a person was convicted of providing false information to the Registrar of Companies. The person in question submitted documents in which he had represented himself as an auditor of company financial statements when he was not in fact a person who was qualified to act as such.

⁸ Section 202 of the Companies Act 1990.

⁹ Section 125 of the Companies Act 1963 as replaced by Section 59 of the Company Law Enforcement Act 2001.

¹⁰ Section 53 of the Companies Act 1990.

¹¹ Section 242 of the Companies Act 1990 as amended by Section 106 of the Company Law Enforcement Act 2001.

Failure by Person Disqualified abroad to disclose that Disqualification¹²

Company law requires that persons disqualified in another jurisdiction must notify the Registrar of Companies of that disqualification on their appointment as a director of an Irish-registered company. The information to be disclosed includes:

- the jurisdiction in which s/he is disqualified;
- the date on which s/he became so disqualified and
- the period for which s/he is so disqualified.

Where a disqualified person makes this disclosure, it is available on the Register of Companies for public inspection, and s/he may act as a company director in the State.

However, where a disqualified person fails to disclose that disqualification, s/he is deemed to be disqualified in the State. And if they act as a director while disqualified, they are guilty of an offence. **Illustration 3.2.1** deals with a case which came to the ODCE's attention and which involved a disqualified individual having to apply to the High Court in 2004 for relief from his disqualification, in order to permit him to act as a director of an Irish-registered company. Having regard to the increasing mobility of international business people, this illustration serves to denote the importance of this disclosure obligation.

Sub-Goal 3.3: Sanctioning Parties Disregarding Company and Other Interests

The Companies Acts contain many provisions where the freedom of company stakeholders to act is prohibited or restricted in order to protect the integrity of commercial relations and reduce the risk attaching to the creditors, employees and investors of the companies involved.

Undischarged Bankrupts¹³

Undischarged bankrupts are prohibited by law from acting in a responsible position in a company. In 2004, the Office successfully prosecuted an individual who acted as a company director in this jurisdiction notwithstanding his having been an undischarged bankrupt in Northern Ireland at the time. This conviction was secured with the active support of the Northern Ireland Insolvency Service which gave evidence in support of the ODCE's prosecution. The individual was also convicted of a number of other company law offences as part of the same proceedings and is now disqualified by law from acting as a director of any Irish-registered company for five years.

Restricted Persons acting in breach of the Statutory Conditions¹⁴

Following the requirements introduced in the Company Law Enforcement Act 2001, the directors of insolvent

Illustration 3.2.1: Case of the Difficulties encountered by a Person Disqualified in England and Wales failing to disclose that Disqualification in Ireland

An individual who had been disqualified in England and Wales some years previously sought to involve himself in an Irish-registered company with the support of the company's bankers. Notification of his appointment as the company's director failed to disclose his previous disqualification. This omission meant that he was deemed by law to be disqualified in Ireland¹⁵.

When the matter came to the notice of the ODCE, our enquiries with the UK Authorities confirmed his disqualification in England and Wales. Arising from our enquiries of his status in Ireland, the individual sought professional advice and decided that he would have to seek relief in the High

Court from the deemed disqualification which now obtained in the State. The application for relief related solely to the Irish-registered company, and the effect of relief, if granted, would allow him to act in a responsible position in the management and development of the company.

Having made enquiries of the UK Authorities in relation to the circumstances of his disqualification in England and assessed the situation with respect to the Irish company, the ODCE decided to raise no objection to the application for conditional relief. The High Court was advised of our stance, and the Court subsequently deemed it appropriate to grant the relief sought.

¹² Section 195 of the Companies Act 1963 as amended by Section 51 of the Companies Act 1990, Section 47 of the Companies (Amendment) (No. 2) Act 1999 and Section 91 of the Company Law Enforcement Act 2001.

¹³ Section 183 of the Companies Act 1963 as amended by Section 169 of the Companies Act 1990.

¹⁴ Section 161 of the Companies Act 1990.

¹⁵ Section 160(1A) of the Companies Act 1990 as amended by Section 42 of the Company Law Enforcement Act 2001

companies are liable to be restricted if they fail to satisfy the High Court that they acted honestly and responsibly in relation to the conduct of the affairs of the companies. Once restricted, a person may only act as a director if specific capitalisation requirements are met. The purpose of the capitalisation requirement is to create a situation where creditors and other stakeholders are less likely to be adversely affected by a further company failure.

Now that some 500 persons stand restricted, the Office has been regularly monitoring if any of these persons are continuing to act as a director in a company which is in breach of the company capitalisation requirements. In 2004, we identified a number of potential cases and initiated proceedings against three persons. One of these cases was concluded with a conviction of the individual in question, and he now stands disqualified from being a company director or any other officer of the company for five years.

Acting as Auditor While Not Qualified¹⁶

The function of auditing is statutorily recognised in the Companies Acts because of the important independent and assurance role discharged by auditors in reviewing company financial statements. We successfully prosecuted three persons in 2004 of acting as auditors while not qualified to do so. The Office secured a total of 19 convictions against the individuals in question. A feature of most of these cases is that the persons involved could reasonably have been expected to be conversant with the fundamental distinction between accounting and auditing. We are committed to enforcing this important legal provision and to supporting auditors and their professional bodies in carrying out and promoting qualified and independent audits. Our case pipeline for 2005 suggests that there will be further prosecutions of this type of offence in the future.

Acting as Auditor While Disqualified¹⁷

From time to time, the ODCE becomes aware of situations where firms qualified to act as auditors do so in respect of companies with which they are actually connected, whether as a director or otherwise. This potentially compromises the independence of the audit

process in relation to the company in question and is prohibited by law. In 2004, we prosecuted a firm of auditors for failing to observe their legal responsibilities in this area, and the Court, having thought the 24 charges proven, decided to give the defendants the benefit of the Probation of Offenders Act 1907.

Acting as a Liquidator while Disqualified¹⁸

Similar legal restrictions apply to liquidators, in order to secure the independence and integrity of the liquidation process. One such prosecution was commenced in 2004 and is ongoing at year-end.

Directors' Transactions¹⁹

The ODCE Annual Report for 2003 reported at length on the Guidance produced by the Office in an effort to improve directors' understanding of the legal restrictions involved in using company assets for personal purposes. This work, together with our engagement with directors and auditors on reported non-compliance with this provision, has had a positive effect in raising awareness of these restrictions.

From an enforcement perspective, the Office has, as indicated earlier, a large number of possible cases on hands. One case is ongoing in the Courts at present, and it is hoped to gather sufficient evidence of the quality required to pursue a small number of other cases in this area in 2005.

Unliquidated Insolvent Companies and Dissolved Companies

The discussion under Goal 4.3 reports in detail on the work of the ODCE in 2004 with respect to unliquidated insolvent companies and dissolved companies. As indicated earlier, the Office obtained its first restrictions and disqualifications of the directors of such companies.

Sub-Goal 3.4: Acting against Parties Denying Accountability under the Law

The Director takes seriously any failure by company officers to account for their conduct or to rectify any

¹⁶ Section 187 of the Companies Act 1990.

¹⁷ Section 187 of the Companies Act 1990.

¹⁸ Section 300A of the Companies Act 1963 as inserted by Section 146 of the Companies Act 1990.

¹⁹ Section 40 of the Companies Act 1990.

misconduct following a Court order. In 2004, the Office pursued a number of cases in this category in the Courts.

Persistent Failure to comply with Company Law and Other Requirements

In 2004, the High Court heard an application by the ODCE for the disqualification of two company directors who had defaulted on their company law and tax obligations over an extended period, notwithstanding the making of a High Court order in 2001 compelling them to rectify their non-compliance. Further information on this case is contained in **Illustration 3.4.1**. The Director remains anxious to pursue actively parties with a record of repeated non-compliance with their statutory obligations.

Failure by a Director to deliver Company Books to a Liquidator²⁰

In 2004, the ODCE prosecuted the director of an insolvent company having received information from the company's liquidator that a director had failed to co-operate with him by making available certain books of the company. In the subsequent proceedings, the District Court dismissed the prosecution and awarded costs against the ODCE.

Failure by a Liquidator to report to the ODCE²¹

The liquidators of insolvent companies are now required to report to the ODCE on the affairs of the company

and on the conduct of its directors. Further information on the process is contained under **Goal 4.1** following.

Having secured 14 High Court orders in 2003 requiring liquidators to comply with their reporting obligations, the Office continued to pursue defaulting liquidators who failed to respond to administrative encouragement to discharge their statutory duties. Two such proceedings were concluded in 2004 resulting in the production of the outstanding report in one case and an order for compliance in the second. At year-end, the latter individual remained in default, and if non-compliance continues, it will be necessary for the Office to take further legal action in this case during 2005.

Conclusion

The ongoing efforts of the Office to act against those in breach of the Companies Acts continue to support our overall work in encouraging compliance. Effective enforcement is needed to deter non-compliance and to encourage a more compliant corporate environment. We will continue in 2005 to seek a good balance between our compliance and enforcement work in the interests of improving market conduct and reducing enterprise risk.

Illustration 3.4.1: Case of Widespread and Repeated Non-Compliance with Statutory Obligations

In 2004, the High Court heard an application by the ODCE for the disqualification of two company directors who had:

- failed for a period of more than ten years to submit annual returns to the CRO and corporation tax returns to the Revenue Commissioners;
- failed to comply with a High Court Order in 2001 to deliver within three months all outstanding annual returns to the CRO and certain outstanding tax returns to the Revenue Commissioners and
- failed to discharge one High Court judgement obtained by the Revenue Commissioners in 2003 against the company for over €240,000 in aggregate.

Following the commencement of the ODCE proceedings, the High Court heard that the directors had filed the outstanding annual returns and corporation tax returns with the CRO and Revenue respectively and that an accountant was appointed as a director of the company in place of one of the existing directors. On the other hand, the company's indebtedness to the Revenue had in fact increased, although evidence was before the Court that a financial institution was disposed to provide loan facilities to discharge the company's tax liabilities, subject inter alia to satisfactory security cover.

At the conclusion of the proceedings, the High Court reserved its decision on the disqualification applications, and a decision was awaited at end-2004. The application was subsequently dismissed in early 2005 and is under appeal.

²⁰ Section 293 of the Companies Act 1963.

²¹ Section 56 of the Company Law Enforcement Act 2001.