



## **Delinquent directors under the Mauritius companies Act 2001: A comparative study**

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### **Abstract**

With the rise in the activities of delinquent directors, great treats have been placed on the economy of many countries as well as on investors' confidence. Mauritius is of no exception. In fact, Transparency International (2017) which measures public sector corruption, has given Mauritius a score of 50 points out of 100 in its 2017 Annual Corruption Perception Index. Furthermore, Transparency International (2017) indicates that one of the key factors which contributes to corruption in Mauritius is director delinquent activities. Hence, one can deduce that the lack of an appropriate legal framework results in a rise in fraudulent activities by directors. This research aims identifying the loopholes in Mauritius laws regarding provisions on director's disqualification. For this purpose, a comparative analysis will be made between Mauritius Companies Act 2001 and the UK Company Directors' Disqualification Act.

The methodologies for the research are in essence comprised of the black letter approach which will analyse the legal provisions relating to directors in Mauritius and UK. Journals, books, reports amongst others will be also examined. A comparative study will also be carried out with respect to the laws on directors of the UK.

The paper aims at responding to the research objectives set out above. In particular, it is suggested that the laws of Mauritius should be amended to provide for some measures that have been adopted by the UK to bring a reduction in the number of delinquent activities committed by directors in Mauritius.

**Keywords:** directors in Mauritius, disqualification of directors in Mauritius, comparing laws on disqualification of directors in Mauritius and the UK

### **1. Introduction**

#### **1.1 Overview**

For many years, several companies, either nationally or internationally, have been victims of scandals, more particularly corporate scandals. The underlying cause behind such scandals is the fraudulent actions committed by the directors of the company. As such, the Company Directors' Disqualification Act 1986 of UK (CDDA) is seen as one of the most vital piece of legislation that restricts the powers of directors. Moreover, procedures are summarized and used for investigation and the disqualification of company directors on the basis of unfit activities.

#### **1.2 Background**

The disqualification process, which is regulated by the UK CDDA, restricts the liberty of directors to be involved in the participation of the solvent companies' management. Under this act, a director is classified as either fit or unfit executive. Moreover, the term "Director" has been subject to great amount of misunderstanding since the confusion lies in the separation of law between directors and shareholders. In fact, if a company is set up by two or three people, it is often seen as a partnership but by whom decision is to be made: directors or shareholders? In that respect, Section 128 of Mauritius Companies Act 2001 defines a director as:

"A person occupying the position of director of the company by whether name called..."

Besides, to have a proper grasp of the issue, it would be of great importance to go back to the history of UK CDDA as well as the Mauritius Companies Act 2001. First, the UK CDDA has been considered in the case of *Official Receiver v Wadge Rapps & Hunt* [2003] UKHL 49 under Section 75 of the then UK Companies Act 1928 and which was later shifted to Section 275 of the UK Companies Act 1929. The issue in the case was typically to what extent the powers given under Section 236 of the Insolvency Act 1986 on the office-holder of the company in liquidation can be recognized by law in the exercise of gaining evidence for the use of disqualification proceeding under Section 6 of the Company Directors Disqualification Act 1986.

Thereafter, various other expansions occurred in the legal system for the improvement of the disqualification order. Succeeding the report of the Committee on Company Law Amendment 1945, Section 33 of the Companies Act 1947 has been reviewed upon the grounds a disqualification order could be made. Section 9 of the Insolvency Act 1976 stated the case where a person had been a director of more than one company in liquidation, his conduct as a director is declared unfit in the management of a company. And Section 93 of the Companies Act 1981 disqualified the directors on a maximum period of 15 years. In Mauritius, the disqualification of directors is made under the Companies Act 2001 due to the fact the principles underlying the CDDA 1986 is not into practiced in our island. At first, the Companies Act of Mauritius has been introduced in 1908, following by 1913 act and 1984 Act.

The origin of the Companies Act 1984 came from the UK Companies Act 1984 and used as basic model the Singapore Companies Act 1967, enacted in 1970 and 1975. Moreover, a few provisions from the Companies Act 1967, 1972, 1976 and also the Australian Companies Act 1961 were used.

Following the important innovations in the financial sectors since 1984 and the development of Mauritius an offshore financial center, the Mauritius government faced pressures on the review and amendment of the existing legislation. These changes aimed at protecting investors and other stakeholders in the changing business world and helped in creating new investment opportunities. Improvements. Consequently, the Companies Act 1984 was repealed and the Companies Act 2001 was then enacted.

### 1.3 Research Problem and Objectives of the Study

With the rise in the activities of delinquent directors, great treats have been placed on the economy of many countries as well as on investors' confidence. Mauritius is of no exception. In fact, Transparency International (2017) <sup>[2]</sup> which measures public sector corruption, has given Mauritius a score of 50 points out of 100 in its 2017 Annual Corruption Perception Index. Furthermore, Transparency International (2017) <sup>[2]</sup> indicates that one of the key factors which contributes to corruption in Mauritius is director delinquent activities. Hence, one can deduce that the lack of an appropriate legal framework results in a rise in fraudulent activities by directors.

In the context of the UK, while the country has enacted the CDDA, evidence demonstrates that corruption committed by directors is high. For instance, the European Commission Special Eurobarometer Corruption (2012) conducted a survey where 71% of the UK citizens argue that corruption is a major problem caused by the delinquent directors in the UK. Furthermore, 64% of the dwellers agree on the fact that corruption is part of the UK culture. This in turn begs the question as to whether the CDDA is effective to act as deterrent for directors to be indulged in fraudulent activities.

Hence, the objectives of this paper are firstly to analyze the effectiveness of CDDA as a corrective and preventive mechanism for the delinquent directors. Thereafter, a recommendation will be made for Mauritius with the view of promoting legal and ethical practices for directors.

The methodologies for the research are in essence comprised of the black letter approach which will analyse the legal provisions relating to directors in Mauritius and the UK. Journals, books, reports amongst others will be also examined. A comparative study will also be carried out with respect to the laws on directors of Mauritius and the UK.

The first part of this paper has provided a general introduction on the topic followed by a deep study of its historical background. The following parts of the paper are structured as follows: part 2 consists of an analysis of the CDDA and the Mauritius legal framework in relation to company directors. Part 3 will discuss the common law duties of directors while part 4 will critically examine the extent to which the CDDA is effective in combatting the delinquent activities of directors. Part 5 will provide for some recommendations for Mauritius stakeholders and will finally conclude the paper.

## 2. An analysis of the laws relating to directors disqualification process

### 2.1 The UK CDDA 1986

#### 2.1.1 Background

For several years, the UK CDDA 1986 has proved its effectiveness. A more recent study published by Williams Lea Group (2017) <sup>[3]</sup> has found that about 1208 directors have been disqualified from office in 2013 to 2014 on the basis of unfit conduct. In fact, the UK CDDA 1986 is part of the UK Company Law where several procedures are incorporated to limit the directors' conducts. Moreover, the courts have the ability to enforce under UK CDDA 1986 a number of sanctions with regards to the disqualification of companies' directors. The courts may also conduct investigations to provide evidence for director's fit or unfit conduct. What is meant by "fit" is only the ability to show whether a director behaves in the interest of the future company.

In addition, unfit behaviors are enacted under Section 2 to 12 of the UK CDDA 1986. They include wrongful trading, unfit conduct, not obeying to the rules enforced in the UK Companies Act and situations where a company director fails to fulfill the competition law. The term "unfit conduct" is made up of different features. The most punishable offence is triggered when directors allow the continuity of business activities even if the company is insolvent. Furthermore, accomplishing management roles such as recruitment of staffs, control of company account or to take executive decisions, shall be considered as breaching the disqualification order. As required under Section 221 of the UK Companies Act, as it deals with accounting records, not submitting relevant records to the Companies House is for such an extent an offense. Unfit conduct also takes into account the failure to pay the tax owed or the submission of tax returns. Moreover, as a company is a juristic person, the use of company's assets for personal benefit is forbidden under the 1986 Act. Any fraudulent activities as well as corruption dealings are followed by the company's director disqualification. It is crucial for the directors to comply with the instructions obtained from Official Receiver of appointed insolvency practitioner.

Some practical advantages of the CDDA include the following

- a. A disqualification process provides protection to public interest from future activities. This goes in line with the aim of the UK CDDA 1986 which is to limit the directors' activities in order to ensure a good repute of the company as well as the director.
- b. UK CDDA 1986 acts as a warning. It encourages ethical behaviors, reduces the amount of unfit conducts and provides the choice for rehabilitation.
- c. Moreover, UK CDDA 1986 contains procedures which are available online and where the citizens may have access to it for better understanding of the process.
- d. The CDDA helps to identify those who make an abuse of the privilege of the limited liability for their own benefit at the expense of investors and the society at large. The procedures are formal and well-established as it is the court which sanctions delinquent directors for a period of time.

**Yet, there are some disadvantages associated with the CDDA which are as follows**

- a. It is impossible to identify, with full confidence and precision, all the specific cases where the disqualification of companies' directors occurred.
- b. Some aspects of the law are broad and complex to evaluate, for instance Section 2(1) provides for a vague definition on who can be disqualified from the office.
- c. A limit in the availability of specific file documentation may result in the unfeasibility to offer any evidence-based view as to make the sanctions effective.
- d. A research by Watt (2013) showed that in some cases, the disqualification of honest persons has been made "in a bid to save jobs by keeping the company trading" or because of what they might consider to be "quite small matters, such as errors in paperwork".
- e. Bankruptcy may occur because of unexpected circumstances, for instance, the economic crisis in 2008, but not because of risk taking.

**2.1.2 Directors disqualification**

Courts in the UK have the power to issue a director's disqualification order on the following grounds:

- a. Unfit conduct in the promotion, formation, management or liquidation of a company
- b. Wrongful trading (such as trading while insolvent)
- c. The directors fails to fulfill the requirements under the Companies Act legislation
- d. Failure to comply the competition law
- e. Individuals commit criminal offences (either in the UK or abroad) related to the promotion, formation, management or liquidation of a company.

Upon being issued a disqualification order, the director is not only suspended from exercising his power as director but he cannot act in the capacity as promoter or founder or in any managerial function in a company. Furthermore, the continuity of a directorship function after disqualification is a criminal offence and may make the director legally responsible for the debts of the company. In terms of sanctions, Lord Dillon LJ in the case of *Re Sevenoaks Stationers (Retail) Ltd (1990)* stated three distinct sets of the maximum disqualification period, being for:

- a. Serious cases : over ten years,
- b. 'Relatively not very serious' cases ; two to five years, and
- c. Cases which are not included under the first one; between six to ten years.

In addition, the CDDA categorizes the disqualification of directors as follows

- a. A disqualification period from 5 to 15 years for misconduct such as fraudulent trading.
- b. FOR unfitness a period of 2 to 15 years

The purpose of the CDDA includes the maintenance of integrity in the business environment and obligations are imposed on any persons who wish to become directors of limited companies to follow some criteria. The first aspect is the performance of their duties in an honest and responsible manner. The second is to ensure the compliance with relevant

laws and regulations and the third one is the use of appropriate skills and care so as reduces the risk for any conflict of interest between creditors, customers, shareholders and employees in the company. Director disqualification is a vivid and dominant tool to ensure the protection of the public against the abuse of privilege of limited liability. In addition, organizations like Limited liability partnerships (LLPs), Building societies and incorporated friendly societies also used the disqualification regime against the directors.

**2.1.3 Director undertaking**

Under the present law, director disqualification undertakings are divided into two instants. The first and most famous one is under Section 6 of the CDDA, where the proposition of the director disqualification proceedings are made following the insolvency of a company and secondly, under Section 8 of CDDA 1986, after the Secretary of the State investigate in a company.

In general, an undertaking is described as using the same process as in the administration of a disqualification order. It is a voluntary procedure which is entered without any court proceedings but has the same impact as a court order following the approval made by the Secretary of the State and it can only be enacted by the court. During the investigation, an undertaking can, at any time, be agreed by a director. Yet, refusal of the undertaking is possible if the Secretary of State is dissatisfied that, after considering all relevant information, it would unsuitable to accept such an offer. If, before court proceedings start, an acceptance for an undertaking is made, there will be no recovery of any costs for the investigation by the Insolvency Service.

Once the court proceedings commences, a director is still allowed to make an undertaking's offer and this will predict the court proceedings' ending. However, the director is still bound under the duty to pay the costs and expenses introduced in the procedures up to the date of the undertaking.

It is important to note that an undertaking allows the directors to 'put the matter of disqualification behind them' and continue. Moreover, a director may have their own independent professional advice if they face uncertainty as regards the offer of an undertaking.

**2.2 The Mauritius companies act 2001**

**2.2.1 Definition of Director**

Section 128(1) of the Companies Act defines a director as:

- a. Includes a person occupying the position of director of the company by whatever name called;
- b. Includes an alternate director; but
- c. Does not include a receiver.

**In other words, a "director" includes**

- a. A person in accordance with whose directions or instructions a person may be required or is accustomed to act;
- b. A person in accordance with whose directions or instructions the board of the company may be required or is accustomed to act;
- c. A person who exercises or who is entitled to exercise or who controls or who is entitled to control the exercise of powers which, apart from the constitution of the company, would fall to be exercised by the board; and

- d. A person to whom a power or duty of the board has been directly delegated by the board with that person's consent or acquiescence of the board.

For the purposes of the Companies Act, "board" refers to the directors of a company where the number is not less than the required quorum acting together as the board of directors.

### 2.2.2 Appointment and removal of directors

The Companies Act specify that all companies incorporated in Mauritius should have at least one director who shall be ordinarily resident in Mauritius. While no formal requirement exists with respect to the academic qualifications and experience of directors, section 133(2) of the Companies Act provides that no person shall be appointed or hold office as a director if he is a person who:

- a. Is under 18 years of age;
- b. In the case of a public company, over 70 years;
- c. Is an undischarged bankrupt;
- d. Is prohibited to act as director or promoter of or being concerned or taking part in the management of a company;
- e. Is not a natural person; or
- f. Has been adjudged to be of unsound mind.

The Act further specifies that the "first directors" are those whose name appear on the application for incorporation form at the time of registration of the company while the subsequent directors are appointed by ordinary resolution of shareholders unless otherwise provided for by the constitution of the company. Yet, no person shall be appointed as director unless that person has consented in writing to be a director and certified that he is not disqualified from being appointed or holding office as a director of the company. Section 136 of the Companies Act provide some specific instances whereby court may appoint directors, namely.

- a. Where there are no directors of a company or the number of directors is less than the quorum required for a meeting of the board; and
- b. If it is not possible or practicable to appoint directors under the company's constitution.

In such a case, the appointment is made on such terms and conditions as the court thinks fit.

The procedures for removing a director depends on the nature of the company. If the company is a private company, then the director may be removed from office by special resolution. On the other hand, if the company is public, then a director may be removed from office by an ordinary resolution. In addition, once a director of a public company has attained the age of 70, he is automatically removed from office unless the shareholders vote by ordinary resolution that such person shall be re-appointed as director until the next annual meeting.

Furthermore, section 139 of Companies Act provides that the office of a director shall be vacated if the person holding that office:

- a. Resigns;
- b. Becomes disqualified from being a director in accordance with section 133;
- c. Dies; or
- d. Otherwise vacates office in accordance with the constitution of the company.

### 2.2.3 Disqualification of directors in Mauritius

The Companies Act provides for two instances where directors may be disqualified to act in this capacity. Firstly, if a director no longer fulfils the requirement under section 133 to act as director, then he is automatically removed from office as per section 139 of Companies Act. Secondly, the commercial court in Mauritius is empowered to disqualify directors in the following circumstances, where:

- a) A person has been convicted of an offence in connection with the promotion, formation or management of a company or has been convicted of a crime involving dishonesty punishable on conviction with a term of imprisonment exceeding 3 months;
- b) A person has committed the following offences:
  - a. Persistently failed to comply with the Companies Act or Securities Act 2005 or where the company has failed to take reasonable steps to ensure compliance; or
  - b. Has been convicted in relation to the performance of his duties as directors,
- c) Within the period of 7 years before making of the application, a person to whom the application relates, was a director of 2 or more companies an in relation to each of those companies, that person was wholly or substantially responsible for the company for.
  - a. Being wound up
  - b. Ceasing to carry on business because of its inability to pay its debts as and when they fall due;
  - c. Having a receiver or manager of its property appointed; or
  - d. Entering into a scheme of compromise or arrangement with its creditors.

Once the order of the court has been issued, notice is given in the government gazette of the name of the person against whom the order is made. Any person who acts in contravention of this court's order shall commit an offence and shall on conviction, be liable to a fine not exceeding MUR 1 Million and to imprisonment for a term not exceeding 5 years.

### 3. Comparative study and recommendations

In Mauritius, the legal provisions on disqualification of directors do not provide for sanctions in terms of fines or imprisonment for the respective directors, unlike in UK where the CDDA does cater for these. As such, if a director is disqualified in Mauritius, the only sanction is that the latter is not capable of holding office as either a director, promoter or officer in a managerial capacity in any corporate body in Mauritius for such time period as may be specified in the court's order. It is only when the court's order is not followed that the director may be fined and imprisoned. This therefore begs the question as to whether Mauritius laws are too lenient for directors who will be tempted to commit fraudulent activities.

#### Further to the comparative study conducted with the CDDA, it is hereby recommended that

- An amendment to the Mauritius Companies Act should be made in order to make the laws more strict to ensure that director's duties are better enforced,

- The laws should impose sanctions on directors once a disqualification order has been given by the court on the ground of misconduct or fraudulent activities,
- The registrar of companies should be given disciplinary powers which implies that it is able to claim for the disqualification of a director in particular circumstances, and
- A specialised institution should be established and it should act as an independent body to monitor the activities of directors in Mauritius and request for disqualification of directors in some particular circumstances.

#### **4. Conclusion**

This paper has analysed the various provisions relating to directors in both the Mauritius Companies Act and the UK CDDA. A comparative analysis was made in order to assess the efficiency of the legal provisions relating to director's disqualification in Mauritius. It has been seen that the Mauritius Companies Act is a bit lenient when it comes to sanctioning directors who are convicted of misconduct or for being engaged in fraudulent activities. In such circumstances, the law requires that directors cease to hold office but no fine or imprisonment sanctions are provided for. Consequently, this paper suggest that the Companies Act be amended in order to make the legal provisions more strict to deter directors from involving in fraudulent activities.

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