COMPANY LAW REVIEW GROUP
an grúpa athbhreithnithe dlí cuideachtaí

Company Law Review Group

Annual Report 2013

March 2014

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Chairperson’s Letter to the Minister for Jobs, Enterprise and Innovation

Mr. Richard Bruton TD,

Minister for Jobs, Enterprise and Innovation

23 Kildare Street

Dublin 2

13 March 2014

Dear Minister,

It is my pleasure to present to you the Annual Report of the Company Law Review Group (the ‘Review Group’) for 2013.

It has been another eventful year for company law, most notable for the significant progress that the Companies Bill 2012 has made through the Houses of the Oireachtas. It has been no small feat for a Bill of such size and significance to pass through Second and Committee Stage within a year, and I believe that this was possible in part because there is a recognition by you and your colleagues in Dáil Éireann of the importance and the potential of the Bill. The members of the Review Group have followed the debates closely and have been pleased to see the level of interest in the Bill and the commitment to modernising our company law code. It was my privilege to assist in that process too by providing a number of briefings to the members of the Oireachtas Committee on the key provisions of the Bill.

As the Bill enters into its final Stages in the Dáil and onwards to Seanad Éireann, I along with other members of the Review Group will continue to be available to brief Deputies and Senators as required.

I would also like to acknowledge your efforts to bring one of our 2012 recommendations, on examinership, into effect with the enactment of the Companies (Miscellaneous Provisions) Act 2013. The Review Group believes that this has the potential to provide some cost savings for small private companies that could benefit from examinership whilst continuing to respect the constitutional rights of other stakeholders such as, for example, other small companies who might be creditors of the small company in difficulty. We look forward to seeing this new provision commenced and to reviewing its operation over time.

As the Review Group's Work Programme for 2012 and 2013 is now at an end, the enclosed Annual Report gives an account of our work for the full two years. It was a busy period. Alongside the work associated with the Companies Bill 2012, we played our part in the implementation of the Action Plans for Jobs for both 2012 and 2013, with recommendations on debt settlement for small private companies and on the criteria for qualifying for the audit exemption. In some areas, such as developing EU proposals, the Review Group was asked for advice on a more informal basis and I would like to acknowledge the willingness of my fellow members to make themselves available to the Department on that basis.

I would especially like to acknowledge the tremendous support and assistance provided by the Secretary to the Review Group, Ms. Sabha Greene, who has been of immense and invaluable help to me organising the Review Group's meetings and progressing our work programme.

Finally, I would like to thank you Minister for the support and encouragement that you give to us. The year began with your visit to the Review Group, where we spoke of the Companies Bill 2012, which had been published just a few weeks beforehand, and your plans for its passage through the Oireachtas. It has ended with a new 2013 Act and the 2012 Bill well on its way to the Statute Book. As I said at the start, it has been an eventful year.

Yours sincerely,

Dr Thomas B Courtney

Chairperson

1 Introduction to the Annual Report 2013

1.1 The Company Law Review Group

The Company Law Review Group ("The Review Group") was established under the Company Law Enforcement Act 2001 to advise the Minister for Jobs, Enterprise and Innovation ("the Minister") on changes required in companies' legislation with specific regard to promoting enterprise, facilitating commerce, simplifying legislation, enhancing corporate governance and encouraging commercial probity.

The Review Group is comprised of practitioners of company law and of company administration, representatives of business, unions, the accounting profession, and nominees of regulators and the Department of Jobs, Enterprise and Innovation ("the Department"). The Secretariat to the Review Group is provided by the Company Law Modernisation and Development Unit of the Department.

1.2 Highlights of 2012/2014

The Companies Bill 2012 was published on the 21st of December 2012. This was a significant milestone in the history of company law, as the Bill, the largest substantive Bill in the history of the State, will modernise our company law code and consolidate legislation from 1963 to the present.

The Review Group has devoted the majority of its efforts since its establishment to the preparation of this Bill and most of its recommendations from the past 12 years are given effect in the provisions. To mark the publication and to thank the Review Group for its many years of work on the formulation of the Bill, Minister Bruton attended a plenary meeting in January 2013. The Minister met most of the members at that event and spoke of his appreciation for the significant contribution that the Group has made to the development of Irish company law.

Since then, the Bill has completed the first three Stages of its parliamentary progress and is due to go to Report Stage [Dáil] in early 2014. A full update on the Bill is given in Chapter 4 of this Report.

Although the Companies Bill 2012 made significant headway through the Houses of the Oireachtas in 2013, the Government decided that there were a few issues that warranted urgent legislation. Accordingly, on the 11th of October the Minister announced that the Government had given its approval to the priority drafting of a Companies (Miscellaneous Provisions) Bill, with a view to getting it enacted by the end of 2013. One of the sections of that Bill gives effect to the Review Group's recommendation of 2012 to allow small private companies to apply directly to the Circuit Court for the appointment of an examiner. That Bill has since become law and an update on its status, together with a summary of its main provisions, is set out in Chapter 5 of this Report.

As well as contributing to the progress of these Bills, the Review Group worked on other issues, which are listed in the Work Programme for 2012/2014. For most of these items, the Review Group adopted comprehensive reports, with recommendations. These have been submitted to the Minister for his consideration and are each reproduced in full in Chapter 6 of this Annual Report.

1.3 Contact Information

The Review Group maintains a website, www.clrg.org, where it publishes all its reports. The website also lists the members and sets out the current and previous Work Programmes.

The Review Group's Secretariat also receives queries relating to the work of the Group and is happy to assist members of the public. Contact may be made either through the website or directly to –

Ms. Sabha Greene
Secretary to the Company Law Review Group
Department of Jobs, Enterprise and Innovation
Earlsfort Centre
Lower Hatch Street
Dublin 2

Tel: (+353-(0) 1) 631 2527

Email: sabha.greene@djei.ie

2 Membership of the Company Law Review Group

The Minister appointed the current members of the Review Group in May 2012, and their term of office runs to 31 May 2014.

In the course of 2013, Jim Byrne of the Revenue Commissioners completed several years of service on the Group, leaving to take up new duties within Revenue. He was replaced by Brian Boyle.

The full current membership is –

Dr. Thomas B. Courtney	Chairperson
Deirdre-Ann Barr	Minister's Nominee
Brian Boyle (replaced Jim Byrne in 2013)	Revenue Commissioners
Jonathan Buttimore	Office of the Attorney General
Marie Daly	Irish Business and Employers' Confederation
Helen Dixon	Registrar of Companies
Mary Doyle	Irish Banking Federation
Stephen Dowling	Bar Council of Ireland
Ian Drennan	Director of Corporate Enforcement
Paul Egan	Minister's Nominee
Mark Fielding	Irish Small and Medium Enterprises Association Ltd.
Joseph Gavin	Central Bank of Ireland
Michael Halpenny	Irish Congress of Trade Unions
Tanya Holly	Department of Jobs, Enterprise and Innovation
Brian Hutchinson	Minister's Nominee
William Johnston	Minister's Nominee
Brian Kelliher	Irish Funds Industry Association

Aisling McArdle	Irish Stock Exchange
Ralph MacDarby	Institute of Directors in Ireland
Vincent Madigan	Minister’s Nominee
Kathryn Maybury	Small Firms Association
Conall O’Halloran	Consultative Committee of Accountancy Bodies – Ireland
John O’Malley	Irish Auditing and Accounting Supervisory Authority
Mark Pery-Knox-Gore	Law Society of Ireland
Nóra Rice	Companies Registration Office
Jon Rock	Institute of Chartered Secretaries and Administrators
Noel Rubotham	Courts Service
Conor Verdon	Department of Jobs, Enterprise and Innovation

Sabha Greene	Secretary – Department of Jobs, Enterprise and Innovation

Some members have nominated alternates for specific periods of time or areas of work, and they have often made a significant contribution to the Review Group’s work. They are –

Anthony Collins	Institute of Directors in Ireland
Noel Gaughran	Irish Banking Federation
Brian Higgins	Irish Funds Industry
Marie Hurley	Revenue Commissioners
Aidan Lambe	Consultative Committee of Accountancy Bodies – Ireland
Esther Lynch	Irish Congress of Trade Unions
Theresa O’Connor	Central Bank of Ireland
Conor O’Mahony	Office of the Director of Corporate Enforcement
Kevin Prendergast	Office of the Director of Corporate Enforcement

Over the course of its 2012 / 2014 Work Programme, the Review Group received assistance from several people. In particular, it would like to thank the following for their time and advice –

Chris Bollard, Arthur Cox

Gina Conheady, Matheson

Naomi Clohisey, Department of Jobs, Enterprise & Innovation

Marie Dempsey, Department of Jobs, Enterprise & Innovation

Aoife Kavanagh, Department of Jobs, Enterprise & Innovation

Philip McDonald, Department of Jobs, Enterprise & Innovation

Kieran McGarrigle, Arthur Cox

John Moynihan, Department of Jobs, Enterprise & Innovation

Tom Murphy, Revenue Commissioners

Eamonn Richardson, KPMG

3 Implementation of the Work Programme 2012 - 2014

3.1 Introduction

The Minister, following consultation with the Review Group, determines the programme of work to be undertaken by the Review Group, again on a two year cycle. The current Work Programme was adopted in March 2012 for the period 2012 – 2014. Later, in March 2013, the Minister asked the Review Group to add a new item (now Item 8) to the Programme following a commitment made in the Action Plan for Jobs 2013.

Over the course of 2012/2014, the Review Group met 7 times in full plenary, more than 15 times in Committee format, and adopted 4 detailed reports, all with recommendations. As the Work Programme comes to an end, an account of its overall implementation is here in Chapter 3, while each of the reports that were adopted during the two years is included separately and in full at Chapter 6 below.

As the current Work Programme is coming to an end, this Annual Report accounts for the full two year period.

3.2 Content of the Work Programme 2012-2014

The Work Programme is as follows –

Priority Items

1. Provide ongoing advice to the Department of Jobs, Enterprise and Innovation on the preparation and drafting of the Companies Bill [now the Companies Bill 2012], including responding to queries raised by the Parliamentary Counsel and assisting the Department in advising the Minister in matters arising in the course of the initiation and passage of the Bill through the Houses of the Oireachtas.

2. Examine and make recommendations on the feasibility of amending the Companies Acts to introduce a new structured and non-judicial debt settlement and enforcement scheme for insolvent companies.

Other Items for Consideration

3. Examine and make recommendations on whether it is necessary or desirable to provide for amendments to the legislation transposing Directive 2005/56/EC on cross border mergers into Irish law.

4. Examine and make recommendations on whether it is necessary or desirable to provide for amendments to the law relating to the representation of a company before the Courts.

5. Examine and make recommendations on whether it is necessary or desirable to adopt, in Irish company law, the UNCITRAL Model Law on Cross-Border Insolvency.

6. Examine and make recommendations on the need for amendments to the Companies Acts' provisions regarding the re-use of CRO information, having particular regard to –

    - Consideration of the interaction between data protection laws and the CRO's use of personal data

    - Examine possibilities for identity theft and other crimes using information gleaned from the CRO Register

    - Examine the onward sale of data to 'bulk data customers' of the CRO taking into account the impact of the ECJ's decision in the *Compass Datenbank* case and the Re-Use of Public Sector Information Regulations

7. Provide ongoing advice to the Department of Jobs, Enterprise and Innovation on EU proposals, as requested by the Department.

8. Examine the possibility of allowing companies to qualify for the audit exemption where they meet 2, rather than all 3, of the criteria [added in March 2013].

3.3 Report on implementation of the Work Programme

The Review Group made itself available to the Department on issues arising from the Companies Bill 2012 and from the EU's programme of company law and corporate governance reform, on an ongoing and regular basis, with members providing advice to the Department as required. In the case of the Companies Bill 2012 (Item 1), this included providing detailed briefings for members of the Houses of the Oireachtas and assisting in responding to queries and issues that arose in the course of the Bill's parliamentary progress. In the case of EU law (Item 7), members of the Review Group advised the Department on proposals concerning insolvency and money laundering.

For 4 of the remaining items, the Review Group established Committees to examine those in depth and report back to the Review Group in full plenary session, where it considered the issues and adopted final reports. Those items were –

Item	Report & Recommendations adopted
Item 2	September 2012
Item 3	January 2013
Item 6	January 2013
Item 8	September 2013

While a Committee was established for Item 4 and began its deliberations in the course of 2013, it did not prove possible to complete its work before the end of the current Work Programme. As a result, the Review Group will propose that the Minister carry this item over to the next Work Programme, which will begin in 2014.

A full list of the Committees that examined these items, their Chairpersons and Members is set out at Appendix 1 to this Report.

There were developments both nationally and within the EU on insolvency law during the period of this Work Programme, with more expected in 2014. These could have an impact on the implementation of the UNCITRAL Model Law on Cross-Border Insolvency (Item 5). Moreover, the Review Group is in consultation with the Department on aspects of implementation, and these contacts will require more time. As a result, the Review Group will propose to the Minister that he carry this item over to the next Work Programme, starting in 2014.

4 Progress of the Companies Bill 2012

The Companies Bill 2012 was published on the 21st of December 2012. This was a significant milestone for the Review Group in particular as it had dedicated most of its efforts since its establishment to the making of the General Scheme of the Companies Consolidation and Reform Bill (published March 2007), on which the 2012 Bill is based, and, after that, to working with the Parliamentary Counsel on the drafting of the Bill.

The Bill began its progress through the Houses of the Oireachtas with Second Stage debate in Dáil Éireann taking place over two days, the 23rd and 25th of April 2013. In his speech introducing the Bill to the Dáil, Minister Bruton said –

> "…I am delighted with the significant benefits which the [Companies] Bill [2012] will bring to all companies, big and small, across the country. It will make it easier to run a business as a company. An entrepreneur will be able to start a company with a single director. Time will not need to be spent on convening and holding a formal AGM. There will be no need for ordinary businesses to be tied up with objects clauses and articles of association, although the Bill will retain those concepts for those companies that need them.
>
> "This Bill will enhance Ireland's competitive position as a place in which to start or to grow a business. Indeed it will feed directly into the Government's aim to make Ireland the best small country in the world in which to do business….I believe it will bring significant benefits to companies and to business life in Ireland."

Subsequently, the Companies Bill was passed by the Select Committee on Jobs, Enterprise and Innovation on the 6th of November 2013. That Committee made 143 amendments to the Bill, many of them technical in nature. The next Stage, Report Stage, is expected to take place in the Dáil in early 2014.

Since the publication of the Bill, members of the Review Group have remained available to provide expert advice to the Department whenever queries arose, and to give briefings to members of the Oireachtas in advance of debates. The Minister acknowledged this contribution in public when he said at the Second Stage [Dáil] debate –

> "The Bill is the culmination of many years of work by my Department and the Company Law Review Group, the CLRG, [and] I wish to take this opportunity to thank the members of the CLRG for the sterling work they have done in shaping the Bill before the House today….Their interest in this work has endured [from] the start of the lengthy process [to] having this legislation passed."

5 The Companies (Miscellaneous Provisions) Act 2013

5.1 Publication of Companies (Miscellaneous Provisions) Bill 2013

As the Companies Bill 2012 was making headway through the Houses of the Oireachtas, the Government decided to "fast track" some of the provisions in a smaller Bill with a view to getting those provisions enacted by the end of 2013. These provisions included the Review Group's recommendation of 2012 to allow small private companies to apply directly to the Circuit Court for the appointment of an examiner.

Accordingly, on the 14th of November 2013, Minister Kathleen Lynch, on behalf of Minister Bruton, introduced the Companies (Miscellaneous Provisions) Bill 2013, in Seanad Éireann. The purpose of this Bill is to bring forward a few provisions that are designed to support businesses in advance of the enactment of the Companies Bill 2012, which, given its size, may take several more months to complete its passage through the Oireachtas.

5.2 Provisions of the Bill

The main sections are –

- Section 2: Allows small private companies to apply directly to the Circuit Court, rather than first to the High Court, for examinership.
- Sections 3 and 4: Provisions for simplification of the electronic filing requirements of the Companies Registration Office
- Section 5: Facilitates the disclosure by certain regulatory authorities to the Director of Corporate Enforcement of information relating to offences under the Companies Acts
- Section 6: Introduces a levy on statutory auditors and audit firms of Public Interest Entities to defray the costs of the Irish Auditing and Accounting Supervisory Authority for carrying out the functions of external quality assurance
- Section 7: Applies investigation and penalty systems to certain third country auditors and audit entities who carry out audit on companies incorporated in specific third countries and territories

5.3 Enactment of the Bill

The Bill passed all stages in the Houses of the Oireachtas on 18 December 2013 and was signed into law as the Companies (Miscellaneous Provisions) Act 2013 by President Higgins on 24 December 2013. Section 5 on disclosure of information to the Director of Corporate Enforcement came into operation on the same day as the Act, while the remaining sections will require a Ministerial Order before being commenced. All provisions of this Act will be carried over into the Companies Bill 2012.

6 Review Group's Reports on Work Programme Topics

6.1 Report on Item 2 – Debt settlement Arrangements for Small Private Companies

Item 2 Report – Introduction

On foot of the Government's Action Plan for Jobs 2012, the Minister asked the Review Group in March 2012 to examine and make recommendations on the feasibility of amending the Companies Acts to introduce a new structured and non-judicial debt settlement and enforcement scheme for insolvent companies. Accordingly, the topic was added to the Review Group's Work Programme, placed as a priority item.

The Review Group began its deliberations with a full plenary meeting in May 2012, where it heard presentations from three experts on developments in Irish insolvency law, the practical experience of corporate insolvencies, and on the non-judicial commercial voluntary arrangements that operate in the UK. It then established a Committee, chaired by William Johnston, to examine the issues in more depth and report back to the full Group.

The Review Group adopted its final report, with recommendations, at a plenary meeting in September 2012 and submitted it to the Minister shortly after. The full text of that report is reproduced below. Two of the recommendations have since been brought into law in the Companies (Miscellaneous Provisions) Act 2013.

It should be noted that, at the time of the report's adoption, the Personal Insolvency Act 2012 was not yet enacted and, therefore, the Insolvency Service of Ireland was not established. Therefore, references to the Personal Insolvency Bill 2012 and the "new Insolvency Service" in the report should be read accordingly.

Executive Summary of Findings and Recommendations

Findings

1. The Review Group considers that examinership, in the form currently available to small private companies (SPCs), is inadequate by reason of the costs involved which are prohibitive.

2. The more effective a rescue system is in writing down debts owed by an ailing business, the more likely it is that other businesses (perhaps better managed and more deserving of survival) will receive less that they are owed such that their own solvency may be endangered.

3. It is essential that giving an unfair competitive advantage to companies through an examinership must be avoided. Although there will always be companies which fail – examinership is not a process to be used to prop up economically unviable companies. Winding up insolvent companies should always be the default position.

4. The test of a company's "reasonable prospect of survival" is considered essential to any corporate rescue regime.

5. Significant jurisprudence has been developed by the Superior Courts in relation to the interpretation and application of the Companies (Amendment) Act 1990.

6. In Ireland, our Constitution requires that any compulsory write down of debts for less than market value requires compensation for the loss, consent of the creditors or a court order whether by substantive approval of a scheme of arrangement or a right of objection to the Court for dissenting creditors.

7. Other jurisdictions that permit non-judicial procedures to compulsorily write-down third party debt may not be subject to the same constitutional restraints concerning the writing-down of property rights as are provided for by the Irish Constitution.

8. There are no constitutional, legal or conceptual obstacles to extending the jurisdiction of the Circuit Court to permit all aspects of examinership law for SPCs, as contained in the Companies (Amendment) Act 1990, to be brought and determined by the Circuit Court.

9. In considering a non-judicial mechanism for corporate rescue, it is possible to distinguish between the approval of a scheme of arrangement or compromise of debts (which requires *judicial sanction*) from the initiation of an examinership through the appointment of an examiner (which can happen by administrative act) with limited judicial oversight.

10. Were it to be decided, in the case of an SPC, to allow the initiation of an examinership by the appointment of an examiner by administrative, instead of judicial act, some State agency would need to be charged with responsibility for that process.

11. While a number of agencies exist (ODCE, CRO, IAASA etc) the proposed *Insolvency Service* to be established by enactment of the Personal Insolvency Bill 2012 would, given its proposed purpose and functions, appear to be best suited to making an administrative decision that a particular SPC might have a reasonable prospect of survival were an examiner appointed to it. However it is understood that the proposed agency will face significant challenges in establishing capacity to carry out the remit envisaged for it in the Personal Insolvency Bill, that it also faces potentially significant challenges in meeting demand for the proposed new personal insolvency remedies, and that, by virtue of the State's

commitments to the IMF and EU under the Programme of Financial Support for Ireland, priority attaches to the effective implementation of the reform of the personal insolvency regime.

Recommendations

1. **Amendment of existing examinership provisions for small private companies -** That small private companies, within the meaning of section 8 of the Companies (Amendment) Act 1986 should be able to apply directly to the Circuit Court to have an examiner appointed, and not be required to apply to the High Court although that should remain an option. This could be implemented as a stand-alone solution in a timely manner (as the legislative change required is not vast) and would have the immediate impact of lower costs and greater accessibility for SPCs in that it eliminates the requirement for any High Court involvement with associated costs.

2. **Introduction of simplified administrative initiation of examinership for small private companies** – That, subject to the identification of an appropriate agency, and further analysis and deliberation on the policy issues, it appears to the Review Group that it would be legally possible for small private companies to be given an alternative option to traditional examinership, whereby they can initiate the application to be placed into examinership by availing of a non-judicial administrative procedure. The simplified procedure should only extend to the appointment of an examiner. Any scheme or proposal formulated by the examiner must be approved by the Circuit Court.

3. **Possible extended role of new Insolvency Service** - That policy consideration should be given at an appropriate juncture to the practicability of extending the role of the new *Insolvency Service*, proposed to be established following the enactment of the Personal Insolvency Bill 2012, to include the administrative determination as to the initial appointment of an examiner to an SPC, having regard to the priority requiring to be given to the mandate concerned for that agency under the Bill.

4. **Law applicable to small company examinerships -** That with certain limited exceptions (e.g. a shorter initial period of protection, a higher majority of creditors being required to agree to a scheme and possible right of appeal to the High Court of creditors with significant liabilities written down) the provisions of the Companies (Amendment) Act 1990 as interpreted and developed by the Superior Courts, should be applied, mutatis mutandis, to all other aspects of an examinership that is initiated by simplified administrative act.

5. **Examinership in the High Court –** That medium sized companies should continue to have the option of applying for the appointment of an examiner in the High court.

The full Review Group met on 27 September 2012 to consider the recommendations of the Committee and by a significant majority, the ODCE and

Revenue Commissioners expressing reservations, the Review Group approved this report. Revenue stated their view that the proposed approach (in recommendation 2) constitutes a new mechanism, entirely distinct from the established examinership process and, accordingly, that different considerations – including as regards the treatment of tax debts – should, in the view of Revenue, necessarily apply (see sections 7 and 13(10) below).

2. The Minister's request, the Terms of Reference and the Approach of the Review Group

The Minister for Jobs, Enterprise and Innovation has requested the Company Law Review Group ('The Review Group') to examine the feasibility of introducing a new structured and non-judicial commercial debt settlement and enforcement system.

This request is made in the context of the commitment contained in the Programme for Government to introduce new legally binding voluntary commercial debt plan structures to allow small business to restructure debts without recourse to expensive court procedures.

Similarly, the Action Plan for Jobs, which was launched in mid-February, contains a commitment to examine the feasibility of introducing a new structured and non-judicial debt settlement and enforcement system to meet SME needs – this has been referred to as "Examinership Light".

In the context of advancing the commitments in the Programme for Government the Minister wished to have the considered views of the Company Law Review Group as to the potential benefits or challenges from a company law perspective of advancing proposals in this regard. Accordingly, the Minister asked the Review Group to examine the appropriateness of introducing a legally binding non-judicial commercial debt and enforcement system, to be used by small and medium sized businesses ("SMEs") into the Companies Acts, and set out a number of factors to be taken into account. The full terms of reference are in Appendix 1 to this report.

The Review Group approached its task by establishing a Committee chaired by Mr William Johnston. Membership of the Committee was open to all members of the Review Group who expressed an interest in this matter and the Committee met on five occasions from June 2012 to September 2012 to consider the matter set out in the Minister's terms of reference. The Committee included a number of alternate members and others with expertise of the area and its membership is set out below [See Appendix 1 of the full Annual Report].

The full Review Group met on 27 September 2012 to consider the recommendations of the Committee and by a significant majority, the ODCE and Revenue Commissioners expressing reservations, the Review Group approved this report. Revenue stated their view that the proposed approach (in recommendation 2) constitutes a new mechanism, entirely distinct from the established examinership process and, accordingly, that different considerations

– including as regards the treatment of tax debts – should, in the view of Revenue, necessarily apply (see sections 7 and 13(10) below).

3. Background and History of Examinership

The Review Group approached the Minister’s request mindful of the effects of the most serious economic downturn in the history of the State on business. When a business becomes insolvent, by definition there is insufficient money to go around and pay off its creditors. The default position in such cases is that it is wound up and its creditors are paid, if anything, so many cent for every euro owed by the company. Where rescue legislation, such as examinership, can be invoked, the company is allowed to continue in existence but the cost is that its creditors’ debts are written down, such that they are owed less than they would otherwise be entitled to receive. Ironically, the more effective a rescue system is in writing down debts owed by an ailing business, the more likely is it that other businesses (perhaps better managed and more deserving of survival) will receive less than they are owed such that their own solvency may be endangered.

Whereas the process of court protection or examinership, first introduced by the Companies (Amendment) Act 1990, has operated effectively and has saved a number of ailing businesses, the compromising of lawful claims has come at a cost in the form of sometimes significant advisory fees (e.g. legal, accounting, etc) incurred by the creditors and others whose rights are to be impaired. The reality is that every creditor will legitimately seek to ensure that the write-down of what is owed to them is minimised which requires them to retain advisors to advise on whether what is being proposed in the scheme is legal, fair, reasonable and proportionate.

The Minister’s proposal for a legally binding non-judicial commercial debt and enforcement system was made in this context and the challenge faced by the Review Group was to determine whether such a system was legally and constitutionally possible in an Irish context.

The only report to consider the benefit or otherwise of examinership is the Company Law Review Group's report of December 1994 which states at paragraph 2.7:-

> “In looking at the examinership legislation and its application to date we sought to identify the justification for setting aside, in the hope of securing the future of an ailing company, normal commercial rights and interests. Examinership involves a cost which has to be borne, principally by creditors but also by competitors. The justification for the introduction of the legislation must lie within the concept of the public interest – that the benefit accruing to a wider group justifies the impairment of the rights of others".

The Review group’s Report of 1994 highlighted that of 64 companies having examiners appointed, 32 subsequently resulted in a receivership or liquidation (the figures excluded the three largest groups of companies subject to examinership).

The Companies Registration Office has indicated that in 2008, 49 companies went into examinership of which 24 had a scheme of arrangement approved by the Court and then successfully emerged from the process, an almost identical ratio to the process of the early 1990s. However since 2008, the outcome of examinership has been more encouraging (notwithstanding that the figures do not take account of companies having come through the examinership process successfully, ultimately failing at a later stage):-

	Examinership	**Successfully exited Examinership**	**Success ratio**
2009	84	61	73%
2010	29	21	72%
2011	30	21	70%

The increased success ratio could in part be attributed to the recommendations of the 1994 Review Group as introduced by the Companies (Amendment) Act 1999, requiring an independent accountant's report to be prepared for the court to assist in its assessment whether the company (or part of it) by going into examinership has "a reasonable prospect of survival", rather than the less onerous requirement under the 1990 Act of a company (or part of it) requiring to show "some prospect of survival".

The recommendations in the 1994 report were prescribed in recognition of the presumption that creditors will have their debts written down to a greater, or lesser, extent in an examinership. This can have an adverse financial effect on suppliers, particularly the smaller ones who may, themselves, face insolvency if what is owed to them is written-down. In addition, the ability to write-down debts accrued in the course of running a business can distort competition with those competitors who discharge their liabilities in full being placed at a considerable disadvantage. The justification for examinership must, therefore, be founded on the presumption that saving the whole or part of the business involved accrues benefits for society as a whole, best exemplified by the protection of employment, that outweighs the costs suffered by creditors and competitors.

4 Relevance of Examinership to SMEs

Overall, the Review Group considered that there is a difficulty with smaller companies accessing the existing examinership procedures – primarily for cost reasons – and that there is scope for improving access for such companies to court protection and corporate rescue.

However, it is also recognised that any non-judicial debt settlement arrangements open to any category of companies carries the potential for significant loss to creditors whether they be employees, the Revenue Commissioners, local authorities, utility enterprises, lenders or trade creditors. This is clearly not desirable. The difficulty encountered in other jurisdictions in creating robust models highlights the need to ensure there are adequate safeguards, particularly where court oversight is diminished.

It is generally seen that SMEs, which are often family owned and managed, are less likely to attract new investment, which in many cases is essential for the continued viability for companies post examinership.

The Review Group heard anecdotal evidence that some companies which went into examinership did so solely to mitigate their debts. It is important to avoid the "phoenix company" scenario, bearing in mind that Part VII of the Companies Act 1990 was enacted to counter the "phoenix company". It is essential that giving an unfair competitive advantage to companies through an examinership must be avoided. Although there will always be companies which fail - examinership is not a process to be used to prop up badly managed or economically unviable companies. Winding up insolvent companies should always be the default position.

The principal issues which were identified, discussed and considered by the Review Group were:

- Difficulties in establishing the future viability of the whole or part of the business;
- Absence of any source of additional funding for the company;
- Absence of likely interest from new owners/managers to become involved in the business (possibly reflecting a reluctance on the part of present ownership management to cede control of the business in some cases);
- Costs of the process.

These factors would apply to all companies in financial difficulty but may be more pronounced in the case of SMEs, especially when dealing with family owned businesses. The group identified cost as a particular obstacle for small businesses.

The option of replacing the management of the company for the duration of the examinership, or providing some external oversight was considered but is likely to work only in certain cases and may not be practical for most smaller, family run businesses. Related to this would be the option of having a temporary, non-executive director to sit on the board. However, it is considered unlikely to think that persons with the appropriate skills, experience and judgment would agree to become a director of a failing company in such circumstances. It could be made more attractive by absolving such persons from some of the personal liabilities for directors, but they would still be required to act responsibly. It is also likely that such persons would require to be reasonably remunerated for taking on such a role and that given the highly pressurised nature of the role and the attendant risks, a premium would be required on what would normally be charged in such circumstances. In proposing solutions for ailing companies, the Review Group is mindful of the shortage of finance.

The possibility of using a service akin to the Financial Services Ombudsman was considered. However, it was felt that a similar arrangement would still need a right of appeal/judicial review, which is costly. The possibility of re-establishing a state bank was discussed. However, it was indicated this was not favoured at the time examinership was brought into Irish law (when Foir Teoranta was wound down) and this could now give rise to EU State aid issues which could be resolved only on a case by case basis which would not be practical.

5 Costs

While the Review Group was not in a position to review actual cost data for examinership, it was agreed that currently examinership is not generally a possibility for many SMEs due to the cost associated with the High Court procedure. Figures of up to €300,000 have been indicated for the cost of an examinership although there are also cases where costs came in at much less than that. The main reason for the extent of costs is the need for the preparation of an independent accountant's report, a number of High Court hearings during the examinership process and the costs of the examiner during the 70 or 100 day protection period. It was accepted that there will still be professional fees involved for the accountant's report and the examiner (and his or her advisors), but that if the fees are reduced by spending less time in court and being able to avail of the Circuit Court without first having to apply to the High Court (as is currently the position) and the maximum protection period reduced for SMEs, this could open up examinership to SMEs.

It was understood that costs could be reduced if the number of times a party has to apply to court was reduced. In particular, High Court hearings result in significant legal fees. It should be kept in mind that if costs are to be reduced, input from professional advisors and court involvement need to be curtailed – this could adversely affect the quality of examinerships.

The Review Group noted that the legislation already empowers the Circuit Court to oversee the examinership process. However, the application must first be submitted to the High Court and then be remitted to the Circuit Court. Furthermore, the case can be remitted to the Circuit Court only if the total liabilities of the company (taking into account its contingent and prospective liabilities) are less than €317,434.52 (though the draft Companies Bill envisages this threshold being increased to €500,000).

The Review Group considered that the costs of applications which are heard before the Circuit Court would, in all probability, be lower than if heard in the High Court. However, the group was not able to form a view on the extent of any such reduction in costs. Having regard to the fact that costs were identified as an obstacle to access to the examinership process, particularly for smaller companies, the Review Group was anxious to identify any opportunities to reduce costs while still not compromising the integrity of the process.

Against this background, the Review Group considered that the existing and, indeed, the revised threshold for access to the Circuit Court is too low. Rather than attempting to determine an appropriate level at which access should be possible, the Review Group agreed that it should recommend that access to the Circuit Court for examinership applications should be extended to all small private companies, as defined in the Companies Acts. Furthermore, the Review Group felt that the requirement for applications to be filed initially with the High Court should be dispensed with, as is considered further in point 12.

Although the Circuit Court does not currently have direct experience of corporate insolvencies, it was noted that it was planned to give the Court a role in the new personal insolvency regime. Accordingly, the Court could be expected to quickly build a level of expertise in the type of issues arising in insolvency proceedings.

6 The need for judicial oversight

It was noted that some other jurisdictions have dispensed with the need for court involvement (New Zealand) and others do not require court involvement to enter the process, but only to approve the proposals upon exiting examinership (Canada). It was noted, however, that compulsory interference with property rights which are expressly protected under the Irish Constitution and any compulsory write down of debts for less than market value requires either compensation for the loss, consent of the creditors or a court order whether by substantive approval of a scheme of arrangement etc. or a right of objection to the Court for dissenting creditors. This is to ensure that there is a proportionate and objectively justified interference with the creditors' property rights in the interest of the common good and to respect the constitutional right to fair procedures. The advantage of court involvement is that there is a built-in judicial process for protecting the constitutional rights of debtors and creditors.

There need to be adequate safeguards and balances to protect the rights of both creditors and debtors in any system that compulsorily writes down debts. Any compulsory interference with property rights requires an objective policy justification in the first instance and then has to be assessed as to whether it is a necessary and proportionate means to achieve that purpose. Write down of debts without consent or court order could be regarded as an unjustified and disproportionate interference with property rights in contravention of Article 40. The main concern for any court in considering any constitutional challenge will be to:

(a) identify the extent to which minority secured creditors' rights who did not consent to the debts write down have been impaired

(b) establish whether there is an objective justification for this impairment, and

(c) assess whether there are adequate safeguards and protections in any legislative scheme to minimise the adverse impact that the scheme will have upon secured creditors' rights.

The crux of the impairment of minority secured creditors' rights is the possible requirement of a minority creditor to crystallise its security immediately and take a write-down of debt without Court involvement. A secured creditor adversely affected (in its view) by any scheme of arrangement which requires it to accept the immediate sale of the property of which it has a security and which requires it to accept a write-down of its debt (albeit to a sum no less than the value of its security) may challenge the constitutionality of such a system. It is noted that the courts have shown great willingness to interpret legislation to protect the constitutional and property rights of individuals and companies. It is not possible to predict with any certainty the attitude that the courts would take to this proposal and the facts of any particular case. This is emphasised by the fact that the Personal Insolvency Bill is not yet enacted nor has any model under the Bill been tested in the Courts [As mentioned in the introduction, the Personal Insolvency Bill was enacted in December 2012, subsequent to this report]. If the Review Group's proposal is accepted by Government for enactment, legal and drafting advice would be required from the Attorney General's Office on the final form of the proposal to ensure compliance with the Constitution.

It was considered that compulsory interference with property rights which are expressly protected under the Constitution and any compulsory write down of debts for less than market value requires either compensation for the loss, consent of the creditors or a court order whether by substantive approval of a scheme of arrangement etc. or a right of objection to the Court for dissenting creditors. This is to ensure that there is a proportionate and objectively justified interference with the creditors' property rights in the interest of the common good and to respect the constitutional right to fair procedures. This interference with secured creditors' rights occurs not only on a compromise or scheme of arrangement at the conclusion of an examinership, but also at the commencement of an examinership where creditors' rights for the enforcement of debts owing to them are stayed. Thus court involvement is a pre-requisite both at the beginning and end of the protection period. The advantage of court involvement is that there is a built-in judicial process for protecting the constitutional rights of debtors and creditors. The court would not sanction an unconstitutional scheme of arrangement – i.e. one which infringes the rights of a party to the extent that it is excessive, disproportionate or unfair.

7 Appointment of an Examiner

A test of a company's "reasonable prospect of survival" was considered essential to any regime. There is a view that in a number of cases it has been too easy to pass the reasonable prospect of survival test at present. This appears to have arisen not from the approach of the Court but from the outcome and manner in which the independent accountant's report is prepared and presented. It was noted that a consequence of a company entering examinership is not only to give a temporary and hopefully long term reprieve for employees of the company but also a write down of debt owed to suppliers thereby putting the business and employees of suppliers at risk. If examinership is obtained by a company which would otherwise go into liquidation, the write off of debt owed to suppliers may ultimately be more significant if the company subsequently enters liquidation, as the company would have wasted its meagre resources on professional fees incurred in obtaining and going through an examinership.

It was also considered whether an event stipulated in a list of exceptional circumstances which may occur in an SME that could trigger examinership – e.g. collapse of major customer; death or incapacity of principal shareholder/director; sudden interruption of business etc. However, it was felt that it would be too difficult to prescribe these events in the legislation.

8 Priority of claims

Since the introduction of examinerships, the Courts have developed a consistent approach as to the extent and relative percentage write down of debts in approved schemes of arrangement. Different approaches have been developed for secured, preferential, unsecured and subordinated creditors. It is suggested this approach would continue for SMEs undertaking examinership through the Circuit Court.

However, the Revenue Commissioners disagreed on this point. They were strongly of the view that the Review Group proposal is for a new mechanism, entirely distinct from the existing examinership process. They see it as being, in reality, closely aligned to the debt settlement arrangements provided for in the Personal Insolvency Bill and contend that there is an overlap between the type of businesses that may have recourse to the personal insolvency regime as sole traders and the small companies that may seek protection under this proposal. That being the case, the Revenue Commissioners argue that there should be similar treatment of debts under both arrangements. In particular, they consider that those debts that are specifically excluded from the personal insolvency arrangements (unless the relevant creditor agrees in writing to accept the compromise on offer) should be similarly excluded here. Excluded debts in that context would include taxes, duties, levies and other charges owed to the State.

The view of the majority of the Review Group's members was, however, that while it is suggested that the proposed *Insolvency Service* could play a role in the administrative decision to appoint an examiner, this was the only relevant similarity with the Personal Insolvency Bill 2012. The Review Group proposes that save in respect of the initial appointment of an examiner, with minor more restrictive modification the law applicable to the carriage of the examinership should be based on existing law. A majority of the Review Group did not consider that there was any basis in principle to distinguish a scheme approved by the Circuit Court following the appointment of an examiner by administrative act from a similar scheme approved by the Circuit Court or High Court where the examiner is appointed following an application made to that court. Consideration of a new system of priority or increased preference for categories of creditors of insolvent companies whether for employees, the Revenue, local authorities, utility enterprises, lenders or trade creditors would be best undertaken by a separate review.

9 Licensed or qualified insolvency practitioner

The Personal Insolvency Bill introduces the concept of a licensed insolvency practitioner. On the other hand, the draft Companies Bill proposes to introduce a qualification regime for liquidators, and this qualification regime will apply also to examiners. The intention here is to ensure so far as reasonably possible that the independent accountant's report on the company filing for examinership (as well as the scheme ultimately proposed to creditors) is prepared in an appropriately objective manner to minimise the risk that the company will obtain protection on foot of a report which on its face appears adequate but which in fact gives a misleading picture as to a company's prospects of survival.

Concern was expressed that a licensing or qualification system which is primarily linked to membership of professional bodies, without a mechanism for investigation of competence and independence in the exercise of insolvency – specific functions, has its limitations as a means of enforcing standards in the specific field of insolvency practice.

It was noted that the new Companies Bill links examinership with the new qualification regime for liquidators. The view was expressed that effective regulation of insolvency practitioners requires that a designated regulator have the power to both authorise and strike off practitioners and, in that context, to investigate complaints from interested parties as to the extent to which practitioners have fully discharged their responsibilities in individual cases. Regarding qualification/licensing arrangements, the accountancy profession has signalled that they may have to increase their fees if there is a qualification requirement.

The Review Group considered that a reduced court involvement may need to be balanced by additional protections, such as closer regulation of insolvency practitioners, in order to provide the assurance of independence and professional competence traditionally provided by court oversight of examinerships.

10 Approach of other jurisdictions

In approaching the issues, the Review Group considered systems adopted in some other jurisdictions, which may be summarised as follows:-

Australia – A voluntary administration procedure may be initiated by the company without any court involvement. The administrator must be a qualified liquidator registered with the Regulator.

The administrator will put forward a proposal on which the creditors must vote at a meeting. A secured creditor is not required to be bound by the vote but if the secured creditor's dissent threatens the restructuring, the court may require the creditor to refrain from enforcing its security.

In many cases the court will have no involvement but it will intervene to prevent abuse.

Canada – This involves a licensed trustee in bankruptcy filing a proposal with the Office of the Superintendant of Bankruptcy whereupon creditors' claims are stayed. There is no court involvement for this stage.

A meeting of creditors is convened by the trustee at which the company will make its proposals for a debt settlement. If the proposal is accepted by the creditors it must then be approved by the court.

France – There are two procedures for insolvent companies. Under the conciliation procedure a conciliator is appointed to the company whose management remains in control. The role of the conciliator is to negotiate a voluntary arrangement with the creditors, all of whom must agree.

Under the *redressement judiciare* a petition is filed with the court. An administrator is appointed and has six months to devise a plan with a stay on creditors in the meantime with management remaining in control. The court approves the arrangement.

Hong Kong – The procedure involves a compromise between the company and its creditors which is subject to the sanction of the court. This is preceded by a court application for the holding of a creditors' meeting. These are new proposals which are designed to minimise court involvement and provide for greater involvement of creditors.

Malta - This involves the court placing a company under a company recovery procedure by appointing a special controller to manage and administer the company's business for up to 12 months with a possible extension for a further 12 months. The special controller will ultimately make a proposal to the court which if approved will be binding.

New Zealand - The first procedure is a compromise whereby the company proposes a compromise at a meeting of its creditors. The decision of a 75% majority will be imposed on the minority. It appears this procedure does not involve a stay on creditors.

The second procedure is a voluntary administration. The company appoints an administrator. During that time there is a stay on creditors' claims. For an arrangement to be agreed 75 per cent in value and 50 per cent in number of the company's creditors must agree. While the court can intervene, a voluntary administration can be conducted without court involvement.

Northern Ireland – The CVA is operated in Northern Ireland. A CVA is a Company Voluntary Arrangement which involves a private arrangement between the company and its creditors. It is not subject to any publicity and envisages creditors agreeing a debt settlement with the company. The proposal for a debt restructuring is set out by a Nominee at a meeting of creditors which if approved (by 75% in value of all creditors and 50% in value of unconnected creditors) is binding on all creditors. It can be challenged in court if there is a material irregularity or there has been unfair prejudice.

Norway – The approval here involves debt settlement procedures whereby an insolvent company files a petition with the court. The company comes under the control of the supervision of the court. In a compulsory debt settlement, 75% in number and value of unsecured creditors must support this and unsecured creditors must receive at least 25% of their claim. It is understood that this procedure has encountered difficulties in practise.

South Africa – A new procedure has been established where the company makes a filing with the Commission. Affected persons may apply to court to set aside the appointment of a Business Rescue Practitioner (who must be licensed and is subject to regulation). A stay is put on creditors' proceedings, although set off is permitted. The proposal arrangement must be approved by 75% of creditors (in value) and 50% of independent creditors (in value).

The Review Group carefully considered whether any of the foregoing regimes might be capable of being adopted in Ireland. The Review Group had the benefit of the advice of its member representing the Office of the Attorney General and concluded that, absent the consent of all creditors, the compromise of third parties' rights, in Ireland, required judicial sanction. The Review Group is satisfied that the law already adequately facilitates the consensual compromise of debt.

The Review Group also considered that the experience from other jurisdictions indicated that it was necessary that an independent person should be responsible for the formulation of a scheme. In an Irish context, this role is currently fulfilled by an *examiner* and the Review Group saw no reason to create a new position in the context of formulating schemes for small companies.

Within the strictures of the constitutional requirement that the non-consensual compromise of third parties' claims requires judicial sanction, the Review Group still considered that the models in other jurisdictions provided a basis for developing a non-judicial aspect to the process. In this regard the Review Group distinguished between the *appointment of an examiner* from the *sanction of a compromise scheme*. Accordingly, the Review Group focussed its attention on developing recommendations based on:

- having less judicial involvement in the appointment of an examiner, and
- having no judicial involvement in the appointment of an examiner.

11 Extending the role of the Circuit Court

At present, the Circuit Court can oversee the examinership process, but the application must first be submitted to the High Court and then be remitted to the Circuit Court. It was suggested that the role of the High Court could be removed to allow direct access to the Circuit Court. The current threshold for remitting a case to the Circuit Court is where the total liabilities of the company (taking into account its contingent and prospective liabilities) are less than €317,434.52, which is to be increased to €500,000 in the Companies Bill.

The Review Group considered that the "liabilities" test for qualifying to bring an application in the Circuit Court, would be better replaced by a test based on more objective criteria. For this reason, the Review Group believes that the appropriate test should be that applicable to the requirement relating to the preparation of financial statements based upon whether companies are small, medium-sized or large private companies.

Of these, the Review Group considered that its focus should be on small private companies ("SPC"). An SPC is a company falling within section 8(1)(a) of the Companies (Amendment) Act 1986 and means a private company that, in a particular year and in the immediately preceding financial year, satisfies at least two of the following conditions:

— its balance sheet total did not exceed €4,400,000;
— its turnover did not exceed €8,800,000;
— its average number of employees did not exceed 50.

Although some concern was expressed by the ODCE that an SPC, as defined, could have liabilities of many millions of euro, it was thought that adequate protection would be afforded to all creditors by operation of a judicial process and that consideration might be given to providing that a creditor whose debts are written-down over a certain amount (e.g. €4,400,000) will have an automatic right of appeal to the High Court.

If the jurisdiction of the Circuit Court is extended, the Review Group is conscious that this would involve an increase in resources and requires consultation with the Department of Justice and the Courts Service. The need for any increased resources should be justified by extending the examinership process to companies which would otherwise fail and the beneficial impact on jobs, not only socially, but for increased tax revenue for the State would more than compensate for any additional resources required. Although the Circuit Court may not have direct experience to deal with examinerships, the proposal to include the Circuit Court in personal insolvencies should give a degree of critical mass to ensure reasonable familiarity with insolvency proceedings.

The High Court examinership process has worked. The jurisprudence that has been developed by the High Court has resulted in few creditors having a legitimate grievance after the approval of a court scheme of arrangement. The primary reason why it is not working for SPCs is because of the costs involved which are considered to be disproportionate to the resources of SPCs. While the Review Group believe that for some SPCs, even allowing an application to be brought completely within the Circuit Court structure will involve too much cost, it nevertheless feels it would be a lost opportunity to preclude SPCs from bringing a traditional examinership application in the Circuit Court.

The Review Group therefore recommends that SPCs should be able to apply directly to the Circuit Court to have an examiner appointed, and not be required to apply to the High Court although that should remain an option.

By section 8(3) of the Companies (Amendment) Act 1986, a private company qualifies to be treated as a 'medium-sized' company for any financial year if, both in that year and in the immediately preceding financial year, it satisfies at least two of the following conditions:

— its balance sheet total did not exceed €7,618,438;
— its turnover did not exceed €15,236,857;
— its average number of employees did not exceed 250.

These thresholds have only recently been revised upwards and are now at such a level that the Review Group concluded, with some reservations, that, given their new larger size, ailing medium-sized companies should continue to have only the one option namely, to apply to the High Court for the appointment of an examiner.

12 Personal Insolvency Bill and the Proposed Insolvency Service

In considering a non-judicial mechanism for corporate rescue, as noted under point 10 above, the Review Group considered that it is possible to distinguish between the approval of a scheme or compromise (which requires judicial sanction) from the initiation of an examinership through the appointment of an examiner (which could happen on an administrative basis).

Were it to be decided, in the case of an SPC, to allow the initiation of an examinership by the appointment of an examiner by administrative, instead of judicial act, some State agency would need to be charged with responsibility for that determination.

The Review Group considered the Personal Insolvency Bill 2012 [now the Personal Insolvency Act 2012] which it noted is stated to cover trade debt, and found that a number of provisions in the Bill may be usefully adopted for certain companies also. The Review Group, in particular considered that while a number of agencies exist (ODCE, CRO, IAASA etc) the proposed *Insolvency Service* to be established by the Personal Insolvency Bill 2012 would, given its proposed purpose and functions, appear to be best suited to making an administrative decision that a particular SPC might have a reasonable prospect of survival were an examiner appointed to it.

The Review Group is mindful, however, that the proposed agency will face significant challenges in establishing capacity to carry out the remit envisaged for it in the Personal Insolvency Bill, that it will also face potentially significant challenges in meeting demand for the proposed new personal insolvency remedies, and that, by virtue of the State's commitments to the IMF and EU under the Programme of Financial Support for Ireland, priority attaches to the effective implementation of the reform of the personal insolvency regime.

Accordingly, the Review Group recommends that consideration should be given to the practicability of extending the role of the new *Insolvency Service*, proposed to be established to include the administrative determination as to the initial appointment of an examiner to an SPC, having due regard to the priority requiring to be given to the mandate concerned for that agency under the Personal Insolvency Bill.

13 Proposal for simplified initiation of examinership

The Review Group believes that a proportionate response to the difficulties faced by many SPCs is to provide such companies with an alternative, less expensive, option to the current initiation of an examinership which necessitates a court application.

The Review Group proposes that, subject to the identification of a suitable State agency, and further analysis and deliberation of the policy issues, it appears to the Review Group that it would be legally possible for the SPCs to be allowed to initiate examinership by non-judicial procedure. The simplified procedure should only extend to the appointment of an examiner. Any scheme of arrangement or proposal formulated by the examiner must be approved by the Circuit Court.

By majority, the Review Group believes that the law applicable to the carriage of examinership and the determination of any compromise or scheme proposed by the examiner, should be that currently applicable to High Court examinership subject to the variations set out below. The Revenue Commissioners expressed a dissenting view arguing that the proposed approach would be an entirely new scheme requiring careful consideration on its own merits.

While carrying on business, the directors of a company which finds itself insolvent, or likely to become insolvent, have a duty towards creditors either to cease trading and wind up the company or, if they consider, with court protection the company or part of it, has a reasonable prospect of survival, should seek to put the company into examinership. An examinership may offer the prospect of recovery for the ultimate benefit of the company's employees, creditors (who are likely to have the debts already owing to them compromised) and shareholders (who may face dilution).

The Review Group considered that the existing examinership process is adequate for the needs of medium companies (within the meaning of Section 8(1)(b) of the Companies (Amendment) Act 1986) as well as larger companies. Accordingly, the Review Group considered that its proposal for administrative appointment of an examiner should be available only to small companies within the meaning of Section 8(1)(a) of the Companies (Amendment) Act 1986.

This new scheme would offer an alternative to the existing examinership process for small companies but would not prevent small companies opting for traditional examinership in either the Circuit Court or the High Court if they so wish.

The following was considered to be a possible way forward to enable SPCs that may not be able to afford the traditional examinership process to obtain protection for a limited period to restructure the company for the benefit of employees, creditors, shareholders and thus the economy as a whole.

(1) An SPC which is insolvent, or likely to become insolvent, whose directors or shareholders wish to seek court protection for the SPC has a report prepared by an independent expert (within the meaning of Section 501(2) of the draft Companies Bill) (the "Expert"). The primary function of the Expert is to assess the suitability of the company for entry to the process

– this will include an assessment of the company's survival prospects as well as the likelihood of being able to formulate a successful proposal.

(2) The Expert files his/her report with the Insolvency Service (an office dedicated to companies but forming part of the Insolvency Service to be set up under the Personal Insolvency Bill) which, if satisfied that there is a reasonable prospect of survival of the company (or part of it), will issue a protection certificate and file it with the Circuit Court, who will hear any application by a dissenting creditor against the issue of a protective certificate.

(3) On the filing of the certificate with the Circuit Court, in the absence of any contrary order, a stay is put on creditors' actions and any debt enforcement measures. Once a protection certificate has been issued, an examiner is appointed [by the Insolvency Service and notice of appointment is filed with the Circuit Court] ultimately to formulate a proposal for submission in the first instance to a creditors meeting.

(4) Recognising the potential for conflicts of interest, particularly given the limited court oversight involved, there was some support for requiring the examiner and the Expert to be different persons (and to be from different professional firms). On balance, the Review Group considered that it should be allowable for the examiner to be the same person as the Expert as this could save duplication of work and cost.

(5) Neither the Expert nor the Examiner should be a person who has a material connection with the SPC or any of its directors or shareholders.

However, because of the perception or otherwise that having the same person preparing both the Report and the proposal for creditors could be open to potential abuse arising from the absence of scrutiny by the Court, the Review Group considered there may be a case for Experts and examiners to be subject to regulation and/or for a creditor to be able to object to the same person taking on both roles if a creditor considered it inappropriate in any case.

Any new regulatory system would need careful consideration and should have regard, inter alia, to the restricted time scale available for the preparation of an Expert's report.

(6) The preferred protection period should be 70 days, which could on a successful application to the Circuit Court be stretched to 100 days. As the length of time taken to formulate a proposal is generally a cost factor, it would be envisaged an extension of an examinership to 100 days would be unusual unless there were compelling reasons for the extension. An SPC should generally be capable of being saved within 70 days or not at all.

(7) The Examiner would prepare a proposal for submission to a creditors' meeting. If approved by not less than 65% of unconnected creditors in value and not less than 50% in number in each case, the proposal is sent to the Circuit Court for approval, who will also hear any application by a dissenting creditor against approval.

(8) In view of the fact that for SPCs a successful examinership may result in the same directors remaining on the board of an SPC, and that the potential for abuse may be increased through diminished court involvement, one of the Examiner's functions should be to examine the conduct of the SPC's directors and their fitness to continue as directors of the SPC into the future and to report their findings to creditors in advance of the vote on any proposal. In the course of such review, any material misrepresentation given by a director in the course of the preparation of the Expert's Report should result in such director incurring personal liability for the discount of the SPC's debts permitted under the approved scheme of arrangement.

(9) Costs for an SPC seeking and going into examinership should be much reduced from the current levels due to the use of the Insolvency Service and the Circuit Court rather than the High Court as a result of a reduced number of court hearings as well as the reduced legal costs in the use of a lower court.

(10) The majority considered that the priority and level of write down of claims in the categories of secured, preferential, floating charge, unsecured, subordinated and shareholders should follow the current jurisprudence of the courts in approved schemes of arrangement of companies successfully exiting examinership to ensure a proportionate and objectively justifiable interference with the private property rights of creditors. The Revenue Commissioners disagreed on this point and, as set out at section 7 above, articulated the view that this is a new mechanism, entirely distinct from the existing examinership process but closely aligned to the debt settlement arrangements provided for in the Personal Insolvency Bill and, as such, that taxes and other debts should be treated in the same way as applies to those personal debt settlement arrangements. A majority of the Review Group did not consider that there was any basis in principle to distinguish a scheme approved by the Circuit Court following the appointment of an examiner by administrative act from a similar scheme approved by the Circuit Court or High Court where the examiner is appointed following an application made to that court.

The foregoing proposal is recommended as a possible way forward to enable SPCs to obtain protection for a limited period (at less cost than for a medium sized or large private companies or PLCs) to restructure the company for the benefit of employees, creditors, shareholders and thus the economy as a whole.

14 Conclusion

The Review Group considers that the task it faced raised very difficult, complex and in some cases irreconcilable issues of law, policy and principle which were not specific to company law. In attempting to guide the Minister on possible ways to assist small companies the Review Group has suggested the involvement of a State agency that has not in fact as yet been established. Accordingly, the Review Group acknowledges that its recommendations, in relation to the identity of the State agency which would make the administrative determinations, are necessarily tentative. Moreover, should the Minister decide to pursue the proposals suggested by the Review Group, there would need to be a significant amount of inter-Departmental consultation and policy analysis required to draft appropriate heads of Bill.

The Review Group realises that its suggestions relating to the *Insolvency Service* will necessitate consultation with the Department of Justice and Equality and the Courts Service in view of the implications of those recommendations for their respective legislative remits.

By contrast, subject to establishing that the Circuit Court has the necessary resources available to it and the policy agreement of the Department of Justice, the Review Group believes that there is no other reason why the changes proposed to permit all SPCs to bring application directly to the Circuit Court cannot be quickly progressed.

28 September 2012

Appendix 1 to Report on Item 2

Terms of Reference

The Minister asked the Review Group to examine the appropriateness of introducing a legally binding non-judicial commercial debt and enforcement system, to be used by small and medium sized businesses ("SMEs") into the Companies Acts, having regard in particular, but not exclusively, to the following factors:

1. The adequacy or otherwise for small and medium sized businesses of the procedures currently available in this regard under the Companies Acts, and in particular the existing examinership procedure;

2. Whether the particular needs of small and medium sized businesses could be catered for by introducing appropriate modifications to these existing procedures, for example by making greater use of courts below the High Court, or substituting alternative non-judicial safeguards for creditors, such as is proposed in the Summary Approval Procedure in the new Companies Bill;

3. The appropriate level of involvement, if any, of the courts in a non-judicial system, for example, whether there should be a confirmation of any proposal by the court, or a right of creditors to object, or no court involvement;

4. If a non-judicial system were to be introduced, whether its availability should be subject to a test comparable to the current "reasonable prospect of survival" test for examinership, and if so, by whom such an assessment could be made in the absence of court involvement

5. Potential issues regarding secured debts, and whether such security could legally be subject to the application of any non-judicial procedure;

6. Potential Constitutional issues, whether in relation to the possible writing-down of secured debts, or otherwise;

7. Potential cost issues, including the extent to which costs incurred under the existing procedures may be reduced by removing the involvement of the High Court, or any court, from those or any alternative procedures;

8. Potential competitiveness issues, including among competing participants in the same field of economic activity;

9. Potential implications for the willingness of credit institutions to lend to small and medium sized businesses if a non-judicial debt settlement and enforcement system becomes available for such companies;

10. Potential implementation issues, for example, the extent of the availability of any new non-judicial procedure in group situations where some companies are sufficiently small to qualify for such a procedure, but related companies within the group are not so qualified.

6.2 Report on Item 3 – Transposition of Directive 2005/56/EC on cross border mergers into Irish law

Item 3 Report – Introduction

Directive 2005/56/EC is transposed into Irish law by Regulations made in 2008 and amended in 2011. The Minister decided to include this item on the Review Group's Work Programme on foot of representations received in the Department.

The Review Group began its deliberations by establishing a Committee, chaired by Deirdre-Ann Barr, and adopted its final report, with recommendations, at its 69^{th} plenary meeting in January 2013.

The full text of that final report is reproduced below.

1 Introduction

The scope of work for the Group is to examine and make recommendations on whether it is necessary or desirable to provide for amendments to the legislation transposing the EU Directive on cross-border mergers into Irish law. The Minister's briefing to the Group referred to various representations made by legal practitioners to the Department of Jobs, Enterprise and Innovation in this regard. This paper describes the current framework for cross-border mergers in Ireland and considers the following specific issues:

1.1 In section 3 we consider whether there is a minimum number of companies required for a merger by formation of a new company.
1.2 In section 4 we consider the question of pre-acquisition profits in the context of a cross-border merger.
1.3 In section 5 we consider the acquisition of own shares in the context of a cross-border merger.
1.4 In section 6 we consider the acquisition of shares in a holding company in the context of a cross-border merger.
1.5 In section 7 we consider the competent authority for scrutinising cross-border mergers.
1.6 In section 8 we consider the inspection of documents.
1.7 In section 9 we consider the consequences of a cross-border merger for personal rights in real property.

Our review has proceeded on the understanding that the rules governing cross-border mergers are to be retained in a statutory instrument rather than being incorporated in primary legislation. This gives rise to certain vires issues which are addressed below.

2 Cross-border merger – Process and effect

2.1 Directive 2005/56/EC on Cross-Border Mergers of Limited Liability Companies and the amending Directive 2009/109/EC (the "Directives") were implemented in Ireland by the European Communities (Cross-Border Merger) Regulations 2008 (the "2008 Regulations") and the European Communities (Mergers and Divisions of Companies) Amendment Regulations 2011 (the "2011 Regulations") (together the "Regulations").

2.2 The Regulations permit cross-border mergers between Irish limited liability companies and limited liability companies in other EEA Member states. The effect of a cross-border merger is to transfer all of the assets and liabilities of one or more companies (the "Transferor Company" or "Transferor Companies") to another company (The "Successor Company") by way of universal succession. The Transferor Company is dissolved without going into liquidation.

2.3 A cross-border merger can be effected in one of three ways under the Regulations:

> 2.3.1 ***Merger by absorption,*** which is the simplest procedure and which involves the transfer by a wholly owned subsidiary (the Transferor Company) of all of its assets and liabilities to its parent company (the Successor Company), with the Transferor Company being dissolved without going into liquidation;
>
> 2.3.2 ***Merger by acquisition,*** which involves the acquisition by a company (the Successor Company) of all of the assets and liabilities of one or more Transferor Companies in exchange for the issuance to the shareholders of the Transferor Companies of shares in the Successor Company (with or without cash payment), with the Transferor Companies being dissolved without going into liquidation; and
>
> 2.3.3 ***Merger by formation of a new company,*** which involves the transfer of the assets and liabilities of two or more Transferor Companies to a company that they form for such purpose (the Successor Company), in exchange for the issuance to the shareholders of the Transferor Companies of shares in the Successor Company, with the Transferor Companies being dissolved without going into liquidation.

A diagram setting out the features of each of the three types of merger is set out in Appendix 1 to this Report.

2.4 Irrespective of the type of cross-border merger, broadly speaking, the initial phase of the Irish process involves the following steps:

2.4.1 A preparatory phase during which Irish and local counsel in the relevant EEA jurisdictions work together to prepare common draft terms of merger and a directors' explanatory report.

2.4.2 Publication of a notice of the merger in two daily national newspapers and in the CRO Gazette[1]

2.4.3 In certain circumstances an expert's report is required to be prepared setting out details in relation to the proposed exchange ratio and related matters. A separate report may also be required pursuant to section 31 of the Companies (Amendment) Act 1983 (the "1983 Act"), although a second report may be prepared by the same expert[2].

2.4.4 Publishing and making available the merger documents for inspection by the shareholders and employee representatives (or if there are no representatives, the employees) of the Irish merging company during the one month specified statutory period.

2.4.5 Approval of the merger by the shareholders of the Irish company at general meeting (this requirement can be dispensed with in certain circumstances)

2.4.6 An application to the Irish High Court for a *"pre-merger certificate"* to certify that all the pre-merger requirements have been satisfied.

2.4.7 The Regulations also contain detailed provisions regarding employee participation and consultation procedures. Broadly speaking, these provisions will apply in an Irish context where at least one of the merging companies has an average number of employees that exceeds 500 and is operating under an employee participation scheme.

2.5 Once the competent authority in each EEA state (which, in Ireland, is the High Court) certifies compliance with the pre-merger requirements, the final stage of the process is completed in the EEA state of the Successor Company. Where the Successor Company is an Irish company, an application will be made jointly by the merging companies to the High Court to confirm the legality of the cross-border merger. The order of the High Court will specify the date on which the cross-border merger will take effect.

2.6 Once an order has issued from the High Court, the Registrar of the High Court will send a copy of the order to the Companies Registration Office. The Registrar of companies will register the order on the Successor Company's file at

[1] The Directives do not stipulate a minimum number of national newspapers in which the notice must be circulated. The Group recommends that in line with the provisions for domestic mergers that the requirement should be amended to require publication of a notice of the merger in only one daily national newspaper and in the CRO Gazette.

[2] The provisions in relation to expert reports were amended in the 2001 Regulations and further details of the amendments made at that stage are set out in Appendix 2 to this Report.

the Companies Registration Office and is also required to give notice of the order to the competent authorit(ies) responsible for maintaining the companies' register(s) in the EEA state(s) of the Transferor Compan(ies).

2.7 With respect to a non-Irish Successor Company, the Irish Transferor Company is responsible for supplying to the Irish Registrar of Companies the order of the competent authority of the EEA State where the Successor Company is registered, and is further required to specify in writing to the Irish Registrar of Companies the date on which that competent authority determined that the cross-border merger takes effect. Independently of that, the registration authority of the EEA state where the Successor Company is registered is required to give the Irish Registrar of Companies notice that the cross-border merger has taken effect and on receipt of such notice from the foreign registry, the Irish Registrar deletes the registration of the Irish Transferor Company.

2.8 A cross-border merger has the effect of universal succession which, when the Regulations were introduced was quite a novel concept in this jurisdiction. The Regulations specify what universal succession means in this context and provide that as of the effective date:

> 2.8.1 all the assets and liabilities of the Transferor Companies are transferred to the Successor Company;
>
> 2.8.2 in the case of a merger by acquisition or a merger by formation of a new company, where no application has been made by minority shareholders to acquire their shares, all remaining members of the Transferor Companies except the Successor Company (if it is a member of the Transferor Company) become members of the Successor Company;
>
> 2.8.3 the Transferor Companies are dissolved;
>
> 2.8.4 all legal proceedings pending by or against any Transferor Company shall be continued with the substitution, for the Transferor Companies of the Successor Company as a party;
>
> 2.8.5 the Successor Company is obliged to make any cash payment specified in the common draft terms to the members of the Transferor Companies;
>
> 2.8.6 the rights and obligations arising from the contracts of employment of the Transferor companies are transferred to the Successor Company;
>
> 2.8.7 every contract, agreement or instrument to which the Transferor Company is a party shall, notwithstanding anything to the contrary contained in that contract, agreement or instrument, be construed and have effect as if:
>
> > 2.8.7.1 the Successor Company had been a party thereto instead of the Transferor Company

2.8.7.2 for any reference (however worded and whether express or implied) to the Transferor Company there were substituted a reference to the Successor Company

2.8.7.3 any reference (however worded and whether express or implied) to the directors, officers, representatives or employees of the Transferor Company, or any of them, were, respectively, a reference to the directors, officers, representatives or employees of the Successor Company or to such director, officer, representative or employee of the Successor Company as the Successor company nominates for that purpose or, in default of nomination, to the director, officer, representative or employee of the Successor company who corresponds as nearly as may be to the first-mentioned director, officer, representative or employee;

2.8.8 every contract, agreement or instrument to which a Transferor Company is a party becomes a contract, agreement or instrument between the Successor Company and the counterparty with the same rights, and subject to the same obligations, liabilities and incidents (including rights of set-off), as would have been applicable thereto if that contract, agreement or instrument had continued in force between the Transferor Company and the counterparty, and any money due and owing (or payable) by or to the Transferor Company under or by virtue of any such contract, agreement or instrument shall become due and owing (or payable) by or to the Successor Company instead of the Transferor Company, and

2.8.9 an offer or invitation to treat made to or by a Transferor Company before the effective date shall be construed and have effect, respectively, as an offer or invitation to treat made to or by the Successor Company.

3 Is there a minimum number of companies required for a merger by formation of a new company?

3.1 Regulation 2(1) of the Regulations defines a *"merger by formation of a new company"* as an operation in which <u>two or more companies</u>, on being dissolved without going into a liquidation, transfer all their assets and liabilities to a company that they form (the new company) in exchange for the issue to their members of securities or shares representing the capital of that new company, with or without any cash payment. This definition is consistent with the Directive. In particular, the Directive defines a merger as including an operation whereby

"<u>two</u> or more companies, on being dissolved without going into liquidation, transfer all their assets and liabilities to a company that they form, the new company, in exchange for the issue to their members of securities or shares representing the capital of the new company.."

3.2 By contrast, the proposed provisions for domestic mergers contained in part 9 of the Companies Bill [now the Companies Bill 2012] define a merger by formation of a new company as an operation involving <u>one</u> or more companies.

3.3. The Group queried whether the provisions for cross-border mergers should be brought into line with envisaged domestic mergers provisions. It was considered that, where possible and provided it was not inconsistent with the Directives, the harmonisation of the cross border regime with the domestic regime would be desirable in the interests of consistency. Furthermore, such a change might have a distinct practical application where, for example, companies wished to transfer their registered offices from one EU member state to another – an issue which is currently the subject of a consultation process with the European Commission.

3.4 In light of the intention for the present time to retain the cross-border mergers regime in secondary legislation, the Group concluded that such a change to the existing definition would likely be beyond the *vires* of the Minister. The Directive itself defines a merger (involving the formation of a new company) as involving the dissolution of *two* existing companies. To broaden that definition would be to permit a cross border merger to occur in a way not envisaged by the Directive and therefore such a change is not necessitated by Ireland's membership of the EU. It would seem, therefore, that an act of the Oireachtas would be required to give effect to this broader definition of *"merger".*

3.5 To effect such a change by way of statutory instrument would likely be outside the scope of the Minister's delegated powers. Therefore, whilst desirable, the Group cannot recommend such an amendment to the Regulations.

3.6 It was also noted that any such change would require further scrutiny to assess whether it would facilitate a merger in Ireland which was beyond the scope of the Directive and therefore not subject to the reciprocal rules set down in the Directive for cross border mergers occurring in EEA member states.

4 Pre-acquisition profits

4.1 Regulation 21(2) of the 2008 Regulations provides that *"a cross-border merger does not create a subsidiary relationship to which sub-section (5) of section 149 of the Act of 1963 applies…"* This is consistent with the principle of the Regulations and the Tenth Directive, ie that a merger does not create a new parent / subsidiary relationship by interposing an additional company in a group structure, but rather that one of the merging companies by definition dissolves, or disappears from the group structure. Arguably therefore, the language in Regulation 21(2) is superfluous as that is the effect of a merger. However, given that the concept of a merger of two companies was novel in 2008, it was prudent to specify the impact of a merger effected pursuant to the 2008 Regulations in relation to certain other existing legislative provisions.

4.2 The first part of Regulation 21(2) set out above is not problematic, even if it is arguably superfluous. However, an issue arises in respect of the following part of the regulation which goes on to say *"…and accordingly the restrictions in that sub-section have no application to the profits and losses or accounts of an Irish successor company."* In specifying that there is no application to an Irish successor company, the Regulations create some ambiguity as to the impact of section 149(5) in post merger group structures where there is an Irish company involved, but where the Successor Company in the merger is non-Irish. For example, in a downstream cross-border merger where an Irish company is the holding company of two non-Irish companies which merge, and is not a party to the cross-border merger itself, there is no logical reason for treating any profits of the merged entity as pre-acquisition profits if they eventually reach the Irish holding company by reason of the cross-border merger. However, on the basis of Regulation 21(2) as currently expressed, this is not clear. The Group's concern was not that the Irish law restrictions on pre-acquisition profits might be extended to non-Irish companies, but rather to assess the impact (if any) of a cross-border merger on an Irish holding company, where the Irish holding company was not directly involved in a merger involving its downstream subsidiaries (direct or indirect).

4.3 It is submitted that Regulation 21(2) is not intended to distinguish between the impact of a merger involving Irish or non-Irish Successor Companies and it is recommended that the second part of Regulation 21(2) should be omitted so that that regulation reads as follows:

> *"A cross-border merger does not create a subsidiary relationship to which sub-section (5) of section 149 of the Act of 1963 applies."*

5 Acquisition of own shares

5.1. Regulation 21(3) confirms that the restriction on a company purchasing its own shares under section 41(1) of the 1983 Act does not apply to the purchase of any shares in pursuance of a court order under the Regulations.

5.2 The acquisition of own shares by an Irish Successor Company can arise in the context of a downstream merger by acquisition, where the assets and liabilities of a Transferor Company are transferred to an Irish Successor Company which is the company in which the Transferor Company holds shares; the shares in the Irish Successor Company constituting one of the assets transferred by the Transferor Company to the Successor Company. For ease of reference, a diagram setting out this potential scenario is set out at Appendix 3 to this Report.

5.3 In the absence of a specific provision, the shares may end up being dealt with as follows:

> 5.3.1 retained by the Irish Successor Company as ordinary shares, with full voting and dividend rights;
>
> 5.3.2 cancelled by share capital reduction under section 72 of the Companies Act 1963 (the "1963 Act");

5.3.3 acquired by redemption (after conversion) or purchase under Part XI of the Companies Act 1990 (the "1990 Act").

5.4 Giving the (own) shares to the Irish Successor Company under section 41(2) of the 1983 Act serves no purpose as that section is silent on what happens to such shares. The Group considers that there would be merit in providing for an explicit method of cancelling such (own) shares, incidental or ancillary to the merger[3]. As the inclusion of a parent company's shares in the balance sheet of the Irish Successor Company would not appear to be a necessary incident of such a merger (those shares being assets which would for example be eliminated in consolidated accounts of a parent and subsidiary) we recommend that such (own) shares be capable of cancellation by resolution of the Board of the Successor Company.

5.5 For this purpose, we propose the insertion of the following provision in the Regulations modelled on section 208 (b) of the 1990 Act[4]:

"Shares in a successor company acquired by the successor company pursuant to a merger by acquisition may, by resolution of the directors of the successor company, be cancelled in which case the following provisions shall apply as respects those shares:

(a) The amount of the company's issued share capital shall be reduced by the nominal value of the shares redeemed but no such cancellation shall be taken as reducing the amount of the company's authorised share capital.

(b) A sum equal to the nominal amount of shares cancelled shall be transferred to a reserve fund ("the capital redemption reserve fund") and the provisions of the Companies Acts relating to the reduction of the share capital of a company shall apply as if the capital redemption reserve fund were paid-up share capital of the company."

5.6 Section 69(1)(g) of the 1963 Act provides that where a company having a share capital has cancelled any shares otherwise than in connection with a reduction of share capital under section 72 of that Act, the company must, within one month after so doing, give notice of the cancellation to the Registrar of companies specifying the shares cancelled. Accordingly, there is no requirement to insert in the Regulations any specific obligation as to delivery of particulars of the cancellation of shares that would arise under the above proposed amendment.

[3] There is the parallel desirability of shares acquired pursuant to C(A)A 1983 s 41(2) generally, being capable of cancellation, which we do not address in this paper.

[4] The provisions of section 208(b) are at section 107(2) and (4) of the Companies bill 20102, as initiated.

6 Acquisition of shares in holding company

6.1 Regulation 21(3) of the Regulations confirms that the restriction on a company purchasing its own shares under section 41(1) of the 1983 Act does not apply to the purchase of any shares in pursuance of a court order under the Regulations. There is no equivalent exemption in relation to the restriction on a company acquiring the shares in its holding company set out in section 32 of the 1983 Act[5] and/or the related provisions in that regard set out in section 224 of the 1990 Act[6].

6.2 The restriction in section 32 could conceivably be triggered in the context of a cross-border merger by acquisition between an EEA subsidiary (as the Successor Company) and its parent company's EEA holding company (as Transferor Company) where the direct parent company (the "Direct Holding Company") of the Successor Company is an Irish company. In this scenario, the Successor company would acquire the Transferor Company's shareholding in the Direct Holding company as part of the assets of the Transferor Company being transferred to the Successor Company as a result of the cross-border merger. For ease of reference, a diagram setting out this potential scenario is set out in Appendix 4 to this Report.

6.3 Where a cross-border merger is implemented in these circumstances, it gives rise to three potential consequences / effects which require consideration for the purposes of section 32 / section 224:

> 6.3.1 The cross-border merger involves the transfer of shares in Direct Holding Company to the Successor Company
>
> The implementation of the cross-border merger would involve the transfer to a subsidiary (the Successor Company) of shares in its Irish holding company (the Direct Holding Company). The Review Group recalled that section 32 provides that *"a body corporate cannot be a member of a company which is its holding company, and any allotment or transfer of shares in a company to its subsidiary shall be void"*>
>
> The Review Group noted that it is not clear whether the transfer of the shares in the Direct Holding Company in these circumstances (and therefore the merger itself) would be restricted by section 32 and/or section 224. In the absence of express authority to effect such a transfer in the Regulations, the transfer of the shares in the Direct Holding Company to the Successor Company would potentially be subject to section 224 of the 1990 Act such that, for example, consideration for the shares in the Direct Holding Company would need to be provided by the

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[5] Section 32 provides that "a *body corporate* cannot be a member of a *company* which is its holding company, and any allotment or transfer of shares in a company to its subsidiary shall be void". "Company" is defined in the Companies Act 1963 as "any company formed and registered under the [Irish] Companies Acts." "Body corporate" includes Irish and non-Irish companies.

[6] Section 224, as amended by the European Communities (public Limited Companies Subsidiaries) Regulations 1997, provides that a company (including a body corporate) may acquire and hold shares in a company which is its holding company where specified conditions are met. The second reference to "company", as in section 32, covers only those companies which are formed and registered under the Irish Companies Acts. The first reference to "company (including body corporate)" includes Irish and non-Irish companies.

Successor Company out of distributable profits; the Successor company would be prohibited from exercising voting rights in respect of shares, etc.

Whilst this scenario might arise relatively infrequently in practice, the Group considers that there would be merit in explicitly providing that the restriction on a body corporate acquiring shares in its holding company does not apply in relation to the transfer of shares in the context of a cross-border merger. The Group's suggested wording in this regard is set out below.

6.3.2 The Direct Holding company continues to hold shares in Successor company, its holding company.

Following the completion of the cross-border merger in the circumstances outlined, the Direct Holding company would continue to retain a shareholding in its then holding company, the Successor Company.

The Group recalled that section 32 prohibits a body corporate from being a member of a company (an Irish company) which is its holding company. The Group noted that where the Successor Company is an Irish company, the cross-border merger results in the Direct Holding Company (a body corporate, which in this case is an Irish company) becoming a member of its Irish holding company (the Irish Successor Company).

The Group also noted that section 224 has amended section 32 to allow a company (which includes a body corporate) to hold shares in its Irish holding company where specified conditions are met, namely:

(a) The profits of the subsidiary (in this case, the profits of the Direct Holding Company) available for distribution shall for all purposes be restricted by a sum equal to the total cost of shares acquired;
(b) The shares shall, for the purposes of the consolidated accounts prepared by the holding company (in this case the Irish Successor Company) in accordance with sections 150 to 152 of the 1963 Act, be treated in the same manner as required in respect of shares held as treasury shares under section 43A of the1983 Act; and
(c) The subsidiary shall not exercise any voting rights in respect of the shares and any purported exercise of those rights shall be void.

The Group concluded that the shareholding retained by a Direct Holding Company in the Successor Company in this scenario would be subject to the foregoing provisions of section 224. Notwithstanding this, the Group recommended that, for completeness, there would be merit in explicitly stating this in the Regulations. The Group's suggested wording in this regard is set out below.

6.3.3 The Direct Holding Company may continue to hold a majority shareholding in Successor Company, its holding company.

Generally speaking, the shareholding retained by the Direct Holding Company in the Successor Company will be a minority shareholding (since, in most cases, the Direct Holding Company's existing shareholding will be materially diluted upon the issuance of shares in the Successor Company to the shareholders of the Transferor Company in consideration for the merger).

However, the Group noted that the situation could conceivably arise (however unlikely it may be) where a very small number of shares could be issued by the Successor Company to the shareholders of the Transferor Company, such that following the merger, the Direct Holding Company could potentially retain a majority shareholding in the Successor Company (leading to the illogical result that each company effectively becomes the holding company of the other).

The Group noted in particular in that context that the Regulations, unlike the Directive, do not contain a restriction in the definition of *"merger by acquisition"* in relation to the maximum cash element of the consideration that may be provided by a Successor Company to the shareholders of the Transferor Company in the context of a merger by acquisition. The Group noted that where a very large part of the consideration for a merger by acquisition is provided in cash, the situation could arise where the Direct Holding Company retains a significant shareholding in the Successor Company.

The Group then generally considered the difference between the definition of *"merger by acquisition"* in the Regulations and in the Directive. The Group noted that although Article 2(2) in defining a merger stipulates that the maximum cash consideration is to be 10% of the nominal value of the shares, Article 3(1) states that the Directive also applies to mergers where the laws of the Member State allow the cash consideration to exceed the 10% threshold. The definition in the Regulations, not being subject to the 10% cash consideration restriction, potentially gives rise to vires questions (insofar as the Irish statutory instrument arguably facilitates cross-border mergers by acquisition other than those specifically facilitated by the Directive). The Group is of the view that there would be merit in bringing the definition of *"a merger by acquisition"* into line with the definition set out in the Directive. The Group's revised definition is set out below.

The Group noted that, where the definition of cross-border merger by acquisition is amended as outlined below, one indirect effect would be that the illogical situation outlined at the first paragraph of this section should be highly unlikely to arise. Therefore, in the view of the Review Group, no further amendments are required in this regard.

6.3.4 Recommendation

In light of the foregoing, the Group proposes the insertion of the following new provision in the Regulations:

> *"Section 32 of the Act of 1963 (which restricts the right of a body corporate to acquire or hold shares in its holding company), as amended by Section 224 of the Act of 1990, does not apply to the transfer of shares in an Irish holding company as part of a cross-border merger.*
>
> *"Where an Irish subsidiary of an Irish holding company becomes the holding company of the first Irish holding company as a consequence of a cross-border merger, the shares retained by the Irish holding company in its former subsidiary shall be treated by the Irish holding company in accordance with Section 224 of the Act of 1990."*

The Group also suggests that the definition of *"merger by acquisition"* set out in the Regulations is amended to read as follows:

> *"'Merger by acquisition' means an operation in which a company (other than company formed for the purpose of the operation) acquires all the assets and liabilities of another company that is, or other companies that are, dissolved without going into liquidation in exchange for the issue to members of that company, or the members of those companies, of securities or shares in the first-mentioned company, with or without cash payment <u>not exceeding 10% of the nominal value, or in the absence of a nominal value, of the accounting par value of those securities or shares</u>".*

7 Competent Authority

7.1 The Directives specify that a Member State must designate the court, notary or other authority competent to scrutinise the legality of the cross-border merger. Pursuant to the Regulations, the High Court is designated as the competent authority for the scrutiny and approval of cross-border mergers in Ireland. The Group noted that in other European jurisdictions, a notary was the designated competent authority and that the costs of effecting a cross-border merger in those jurisdictions were lower than the corresponding costs in Ireland. By definition in a cross-border merger, there will always be at least one other jurisdiction involved and therefore the costs comparison is a very real one. It was noted that the proposed new regime for domestic mergers set out in the Companies Bill [2012] provides that it is not always necessary to have the court supervision if the summary approval procedure is complied with. However, the Tenth Directive requires the State to designate a competent authority.

7.2 The Group noted that , given the consequences of a merger (outlined above) and that the concept of universal succession was still relatively novel in Irish law, the designation of the High Court as the competent authority was understandable. It was also noted that courts of similar jurisdiction were the designated competent authority in England and Wales and in Scotland. The Group considered that it might be useful to consider with the Courts Service and any other interested parties, if another court might be an appropriate authority to supervise cross-border mergers. Any such considerations would have to take into account the wealth of relevant expertise and experience in dealing with company law matters by the High Court as well as the geographical limitations on the jurisdiction of the Circuit and District Courts. Accordingly, no recommendation in relation to the designation of another court as the competent authority for scrutinising cross-border mergers is recommended at this time.

7.3 Certain members of the Review Group considered that it would be worth exploring with the Central Bank of Ireland the possibility that it would be designated competent authority for supervision of cross-border mergers of companies regulated by it. The Group is not aware of any restriction on a member state designating different competent authorities for different categories of company.

7.4 Regulation 57 of the European Communities (Undertakings for Collective Investment in Transferable Securities) Regulations 2011 provides that where a merging Undertaking for Collective Investment in Transferable Securities ("UCITS") is authorised by the Central Bank, such mergers shall be subject to the prior authorisation by the Central Bank rather than being subject to the prior approval of the High Court. As a result, the Central Bank is already the competent authority for considering approval of both cross-border and domestic mergers involving Irish domiciled UCITS. Approval of the Central Bank is also required in advance of a change of qualified shareholding of MIFID or IIA regulated companies.

7.5 It was therefore suggested that consideration be given to revising the Regulations to provide that in the case of any cross-border merger involving an entity which (i) falls within the remit of the Regulations and (ii) is authorised and regulated by the Central Bank, the Central Bank be named as the appropriate competent authority with the power to (i) confirm that the pre-merger requirements set down in the Regulations have been complied with[7] and (ii) to confirm the scrutiny of the legality of the cross-border merger under the Regulations[8].

7.6 The Central Bank, however, considered that there is no basis for the expansion of the remit of the Central Bank in this regard. The Central Bank considered that the courts were a more appropriate supervisor of cross-border mergers where third parties are impacted.

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[7] Regulation 13 of the Regulations.

[8] Regulation 14 of the Regulations

8 Inspection of documents

8.1 Under Regulation 9(1) of the 2008 Regulations, and subject to Regulation 9(1A) (inserted by Regulation 6(b) of the 2011 Regulations), members, and employees or their representatives of each merging company are entitled to inspect, free of charge, specified key documents relating to the proposed merger at the registered office of the Irish company during business hours (for at least two hours a day) for one month before the general meeting to approve the merger.

8.2 8.2 Members must also be informed under Regulation 9(2) of their entitlement to obtain, free of charge, full or partial copies of these documents on request. Regulation 9(2) states that the members should be informed of this right when the notice convening the general meeting to approve the merger is circulated.

8.3 8.3 The primary purpose of amendments introduced by the 2011 Regulations was to enable companies and their shareholders, involved in a cross-border merger to use the internet as an alternative to the inspection rights granted by Regulation 9 of the 2008 Regulations. The effect of these amendments appears to be as follows:

8.3.1 Where the Irish merging company does not publish, free of charge on its website, the documents listed in Regulation 9(1) for a continuous period of at least two months commencing at least one month before the date of the general meeting convened in accordance with Regulation 10 and ending at least one month after that date, then paragraphs (1) and (2) of Regulation 9 apply.

8.3.2 Paragraph (1A) is a relieving provision. It disapplies paragraph (1) of Regulation 9 (the obligation to have the relevant documents available for inspection at the company's registered offices for one month prior to the general meeting convened under Regulation 10), where the documents are published on the company's website for the two month period referred to above. Significantly however, Paragraph (1A) of Regulation 9 is made subject to paragraph (1B).

8.3.3 Regulation 9 (1B) gives rise to certain difficulties of interpretation. A literal reading of Regulation 9(1B) suggests that the right to inspect copies of the relevant documents at the company's registered office under Regulation 9(1) is to continue to exist if copies of the documents are available to download and print free of charge from the company's website for the two month period referred to above. This is because paragraph (1B) says that *"paragraph (1A) does not apply"* where the entitlement to obtain full or partial copies, as provided by Regulation 9(2), *"does not apply as a result of the application of"* Regulation 9(2B). Regulation 9(2B) disapplies the entitlement referred to in paragraph (2) of Regulation 9 to obtain , on request and free of charge, copies of relevant documents, provided the documents are available to download and print from the company's website, also free of charge, for the same two month period referred to above. The problem with the drafting of Regulation 9(1B) is that if, pursuant to Regulation 9(1B), the relieving provisions of paragraph

(1A) do not apply in such circumstances, this implies that paragraph (1) of Regulation 9 must continue to apply in such circumstances. The effect of paragraph (1) applying in such circumstances is that the obligation on the company to make the relevant documents available for inspection at the registered office of the company for the one month period would apply, notwithstanding that the documents are available to download and print from the company's website.

8.4 This is presumably not what was intended assuming that, as the Explanatory Note attached to the 2011 Regulations says, the primary purpose of these amendments to Regulation 9 was to give effect to the relevant provisions of Directive 2009/109/EC to facilitate the use by the company and its members and employees of the internet and electronic communication.

8.5 If the Irish merging company does so publish such information on its website, and provided the documents are available to download and print from it, also free of charge for the same two month period referred to above, the Group considers that the Regulations should not preserve the obligation on the company to make physical copies of the same documents available for inspection at its registered office for a separate one month period ending with the general meeting. The right of inspection of the physical documents at the company's registered offices should not apply, provided the Irish merging company does so publish such information on its website, and provided the documents are available to download and print, also free of charge for the same two month period referred to above.

8.6 The ambiguity inherent in the amended Regulation 9 also has the potential to cause some confusion as to the exact obligations of the Irish merging company where it has chosen to upload the relevant documents to its website. In the interests of clarity and certainty, the Group recommends that paragraph (1B) of Regulation 9 and the reference to it in paragraph (1A) should be deleted; and the provisions of Regulation 9 as amended would be renumbered accordingly.

9 Consequences of cross-border merger for personal rights in real property

9.1 As set out above, some of the consequences of a cross-border merger are that:

9.1.1 all the assets and liabilities of the Transferor Companies are transferred to the Successor Company;

9.1.2 every contract, agreement or instrument to which the Transferor Company is a party shall, notwithstanding anything to the contrary contained in that contract, agreement or instrument, be construed and have effect as if:

9.1.2.1 the Successor Company had been a party thereto instead of the Transferor Company

9.1.2.2 for any reference (however worded and whether express or implied)to the Transferor Company there were substituted a reference to the Successor Company

9.1.2.3 any reference (however worded and whether express or implied) to the directors, officers, representatives or employees of the Transferor Company, or any of them, were, respectively, a reference to the directors, officers, representatives or employees of the Successor Company or to such director, officer, representative or employee of the Successor Company as the Successor company nominates for that purpose or, in default of nomination, to the director, officer, representative or employee of the Successor company who corresponds as nearly as may be to the first-mentioned director, officer, representative or employee;

9.2 On first reading, this would appear to mean that all rights in real property whether freehold or leasehold would be transferred to the Successor Company as a consequence of the cross-border merger. In practice, however, conveyancing practitioners have concerns that this language is not sufficient to apply to rights in real property and have suggested that consistent with the principle of what is intended to be the consequence of a cross-border merger, Regulation 19(1) should be amended to include specific provision in respect of real property. The recommendation of the Group in this regard is illustrated by the highlighted language below. This language is suggested by way of example only and it is recognised that legislative amendments affecting real property will require careful consideration by the parliamentary draftsman, if the recommendation is accepted in principle. The principle is that the consequences for real property rights of a cross-border merger would be as highlighted in the text below:

9.2.1 every contract, agreement or instrument (**<u>including leases or any other instruments relating to real property</u>**) to which a Transferor Company is a party shall, notwithstanding anything to the contrary contained in that contract, agreement or instrument, be construed and have effect as if:

9.2.1.1 the Successor Company had been a party thereto instead of the Transferor Company

9.2.1.2 for any reference (however worded and whether express or implied **<u>and whether or not expressed to be a reference to the Transferor Company personally or to the Transferor Company and its successors and assigns</u>**)to the Transferor Company there were substituted a reference to the Successor Company

9.2.1. 3 any reference (however worded and whether express or implied) to the directors, officers, representatives or employees of the Transferor Company, or any of them, were, respectively, a reference to the directors, officers, representatives or employees of the Successor Company or to such director, officer, representative or employee of the Successor Company as the Successor company nominates for that purpose or, in default of nomination, to the director, officer, representative or employee of the Successor company who corresponds as nearly as may be to the first-mentioned director, officer, representative or employee;

9.2.2 every contract, agreement or instrument to which a Transferor Company is a party becomes a contract, agreement or instrument between the Successor Company and the counterparty with the same rights, and subject to the same obligations, liabilities and incidents (including rights of set-off) **in each case whether such are expressed therein to be personal to the Transferor Company or to benefit or bind (as appropriate) the Transferor Company and its successors and assigns),** as would have been applicable thereto if that contract, agreement or instrument had continued in force between the Transferor Company and the counterparty, and any money due and owing (or payable) by or to the Transferor Company under or by virtue of any such contract, agreement or instrument shall become due and owing (or payable) by or to the Successor Company instead of the Transferor Company.

9.3 The Group also recommends that the consequences of a cross-border merger upon the filings with various State registries should be specifically set out in the Regulations. It is therefore recommended that provisions such as the following should be incorporated in Regulation 19:

"19(2) subject to paragraph (3), the successor company shall comply with the filing requirements and any other special formalities required by law (including the law of another EEA State) for the transfer of the assets and liabilities of the transferor companies to be effective in relation to other persons.

(3) Where the successor company is an Irish company:

(a) the keeper of any register in the State shall, upon production of an official copy of an order under Regulation 14 but without the requirement to produce any other document, enter the name of the successor company in place of any merging company in respect of the information, act, ownership or matter in that register and any document kept in that register;

(b) without limiting paragraph (a), the following registers shall be deemed to be a register for the purposes of that paragraph:

(i) the register of members of a company as provided for by section 116 of the Principal Act;

(ii) the register of debenture holders of a company as provided for by section 91 of the Principal Act;

(iii) the register of interests in shares of a public limited company as provided for by section 80 of the Act of 1990;

(iv) the register of charges to be kept by the registrar of companies as provided by section 103 of the Principal Act;

(v) the register of deeds as provided by section 33 of the Registration of Deeds and Title Act 2006;

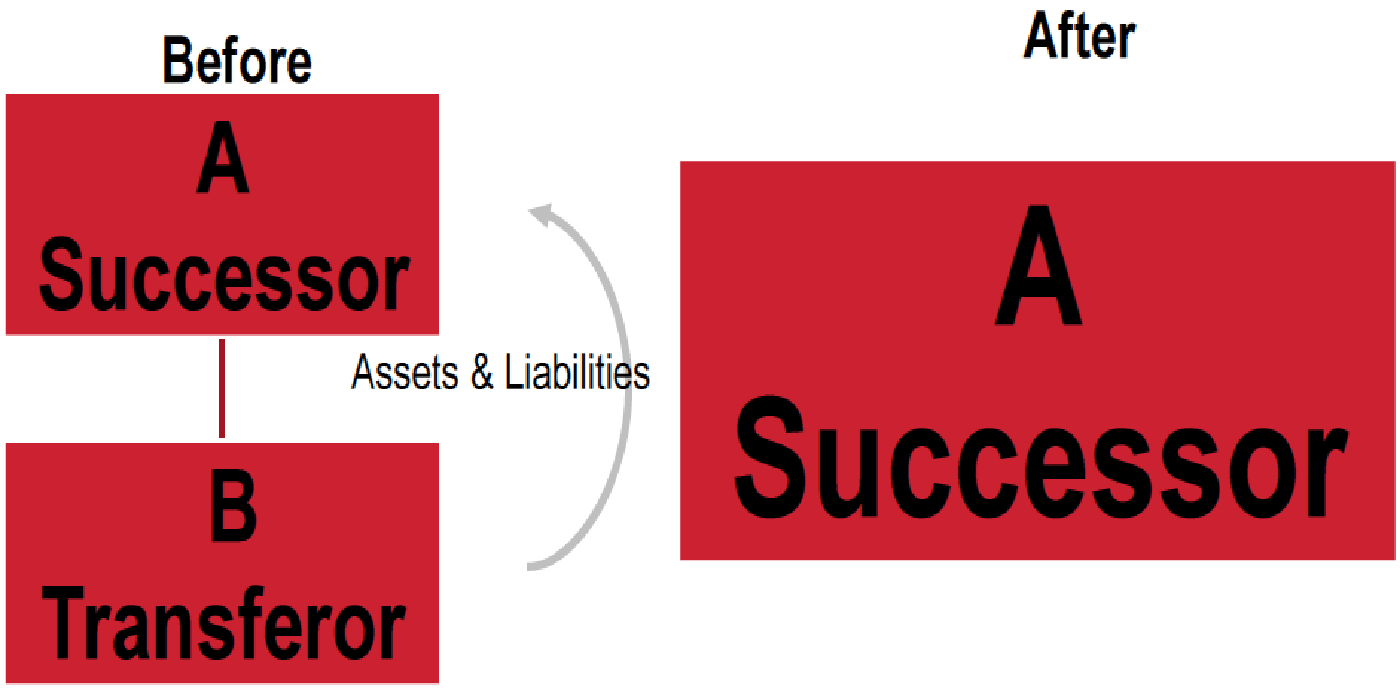
(vi) the Land Registry, as provide by section 7 of the Registration of Title Act 1964;

Any register of shipping kept under the Mercantile Marine Act 1955;

(d) Without limiting paragraph (a), the Registrar of Deeds, with respect to any deed (within the meaning of section 32 of the Registration of Deeds and Title Act 2006) registered by her or produced for registration by her, shall, upon production of an office copy of an order under Regulation 14 but without the requirement to produce any other document, enter the name of the successor company in place of any merging company in respect of such deed."

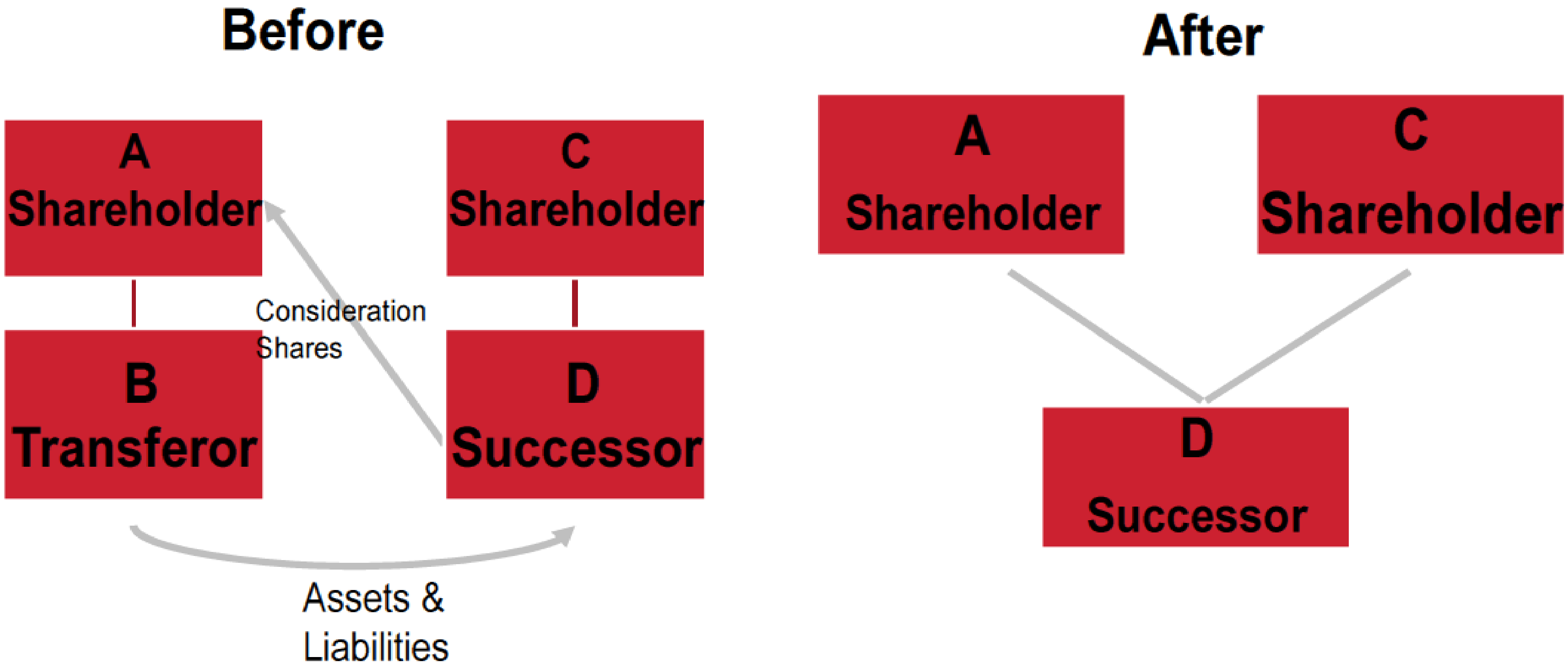
Appendix 1 to Report on Item 3

Cross-Border Mergers – Merger by Absorption



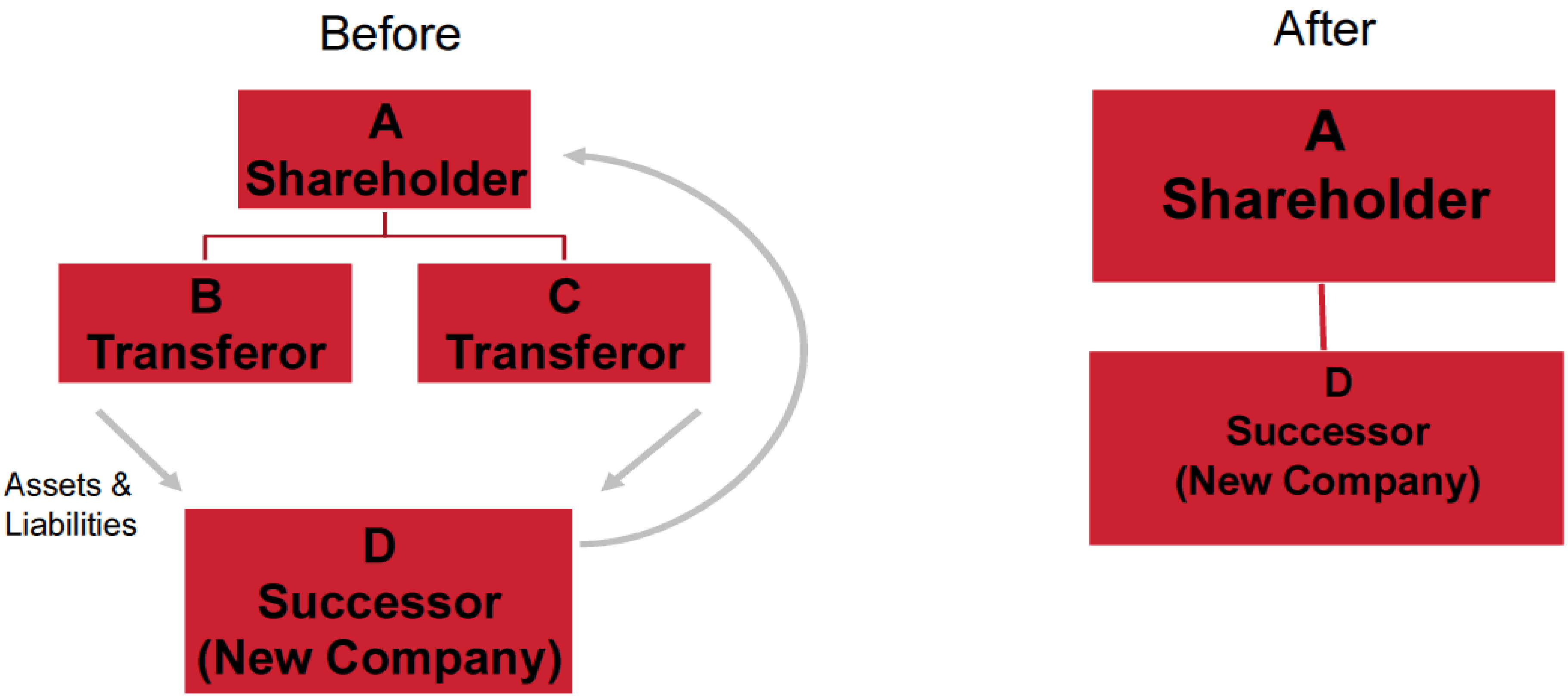
Appendix 1 to Report on Item 3 (Continued)

Cross-Border Mergers – Merger by Acquisition



Appendix 1 to Report on Item 3 (Continued)

Cross-Border Mergers – Merger by Formation of a New Company



Appendix 2 to Report on Item 3

Experts' reports – Amendment of Regulation 21 by the 2011 Regulations

Regulation 21(1) of the 2008 Regulations as originally made, provided that sections 30 and 31 of the Companies (amendment) Act 1983 (the 1983 Act) do not apply to the issue of shares by any company as a consequence of a cross-border merger. Sections 30 and 31, which apply to public limited companies only, transpose Articles 10 and 27 of Directive 77/91/EEC (the "Second Directive"). Article 10 of the Second Directive relates to the initial issue of capital by a public limited company (founders' shares) whereas Article 27 relates to a subsequent increase in issued capital. Both Articles require an independent expert's report where a public limited company issues shares for a consideration other than cash. Articles 10 and 27, as amended by Directive 2009/109/EC, correspond to Articles 10 and 31 of Directive 2012/30/EU, the recast version of the Second Directive.

Regulation 21(1) of the 2008 Regulations was deleted by Regulation 6€ of the 2011 Regulations. The reason for this is explained below.

Mergers of companies entail the issue by the Successor Company of its own shares to the members of the transferor Company in exchange for the shares of those members (already in issue) in the Transferor Company (which company will cease to exist). This means that the shares to be issued will be issued for a consideration other than cash (in the form of the shares in the Successor Company), which brings the share issue within the scope of specific provisions of the Second Directive where the company issuing the shares is an Irish public limited company.

Under the Second Directive, independent experts must produce a report on the consideration other than cash (being, in the case of mergers, the existing shares in the Transferor Company) with particular emphasis on valuation. The Third[9] and Sixth[10] Directives each contain provisions requiring the production of a report by an independent expert or experts. For a company issuing the shares in the context of a merger or division there would have been a considerable overlap between the requirements of the Second Directive and those of the Third or Sixth Directives as the case may be were it not for the fact that the original Second[11], Third and Sixth Directives included measures of relief from the effects of this overlap. There was a similar overlap where a cross-border merger

[9] Directive 78/855/EEC – domestic mergers of public limited companies
[10] Directive 82/891/EEC – domestic divisions of public limited companies
[11] Articles 10(4) and 27(3)

involved the issue of shares by an Irish public limited company but the Tenth Directive[12] did not contain any explicit exemption.

The measures of relief from the effects of this overlap were Member State options. Ireland availed of those in the Third and Sixth Directives but not of those in the Second. The measures of relief contained in the Third and Sixth Directives differed from each other. The Third Directive[13] gave Member States the option of dispensing with the Second Directive's experts' report on consideration other than cash in the context of mergers[14]. The Sixth Directive[15] (divisions) gave member States the option of allowing the same expert or experts to produce the reports required by the Sixth and Second Directives.

Directive 2009/109/EC rationalised this. The provisions of Articles 1(2) and 1(3) bring together in one Directive (the Second Directive) the different Member State options, previously located in the Second, Third and Sixth Directives, in respect of the expert's report (required by the Second Directive) on the issue of shares for a consideration other than cash. These changes are complemented by those made by Articles 2(7), 3(4) and 3(8)(a). A consequence of relocating the exemptions to the Second Directive is that they apply directly to cross-border mergers where these involve the issue of shares for a non-cash consideration by an Irish public limited company.

As a consequence of changes made by Articles 1(2) and 1(3) of Directive 2009/109/EC, Member States could exercise one or other, but not both, of the options corresponding to those previously contained in the Third and Sixth Directives respectively, the choice being applicable to mergers and to divisions. The Department of Jobs, Enterprise and Innovation, having consulted on the issue and having considered the responses, chose to require the production of an expert's report and to avail of the option of allowing the same expert to produce the reports required by the Sixth and Second Directives.

Regulation 21(1) of the 2008 Regulations was based on Regulation 10 of the European Communities (Mergers and Divisions of Companies) Regulations 1987 (S.I. No. 137 of 1987) (the "1987 Regulations") except that Regulation 10 applied only to a company formed for the purposes of a merger by formation of a new company. Regulation 21(1) was not based on any specific provision of the Tenth Directive. The deletion of Regulation 21(1) of the 2008 Regulations corresponds to that of Regulation 10 of the 1987 Regulations. The deletion of Regulation 10 of the 1987 Regulations gave effect to Article 2(7) of Directive 2009/109/EC which deleted Article 23(4) of the Third Directive (Article 2(7) of Directive 2009/109/EC complements Articles 1(2) and (3) of that Directive). Article 23(4) of the Third Directive provided that the Member States need not

[12] Directive 2005/56/EC – cross-border mergers
[13] Article 23(4)
[14] Similar to Article 27(3) of the original Second Directive (now the first sub-paragraph of Article 31(3) of the Recast Directive).
[15] Article 8(3).

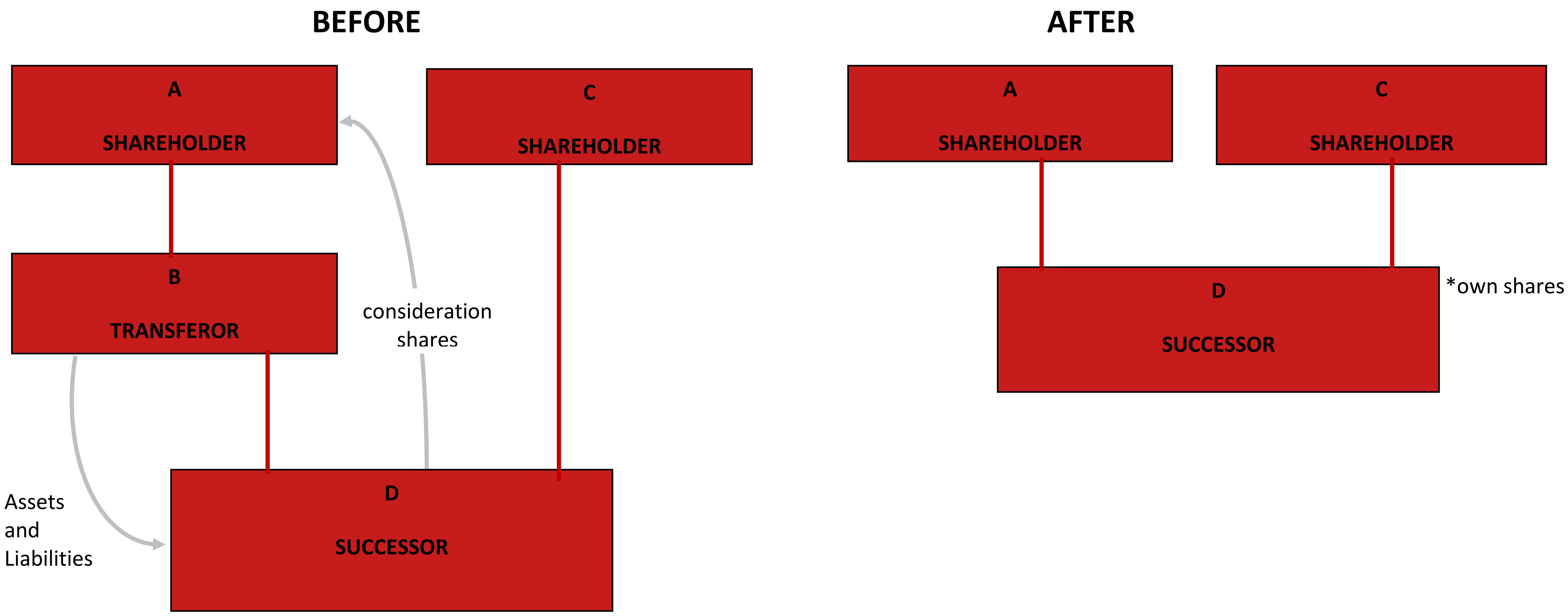
apply to the formation of a new company the rules governing the verification of any consideration other than cash which are laid down in Article 10 of Directive 77/91/EEC. The deleted Article 23(4) of the Third Directive corresponds to the first sub-paragraph of the new Article 10(5) of the Second Directive (and of the Recast Directive).

A number of provisions of the 2008 Regulations do not derive from specific provisions of the Tenth Directive but are based on provisions of the 1987 Regulations, some because of specific linkages between the Tenth and Third Directives and others because provisions of the 2008 Regulations were modelled on those of the 1987 Regulations and, indirectly, on those of the Third Directive. Article 4(1)(b) and (2) of the Tenth Directive, read in conjunction with Recital 3, may have been the basis of this approach. However, Regulation 21(1) of the 2008 Regulations went further than the equivalent provision of the 1987 Regulations in that its scope was not confined to the formation of a new company.

There is no basis for a provision in the 2008 Regulations equivalent to the deleted Article 21(1). The exemptions provided by Articles 10(5) and 31(3) of the Recast Second Directive are now reflected in section 31 of the 1983 Act (as amended by S.I. No. 306 of 2011).

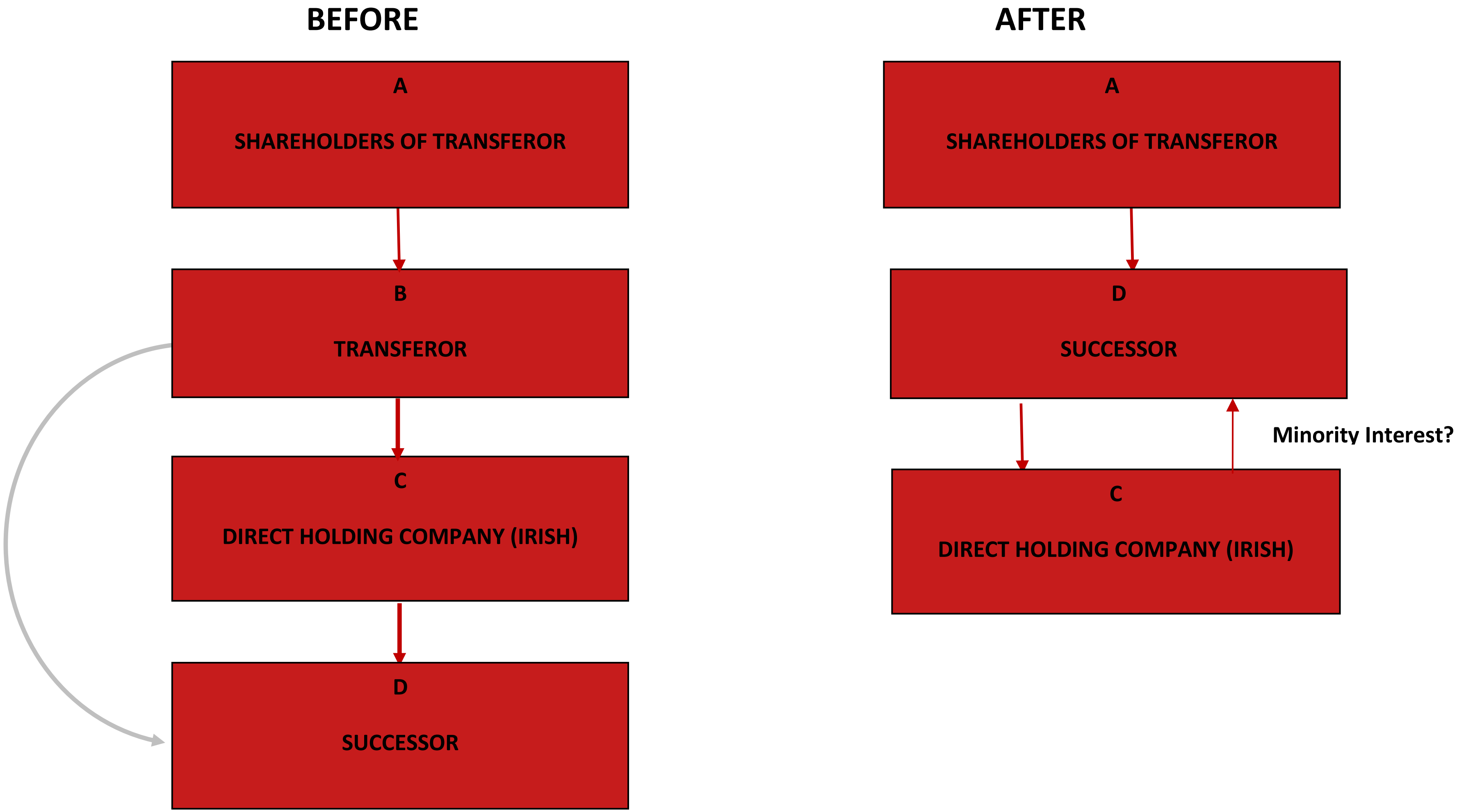
Appendix 3 to Report on Item 3

Acquisition of own shares



Appendix 4 to Report on Item 3

Acquisition of Shares in a Direct Holding Company



6.3 Report on Item 6 – Provisions regarding the re-use of information held by the Companies Registration Office

Item 6 Report – Introduction

The Review Group was requested to examine and make recommendations on a number of issues pertaining to data, including personal data fields, that are collected by the CRO and the subsequent re-uses of this data. In particular, the Review Group examined –

- The interaction with data protection laws and the CRO's use of personal data
- Corporate identity theft and other issues arising from information gleaned from the CRO Register
- Onward sale of data to "bulk data customers" of the CRO and the subsequent re-use of that data
- Retention (for live companies) and Archiving (for companies dissolved 20 years or longer) of CRO data

The Review Group established a Committee, chaired by Helen Dixon, and adopted its final report at its plenary meeting in January 2013. The full text of that report is reproduced below.

1 The Interaction with Data Protection laws and the CRO's use of personal information

The Review Group considered that a full treatment of this topic would require a re-examination of all of the personal data that the CRO is required to collect under the Companies Acts (including in respect of directors, company officers, members and auditors). In this re-examination, the question should be asked if all of this personal data is essential for the purposes intended under the Acts.

The Review Group also identified the need for some analysis to be done in the area of the additional personal data that is occasionally supplied to CRO by presenters in purported compliance with the Companies Acts (e.g. marriage certificate where a director is switching from her maiden to married name). Since 2010, CRO has implemented systems to prevent recording of such information on the public register but the question arises with regard to the fate of historically available personal information.

In November 2012, the Review Group examined a full list of all the personal data that the CRO collects and the circumstances in which each piece of information is required were identified. The group also examined a recent presentation, commissioned by the EU, comparing the data available on national public business registers in the 27 EU Member States.

Personal data

As a starting point, it was noted that it has been a fundamental principle of company law that anyone can inspect the register. Secondly, disclosure of certain information has been seen as the proper trade-off for the privilege of limited liability. Accordingly, there would need to be clear justifications for, and analysis of, the consequences of any proposals to reduce the disclosure obligations.

It was also noted that any proposals to withhold information statutorily supplied to CRO from the public register would require amendment to section 370(1) of the Companies Acts 1963. As a consequence, the statutory forms would need to be reviewed to assess how best to separate information destined for the public register from information that would be kept, but not made public, by the CRO. Proposals that required some parts of forms to be redacted would impose a significant burden on the CRO. On a related point, it was concluded by the group that any proposals to restrict publication should be limited to future company filings, as it would be virtually impossible to amend existing filings and the personal data in those historic filings is in any event already in the public domain.

The Group's analysis of each item of personal information is set out in detail in Appendix 1.

Conclusion

In the majority of cases, no change is recommended in relation to either the collection or publication of the majority of existing personal data fields collected by the CRO. The most fundamental change considered by the Group was whether to allow limited or available-to-all non-publication (but not disclosure to CRO, which would remain) of director home addresses. A number of proposals in respect of non-publication were discussed. Overall the Review Group was of the view that if the address was to be withheld from publication, it should be in limited cases only (that is, for example, cases where the personal security of the director was at risk). Having comprehensively reviewed the issue, the Group endorsed the original 2006/2007 proposal of the CLRG that a system be put in place whereby An Garda Síochana would be the body to certify as to a risk to personal security on the application to them by a specific director.

Further, the issues around publication of directors' usual residential address and date of birth relate to the requirement for a means to identify directors. The Review Group considered that it might be useful for a future CLRG work programme to consider whether a new perspective could be brought to the issue of introducing unique individual identification on the register, which work might include an analysis of the opportunities, if any, presented by the new Social Protection Public Services Card.

ISSUE OF COMPANY HIJACKING

As a current officer of the company at the time when a B10 is being filed with CRO, a newly appointed company director may notify on behalf of the company the fact of his/her appointment to CRO on Form B10. The concern here centres around a person potentially submitting notification to CRO that they have been appointed as director of a company and notifying CRO that another director or directors have resigned, when this is not in fact the case.

The nature of the Irish registration system was considered. Under the Companies Acts, there is notification to CRO from the company concerned after the fact of appointment/resignation of a director. Possible solutions to hijacking examined included requiring that a solicitor verify that the appointment/resignations notified on the Form B10 in fact took place; using the rules that will apply on the death of the single director in the Companies Bill; or CRO being required to contact the person alleged to have resigned upon receipt by CRO of notification of termination. However, the frequency of the problem was also reviewed (not very common). On balance, the Group did not consider any of these suggestions to be considered proportionate. The concern was that they were cumbersome and would cause problems for the vast bulk of companies which file bona fide notifications in relation to their directors with CRO. These suggestions would also delay the publication of the notices of appointment/termination of company officers on the CRO's register, which would be undesirable, and would result in the public register being out of date for longer than under current law.

Taking into account the CRO's "watch" system on its online filing environment, CORE, it was considered that this watch system could be promoted to a greater extent as a safeguard against this problem. To take any other route risks taking a hammer to crack a nut. Further, there have only been two cases in the last ten years that the CRO is aware of. In addition, registration of a filing by CRO does not create legal validity in most cases.

Ultimately, the Review Group concluded that issues in this area do not arise with any great frequency and recommended no change to the system of notification of new officer appointments and officer resignations to CRO.

2 Bulk Data Supply by the CRO

The Review Group examined the matter of data, including personal data, sold under licence by the CRO to commercial third parties and looked back to the origins of this licensing arrangement. The CRO had compiled an electronic database of company information and images on a per-company basis, starting in the early 1990s, and from then on, no longer maintained hard copy company files. The register is the electronic CRO database. In the early 1990s, CRO was unable to service the demand for company information and was also unable to operate in the field of adding value to the basic statutory information. Dun & Bradstreet were willing to provide this service and so they began to purchase the data and images from CRO, receiving updates via data tape every 14 days. This market developed with more bulk customers coming on-stream. As of 2013, there are seven customers who purchase CRO data in bulk under Licence. CRO was not *obliged* to start selling the statutory data in bulk when it started but once it had, it could not readily terminate the supply of data and images in bulk. In 1999, the search facility on the CRO website was injuncted by one of the bulk customers who was unhappy with the live search facility then being provided by CRO, given that the bulk supply at that time was every 14 days. CRO thereafter moved to upgrade its supply mechanism and by late 2001 was in a position to offer a Licence to bulk customers for the supply of data and images on an every working-day basis. This Licence was effected under the Copyright and Related Rights Act 2000.

Section 370(1) CA 1963 (replicated in section 892 of the Companies Bill 2012) accords a right to inspect the documents kept by the registrar - over the years, CRO has received a number of complaints that by actively supplying the data, rather than operating a passive inspection service, as envisaged by section 370(1), the Registrar was acting outside her functions under the Companies Acts. Furthermore, the lack of any legislative basis for bulk data supply in the Companies Acts had proven to be unhelpful to the Office in the defence of the 1999 injunction proceedings. For these reasons, the Office requested CLRG a number of years ago to review the issue as to whether there should be an express legislative provision in the Companies Acts recognising the fact of bulk supply.

A recent Austrian case came before the ECJ in the matter of **Compass Datenbank .v. Austria** where the court decided last July that the Austrian register was not an undertaking insofar as it limited itself to carrying out of the functions of the statutory register. That ruling was not unhelpful to CRO but the factual background varies very considerably from the CRO model, there being no bulk supply in Austria. CRO voluntarily entered the field of bulk data supply and there is now a large and well-defined bulk data market and it would not be open to the Office to unilaterally withdraw from same at this juncture and to revert to merely allowing inspection on request on a per-item basis of the register/documents kept by the Registrar. CRO considers that the Companies Acts ought to reflect the bulk supply issue.

The Review Group concluded there may be scope to add a function of the Registrar to the new Companies Bill facilitating the current licensing arrangement. The Review Group noted that the UK has no such provisions in its legislation. Section 370(1) CA 1963 has been included in the Companies Bill 2012 as section 892, as follows:

(1) On payment of the prescribed fee, any person may –
(a) inspect any document kept by the Registrar;
(b) require the Registrar to certify a certificate of incorporation of any company;
or
(c) require the Registrar to certify a copy of or extract from any other document or any part of any other document kept by the Registrar.

This is the same approach as under current legislation in that it envisages a passive role for the CRO and does not take account of bulk supply which is not on payment of the prescribed fee on a per-item basis but discounted to take account of the bulk nature of the supply and the inherent time lag that is inbuilt to such supply. In order to underpin the licensing to third parties of data and images from the Government copyright database that is the CRO register, CRO proposed that section 892 be expanded by the inclusion of an additional subsection along the lines that "*Without prejudice to subsection (1), the Registrar may make available the documents, including extracts from such* *documents, kept by her, on such terms and in whatever manner she deems appropriate*", which proposal was endorsed by the Review Group.

3 Archiving and Retention Policy

The Review Group examined retention and archiving as two separate issues. Retention of statutory filings relates to both live and dissolved companies. Archiving relates to statutory filings in respect of companies which have been dissolved more than 20 years (beyond the possibility of restoration to the register under the Companies Acts). After 20 years, a dissolved company is defunct in that it can never be restored.

The current archiving provision (carried forward without amendment into the new Bill) requires CRO to retain the paper filings for 20 years post-dissolution of a company and then to send "the documents" to the National Archives.

> ***"(313) - Disposal of documents filed with registrar***
>
> *The registrar of companies, shall, after the expiration of 20 years from the dissolution of a company, send all the documents filed in connection with such company to the Public Record Office."*

Section 313 CA 1963 was, however, devised for the era of hard copy filings which were placed by CRO on hard copy company files. CRO ceased to maintain hard files in respect of companies more than 20 years ago and the CRO register has been maintained electronically ever since. The paper filings are scanned and made available as electronic images. The original hard copy filings are retained by CRO and filed in storage in date order in terms of 'document-received date', not on a per-company basis. Approximately €300K was expended by the CRO in 2011 alone on storage and retrieval facilities in respect of hard copy company documentation.

A previous CLRG recommendation from 2001 endorsed the destruction of paper documents held by CRO three years after receipt of a document, provided that same had been reliably scanned and the electronic version remained available for inspection – the Minister was to be given power to designate a class or classes of documents that were suitable for destruction. This covered both live and dissolved companies. This recommendation has not fed into the new Bill, however.

With regard to archiving, section 313 has not been complied with in practice for many years by the CRO. The fact that the forms are not put on hard copy individual company files (instead paper submissions are stored by the CRO in batches by date received) causes practical difficulties in complying with section 313 (in terms of CRO identifying the documents that relate to a company which is dissolved for 20 years plus) as well as rendering the records less attractive to the National Archives. As of December 2012, the National Archives has indicated that it does not have an Electronic Archivist employed and has no systems or facilities available to take in electronic records due to a lack of funding for development of same. The National Archives have run a small number of pilots around electronic data receipt with a few Government departments but these have been limited in scope. In terms of paper receipt by the National Archives, they would require paper records to be on accessible company files rather than batches by date of documents received at the CRO, so in fact it would not be possible (at least not without the use of a massive amount of human resources) at this point for CRO to separate out of these batches papers relating specifically to companies dissolved 20 years or more and to effectively create a hard copy file for each such dissolved company at this remove. Notwithstanding these practical difficulties, however, the National Archives has indicated on consultation in relation to this report, that it considers that the current section 313 of the Companies Acts to be in any case overridden by the provisions of the National Archives Act, 1986. It is the view of the National Archives that the CRO, both in respect of its own administrative records and those it creates and maintains in relation to the registration of companies, is since 1988 subject to the provisions of the National Archives Act, 1986.

This Act, which established the National Archives and came into operation in 1988, requires all bodies subject to its provisions to preserve records, to seek permission from the Director of the National Archives prior to the destruction of any records, and to transfer records worthy of permanent preservation to the National Archives when they become 30 years old for the purpose of making them available for public inspection and research use.

What would appear to be needed and what is at issue here then is an archiving provision that reflects electronic filing and the electronic CRO register and which acknowledges that company information is currently kept on a database, instead of hard copy files. The record is therefore now the electronic document. It was acknowledged that there can be a problem with how electronic information is retained and archived, in that it can be saved in certain ways which subsequently become obsolete which has consequences for retrieval. The Review Group considered that an electronic CRO Archives Database into which the electronic records of companies dissolved 20 years or more are stored and made publicly accessible is the best solution and that section 313 ought to be replaced with a provision reflecting this.

The retention issue was then further discussed by the Group in respect of companies which are live or which have been dissolved for less than 20 years and on that basis capable of being restored under the Companies Acts. The Review Group considered whether to accept the previous CLRG recommendation as to destruction. Paragraph 7.9.2 of the First Report of the CLRG (2001) came to the following conclusion on the issue:

> *"Section 313 of the 1963 Act provides that the Registrar shall, after the expiration of 20 years from the dissolution of a company, send all the documents filed in connection with such companies to the Public Record Office. Consequently, the CRO is obliged to retain all documents filed during the lifetime of every company for a twenty year period after each company has been dissolved, notwithstanding that the documents may also be stored in electronic form. The Review Group recommends that, subject to there being a reliable assurance as to the integrity of the information, and provided that the information is capable of being displayed in intelligible form, and that it is readily accessible so as to be usable for subsequent reference, the Minister ought to be empowered to*

permit by order the destruction of a certain class or classes of documents, after a period of at least three years has elapsed since date of delivery of a document in that class to the CRO, and to deem the electronic copies of such documents to be the originals of the documents for all purposes."

Given advances in digital technology and the fact that electronic storage costs are lower than they were in 2001 when this recommendation was made, this proposal could be altered in order to allow for:

- discretion on the part of the Registrar to destroy certain classes of documents,
- after a set period;
- provided that reliable, electronic copies have been made.

It would also appear to be prudent to include a provision to the effect that electronic versions of filed documents (or extracts from same) could be relied on in Court proceedings as evidence. Being able to rely on purely electronic copies of documents has some precedent in legislation. Section 9 of the Electronic Commerce Act 2000, states that :

*"**9.** – Information (including information incorporated by reference) shall not be denied legal effect, validity or enforceability solely on the grounds that it is wholly or partly in electronic form, whether as an electronic communication or otherwise."*

Notwithstanding the small number of cases where it may be relevant, the ODCE notes that in respect of electronic documents where the original is no longer available, handwriting analysis is not possible in respect of scanned copies, and as such the ability to prosecute cases involving allegations of forgery relating to such documents would not be possible

Having examined relevant statutory retention periods in other legislation, in particular Revenue's, the Review Group recommends that the Registrar be given power to no longer retain certain classes of paper records after 6 years where a reliable electronic record is available and this electronic version now constitutes the record. Constitutional documents would be permanently retained. Further, the provision to no longer retain would be an enabling provision only and CRO would not dispose of any paper records for which it had notice that there was a third party requirement to retain beyond the 6 years. An in depth and detailed analysis of the records and formats of records retained by the CRO would be required between the National Archives (which has expressed its willingness to engage) and the CRO before suitable legislative heads of bill could be drafted. Such engagement between the bodies is necessary to ensure that destruction or archiving provisions of any future Companies Act do not cut across the existing statutory role of the National Archives in this area. Further, the Group is aware that the Law Reform Commission is considering the wider issue of documentary evidence and technology and in that context any possible future legislation may need to take cognisance of any proposals emanating from the report of the Commission which is scheduled to be published in 2013.

Appendix 1 to Report on Item 6

Surname and forenames:

No proposal for change. All fields required.

Former surname

Retain field. ODCE has indicated that it is useful in tracing certain directors.

Initials

Section 195 register of directors (which the CRO register is intended to mirror) requires the *"present forename and surname and any former forename and surname"* of each director, which means that a directors' forename is required to be recorded, and not an initial. S.I. No. 39 of 2002, Companies Act 1990 (Form and Content of Documents Delivered to Registrar) Regulations 2002 – Regulation 15(1) provides: *"An individual shall be referred to in a document by his or her surname, and all of his or her first names"*. This gives the CRO a legal basis to reject a document whereby a director's forename is not given, just his or her initials, and is in line with the section 195 requirement. No change is recommended by the Review Group here.

Usual residential address

The Group considered the outline content of a number of representations made to the Department on the subject of residential addresses. Previous representations on the issue proposed withholding the private home addresses of directors from the register, saying that experience showed that some foreign investors were put off setting up companies in Ireland because of concerns for their own safety if their home addresses were made public. Apart from the impact on inward foreign direct investment, certain representations also suggested that the current requirement for publication has a negative effect on Ireland's competitiveness vis-à-vis the UK, where it is possible to have one's home address kept private.

The Review Group noted the practice in some jurisdictions either not to provide for publication of the usual residential address of a director or to facilitate exceptions, subject to satisfaction of conditions such as where a national identity card has been provided.

There was some discussion on the original basis for the requirement for disclosure. Likely reasons identified were that it assists in identification of a person; that it may have been intended to help investigators gain confidence in directors (if a person is regularly on the move, it could raise questions). It was also considered that, nowadays, people are more inclined to research companies and their directors on the internet.

There was agreement that the CRO should continue to collect this information, but there were two schools of thought as to whether it should be published or not. The first considered that it could only be withheld where there was a serious concern for personal safety, for example where a person is a director of a company engaged in vivisection or chemical research. The counter argument was that it should never be published on the basis that it is not relevant to the public. This point of view argued that it is simpler to make it the rule to withhold for all and was based on experience of, where some who are engaged in sectors that are not obvious targets, such as construction, had still come under personal attack at home. If those people had to apply for privacy, it is possible that they would be refused on the grounds that they do not operate in a "dangerous sector". It was also noted that journalists can use this information to camp outside a home.

It was suggested that removing this information from the CRO's register might encourage people to start turning up at companies' registered offices looking to inspect their registers. Again the question of accuracy for legal proceedings was mentioned, although any recommendation for change would allow the ODCE to have access to addresses.

Another issue examined was the current context, where there has been public disquiet as to how companies, particularly groups of companies, arrange their affairs. The Review Group noted that any proposal to reduce the amount of information in the public domain is likely to be met with a backlash. Sound arguments showing that withholding this information would reduce the risk of harassment would be needed and indeed evidence that harassment arising from publication of addresses on the CRO register (for purchase) would need to first be adduced.

Informal consultations were also conducted between the CRO and some of their bulk data customers who offer value-added products based on the COR database. Their views are strongly in favour of the retention of home addresses and dates of birth on the public register. Without this, they insist that it will not be possible for interested parties to definitively identify the specific director with whom they are dealing. It would lead to a loss of confidence for suppliers wishing to extend credit terms to companies. With no national identity card nor other system of unique identification of directors in Ireland, it would not be possible to distinguish directors with the same name from one another. One bulk data customer suggested that claims of personal security risk are greatly exaggerated and that their experience of those objecting to publication of personal data centres on the fact that the individuals concerned generally have judgments recorded against them and / or are seeking to hide something. In summary, bulk data customers, businesses, credit rating firms and banks on foot of CRO data would not appear to be in favour of any reduction in information published as to directors' residential addresses.

Ultimately, the Review Group noted that the information held by the Registrar of Companies forms but a small part only of the information generally available about directors. Names and addresses can be gleaned from telephone directories, the Register of Electors, the Registry of Deeds, the Land Registry, local planning authorities and indeed the publicly available information in other jurisdictions. If the law were to be amended to allow a director's usual residential address to be kept off the CRO public record, it must be recognised that an amendment to the Companies Acts would not keep that address out of the public domain; it would simply provide an impediment to an easier discovery of that address.

The Review Group considered whether to follow the example of the original United Kingdom system, in facilitating non-disclosure of a director's residential address where the director provides evidence that he or she would be at serious risk of violence or intimidation as a result of the activities of the company (the UK has since moved entirely to publishing only a service address in respect of every director and recording the usual residential address off the public register). The Review Group considered that it would clearly be desirable in such extenuating circumstances that a procedure exist to allow for non-publication in limited cases on the register of the usual residential address. The Group considered, however, that issues arise in terms of finding a satisfactory procedure, not least on account of the burden and cost of administration that would fall upon State agencies as a result. In addition, any solution would benefit future directors only and not any person who is already a company director or may become one prior to any change in the law to give effect to a non-publication procedure.

The Review Group considered options as follows to implement limited withholding of the usual residential address from publication by the CRO:

1. Application by a company director to the Gardaí who would issue a notice to the CRO to confirm a case for non-publication. This would be similar to the process originally introduced in the UK. The Review Group considered this process would be suitably robust and allow for application only to genuine cases.
2. Application by a company director to the ODCE. This possibility was considered but also rejected on the grounds of resources and further as to how ODCE staff were to assess if a security risk did indeed exist.
3. Allow for publication of just a limited extract of from a notified address – for example, Patrick Murphy, Stepaside, Dublin 18 and keep the remainder off the CRO register. This was considered and has the benefit of allowing for potential identification of an individual without revealing the full address. However, it would be an extremely time-consuming an difficult system for the CRO to administer.

While the Review Group in general was in favour of potential facilitation of suppression in only limited cases, it went on to consider a solution to allow for application by any director to prevent the publication of a home address. The Review Group considered such a solution on the basis that it may be easier to administer a system open to all rather than one that requires assessment of individual circumstances.

4. Provide for a legal procedure available to all company directors to apply to the CRO to have their usual residential addresses omitted from the public record – the register of directors kept by the company and the statutory forms usually containing that residential address (B1, B10). The proposed procedure would involve company directors procuring a qualified service provider to maintain a service address for that director for a two year period, which would be renewable. A detailed outline and draft heads for such a solution are set out in Appendix 2 of this Report. The benefits of this system would be that it would be open to all to apply. The downside is that it may only end up being utilised by those that could afford it rather than those whose personal security is at risk. Further it would present a

massive administrative overhead for the CRO in terms of its implementation.

Overall, the Review group concluded that solution number 1 above presents the most suitable implementation option to achieve the result of allowing non-publication only in the limited cases meriting such action. It is recommended that the matter be followed up with the Department of Justice as soon as possible with a view to examining how it could be operationalised between the CRO and An Gardaí Síochána. Legislative underpinning for such a procedure would need to be provided for by way of amendment or addition to the Companies Bill 2012.

<u>Date of birth</u>

The Review Group considered two objections to this requirement. These were the fear of identity theft and the more limited concern from some that the revelation of their age could affect their career negatively.

The value of this information in identifying people was examined. It was noted that this requirement was introduced in 1990, and was designed to deal with so-called phoenix companies. It was agreed that it is useful in the case where different generations of families have the same names and addresses, which is relatively common in Ireland. Moreover, if there is any move to withhold home addresses, then also withholding dates of birth could make it very difficult to identify people.

On balance, it was believed that there is noticeably more concern with the publication of home addresses than with that of dates of birth (based on queries to CRO and on the experience of some of the Group). Interestingly, the bulk data customers informally consulted said that they regularly receive more queries around the publication of the date of birth. As a result, one bulk data customer in particular now publishes only date of birth ranges (for example, 1970-1974) rather than the full DOB on the free portion of their website. In addition, that same bulk data customer omits every second line from addresses on the publicly available information prior to purchase so only, for example, Patrick Murphy, Stepaside, County Dublin may appear. Once a purchase of a document is made, however, the director’s full DOB and home address can be seen. Ultimately, the Review group recommended no change in relation to publication of date of birth.

<u>Business occupation</u>

It was considered that this is not useful, as for the most part, people state such things as “company director” or “housewife” as their occupation. It was agreed that this could be dispensed with but the Review group recommends retaining it for the limited utility it has on occasion for the ODCE.

<u>Nationality</u>

A company currently is obliged to identify those directors with non-Irish nationality on its headed paper. Therefore, the nationality of directors has to be required to be supplied to the company for inclusion in the company’s own section 195(1) register of directors and secretaries. Given the headed paper imposed on companies by section 196, it seems unnecessary to require nationality identification to be notified also to the CRO for its register. No strong views either way emerged and it was recommended that no change be made.

Other directorships

While some directors have complained about the need to provide details in respect of a 10 year period, this will be abridged in the Companies Bill [2012]. One possible idea here would be to require directors to identify current directorships versus previous directorships, in the interests of clarity. Otherwise, no change was recommended. The Review group agrees with the proposals in the Bill to reduce the number of years for which directorships must be recorded.

Beneficial ownership

It was noted that a lot of other EU Member States have an obligation to disclose beneficial ownership. However, the current rules excluding the notification and / or recording of any trusts in relation to shares in the company's own register of members are carried over in the Bill, and are being extended to expressly refer to the CRO register also in this context. No change recommended.

Telephone and fax numbers

No change recommended.

Email addresses

It is optional to supply CRO with a company email address on a hard copy filing, but mandatory for e-filing. The compulsion is to enable the CRO to save money by corresponding with the company by email, rather than by post. Also, because the company is availing of the e-filing facility, it is not unreasonable to look for an email address. It was agreed that this is useful for the CRO.

To date there have been only a few objections from companies. A concern about spam was expressed. CRO does not see this as a real threat as the information is not easily accessed and used by outsiders. Looking ahead, this issue pointed to the usefulness of designing statutory forms whereby the non-public information could be included on a discrete final page, to make it easier to scan the publicly available information separately and keep certain information collected by CRO out of the public domain. If this was to be pursued at a later date, it would require the Companies Acts to be amended to provide that the information concerned was not made publicly available.

PPSN

This piece of information is not publicly available, and is used as a method of identification by the CRO for internal purposes only. There are difficulties with using the PPSN as a general system of identification as it is not designed to be a unique identifier. So far, there have been no objections raised with the CRO about its use.

Garda National Immigration Board number

This is only used in cases where the person is not known to the person witnessing a declaration and is an acceptable alternative to, say, a passport when a statutory declaration is being sworn. However, under the new Companies Bill [2012], all statutory declarations are being removed and being replaced with unsworn declarations so CRO will no longer receive details of GNIB numbers.

ROS signature

Presenters and company officers may optionally sign the CRO online forms using the Revenue’s online signing system. As it is optional, no officer is obliged to supply CRO with personal information in this regard. The fields of information securely exchanged with Revenue are minimal and are detailed on the CRO website. No change was recommended.

Appendix 2 to Report on Item 6

Proposal regarding withholding of the usual residential address from publication by the CRO

This was not endorsed by the Review Group but is included for completeness.

Terms and conditions and draft heads of Bill under which all directors could apply in order to have their usual residential address kept off the register:

The director's usual residential address would be provided:

- By the director to the company; and
- By the company to the Registrar of Companies;

separately from the director's other particulars.

The director's obligation to notify the company of changes in his or her usual residential address and the company's obligation to notify the Registrar of Companies would remain unchanged.

Comment: It was considered necessary to ensure for enforcement purposes that the director's usual residential address be available.

The director's usual residential address would be freely available to any State agency, including but not limited to the Revenue Commissioners, the Gardaí and the Director of Corporate Enforcement.

Comment: It was considered necessary to ensure for law enforcement purposes generally that the director's usual residential address be available.

The director would, at least once every two years, designate another address in the State for all purposes under the Companies Acts which would satisfy the following conditions:

(i) It must be the professional office of or employing a relevant services provider (solicitor, accountant, chartered secretary) and be open for business during usual office hours;

(ii) That relevant services provider must undertake to the Registrar to furnish to the director all communications addressed to that director received by the provider.

The substitution of the designated address for the usual residential address would cease to apply upon the expiry of two years from the delivery of the notification of designated address, without a fresh notification being received by the Registrar, in such event:

- The director's residential address would be inserted in the company's register of director's; and
- The Registrar would put the separately furnished residential address information in respect of that director on the publicly available file of the company.

Comments: (1) The requirement for an undertaking is in order to impose both a moral and a professional responsibility on the giver of the undertaking. Breach of an undertaking is a disciplinary matter for the professionals anticipated to be giving the undertaking.

(2) The two year period is modelled on the period for a bond under section 138(2) of the Companies Bill [2012], where a company does not have as director at least one individual who is resident in an EEA Member State. The requirement for renewal imposes a requirement for vigilance on the director and the professional services provider and also enables the provider to cease to carry out the function every two years.

Any document received at the designated address would be considered to be received by the director and any person serving a document there should not be concerned to establish whether the director has in fact received the document.

Comment: This is modelled on section 52 of the Companies Bill [2012] relating to service of documents on a company.

The amendments to the Companies Bill [2012, as initiated], would be as follows:

A. The insertion of a new subsection into section 150 of the Bill:

(13) Subsection (2)(c)shall apply in relation to a company with "his or her designated address within the meaning of section 150A" in substitution for "his or her residential address" if and for long as the company and the Registrar holds a relevant undertaking as provided by [section 150A(2)(b)].

B. The insertion of a new section 150 A into the Bill:

Designated address for a director

(1) Subject to the provisions of this section, a director may, for the purposes of section 151(3) of the Bill furnish particulars of an address in the State as his or her designated address which satisfies the conditions in subsection (2).

(2) The designated address shall be a professional office that is open as a matter of course during usual office hours of an individual who –

(a) Is –

(i) A person named in the Table to section 634(4) of the Bill[16]; or

(ii) A chartered secretary; and

(b) Has given an undertaking in writing in the prescribed form in favour of the company and of the Registrar, effective for a period of two years from and including the date of its execution, to forward forthwith to the director all and any written and electronic communications received on his or her behalf by the individual.

(3) Without prejudice to other methods of service of documents on a director, a document may be served on a director that has designated an address under this section by leaving the document at or sending it by post to that designated address.

(4) Any document at any time left at or sent by post to the place recorded at that time by the Registrar as the situation of the designated address of a director shall be deemed to have been received by the director, and no person leaving or sending such a document shall be concerned to investigate to ensure that the director has received it.

(5) An individual who has given the undertaking referred to in subsection (2)(b) that fails to comply with that undertaking shall be guilty of a category [-] offence.

[16] Member of a prescribed accountancy body; practising solicitor,; a member of a professional body as IAASA may from time to time recognise for the purpose of section 634; person qualified under the laws of another EEA state to act as liquidator; a person with practical experience of and knowledge of relevant law approved by IAASA.

6.4 Report on Item 8 – Meeting the criteria to qualify for the audit exemption

Item 8 Report – Introduction
Under current law, certain types of company qualify for audit exemption if they meet three criteria relating to balance sheet total, turnover and number of employees. The High Level Group on Business Regulation recommended in its 2012 Report that the Minister for Jobs, Enterprise and Innovation would consider the suggestion to allow companies to qualify for the audit exemption when just two, rather than all three, of the criteria are met. The Minister subsequently included a commitment in the Action Plan for Jobs 2013 to examine the case for this suggestion, which included an open public consultation and a referral of the issue to the Review Group for an expert view on the feasibility and impact of such a change in company law. Accordingly, on 27 March 2013, the Minister wrote to the Chairman, formally requesting the Review Group to consider the potential benefits or challenges, from a company law perspective, of advancing this proposal, and to make recommendations. The Review Group established a Committee, chaired by Mark Pery-Knox-Gore and adopted its final report at a plenary meeting in September 2013.

1 Introduction

Under current law, certain types of company qualify for audit exemption if they meet three criteria relating to balance sheet total, turnover and number of employees.

The High Level Group on Business Regulation recommended in its 2012 Report, that the Minister for Jobs, Enterprise and Innovation would consider the suggestion to allow companies to qualify for the audit exemption when just two, rather than all three, of the criteria are met. The Minister subsequently included a commitment in the Action Plan for Jobs 2013 to examine the case for this suggestion, which included an open public consultation and a referral of the issue to the Company Law Review Group ("the Review Group") for an expert view on the feasibility and impact of such a change in company law.

Accordingly, on 27 March 2013, Richard Bruton TD, Minister for Jobs, Enterprise and Innovation, wrote to Dr. Tom Courtney, Chairman, formally requesting the Review Group to consider the potential benefits or challenges, from a company law perspective, of advancing this proposal, and to make recommendations.

2 Terms of Reference and Working Method

The Minister asked the Review Group to examine the appropriateness of amending the Companies Acts to allow companies to qualify for the audit exemption where they meet just two of the three current criteria for audit exemption, having regard in particular, but not exclusively, to the following factors –

- The appropriateness of reducing the requirement from meeting three to just two criteria
- If it is appropriate to require compliance with two, then, should any particular criteria be singled out over others, e.g. should any one or two be mandatory
- Whether any new safeguards would be needed if the requirements were changed
- Whether it is appropriate to change the requirements for all companies that are covered by the current audit regime or if it would be necessary to exclude some types

The Minister asked that the Review Group report back to him, with recommendations, by Friday 20 September 2013.

Accordingly, the CLRG established a Committee to examine the question in more depth and to make recommendations to the full CLRG. That Committee, under the chairmanship of Mark Pery-Knox-Gore (the full membership of the Committee is listed at Appendix 1), met on four occasions and reported back to the full Review Group. The Review Group met in plenary session on the 13th of September, considered the Committee's views and adopted the recommendations that are set out at the end of this report.

3 Current Law

Section 32(3)(a)(ii) and (iii) of the Companies (Amendment) (No.2) Act 1999 provides that a private company limited by shares that meets three specified criteria may be exempted from the general rule that the annual accounts of a company must be audited. The three criteria, and their current thresholds, are –

- Annual turnover does not exceed €8.8 million
- Balance sheet does not exceed €4.4 million
- Average number of employees does not exceed 50.

The current thresholds were set in August 2012 and are given effect in two Statutory Instruments –

- European Union (Accounts) Regulations 2012 (S.I. 304 of 2012)

- Companies (Amendment) (No. 2) Act 1999 (Section 32) Order 2012 (S.I. 308 of 2012).

There are some additional obligations on a company that seeks to avail of the audit exemption, notably that it must be up to date with its annual return filings to the Companies Registration Office (the CRO). Moreover, members of a company who meet a specified numerical threshold have a right to require an audit despite the fact that a majority of the members of the company may wish to take up the exemption. Finally, certain types of companies, such as financial companies listed in the Second Schedule to the Companies (Amendment) (No.2) Act 1999, are prohibited from availing of the audit exemption.

This legislation transposes into Irish law elements of the Fourth Council Directive on the annual accounts of certain types of companies, which provides that Member States may exempt companies from the obligation to conduct an annual audit where they meet at least two of the three criteria. When introducing this provision into Irish law in 1999, the Oireachtas chose to require companies to meet all three.

4 Developments in the law

4.1 The new Accounting Directive (2013/34/EU)

The Fourth Directive of 25 July 1978 on the annual accounts of certain types of companies (78/660/EEC) contained a number of exemptions for small companies and medium-sized companies in the form of Member State options. The classification of a company as small or medium-sized was determined by three criteria or thresholds, these being "balance sheet total" (i.e. total assets), turnover and average number of employees. A company that met two out of three criteria fell to be categorised as small or medium-sized (though the Fourth Directive did not contain these terms). The levels of the thresholds were set out in the Fourth Directive and the monetary thresholds were adjusted periodically for inflation. In implementing these exemptions or derogations, Member States were free to set lower thresholds.

Article 51(1) of the Fourth Directive required that financial statements be audited but gave Member States the option of exempting small companies from audit (Article 51(2) and (3)). This was the legislative basis for the introduction of the audit exemption in the Companies (Amendment)(No.2) Act 1999.

Directive 2013/34/EU of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings replaces the Fourth Directive. It must be transposed into national law by 20 July 2015. Unlike the Fourth Directive, the new Directive takes the small company or group as the starting point and imposes additional requirements on medium-sized companies and groups and on large companies and groups as well as on "public interest entities" (in very broad terms, limited companies the securities of which are admitted to trading on a regulated market, banking companies and insurance companies).

Directive 2013/34/EU has no audit requirement for small companies. Chapter 8 of Directive 2013/34/EU addresses auditing. Article 34(1) states:

> "Member States shall ensure that the financial statements of public-interest entities, medium-sized and large undertakings are audited by one or more statutory auditors or audit firms approved by Member States to carry out statutory audits on the basis of Directive 2006/43/EC."

Recital 43 states:

> "The annual financial statements of small undertakings should not be covered by this audit obligation, as audit can be a significant administrative burden for that category of undertaking, while for many small undertakings the same persons are both shareholders and managers and, therefore, have limited need for third-party assurance on the financial statements. However, this Directive should not prevent Member States from imposing an audit on their small undertakings, taking into account the specific conditions and needs of small undertakings and the users of their financial statements."

4.2 The Companies Bill 2012

The Companies Bill 2012 was published on 21 December 2012 and, once enacted, will replace the existing Companies Acts 1963-2012. The Bill, as initiated, carries forward the existing legislative provisions in relation to audit exemption and also proposes to extend the scope of the exemption.

In this regard, the Bill provides for the application of the exemption, for the first time, to companies limited by guarantee. It also provides that a company may be a either a parent or a subsidiary, applying the three criteria to the group as a whole and not to individual companies within the group. It also proposes the application of the audit exemption to a dormant company.

The thresholds for the audit exemption are set out in the Companies Bill at sections 359(6) and (7). These are unchanged from the current thresholds (see 3 above) as is the rule that any company (or group) availing of the exemption must meet all three criteria. All other requirements, such as that the company must be up to date with its annual return filings in the CRO, are carried over in the Bill.

5 Information gathered by the Review Group

To start, the Review Group identified information that it considered relevant to help it assess how many companies would become entitled to avail of the exemption if they were only required to meet two criteria. Accordingly, the following information was sought –

1. Statistics on Irish companies that currently qualify for the exemption and on companies that would come within scope if the criteria were reduced to two and, in each case, if possible, their type and activities
2. Information from the High Level Group on Business Regulation on figures compiled by it at the time it recommended raising the thresholds (figures pre-August 2012 that estimate the impact of raising the monetary thresholds (i.e. balance sheet and turnover))
3. Information on the regimes in other EU Member States, in particular whether they impose any additional safeguards and, if so, what they are, and if they make any one or two of the criteria mandatory.
4. Summary of the views submitted to the Department of Jobs, Enterprise and Innovation under the public consultation on this topic, which ran alongside the CLRG's work.
5. Information on the UK consultation (October 2011) and the subsequent changes to UK law (Regulations of 2012)

With regard to the statistics on Irish companies (No. 1 above), the Review Group would like to acknowledge the assistance of the Companies Registration Office (the CRO) and Vision-Net (a company providing information on Irish companies), who supplied information insofar as it is available. Unfortunately, as small and medium-sized private companies are only required to supply information on their balance sheet and not on turnover or number of employees, the statistics supplied could not give a full picture to the Review Group (see Appendix 2). Similarly, the information obtained from the High Level Group on Business Regulation was somewhat speculative in nature and not based on full and accurate statistical data about companies coming within scope.

6 Issues considered by the Review Group

Once the Review Group had gathered as much of the relevant information as it could, it examined the following –

- The case for the status quo and the case for change (i.e. reduction to two criteria) including the likely impact of change, for example for the running of businesses and the enforcement of law
- Whether any two or one of the criteria are more meaningful than the other(s) and should be made mandatory if a change is made
- The safeguards that are in place and whether there would be a need for more, such as restricting the application to fewer types of companies, if change takes place

The discussion on each is summarised below.

6.1 The case for the status quo

The Review Group began by identifying arguments for maintaining the current regime. Firstly, it was noted that there has been no independent study of the impact of the audit exemption since it was introduced in 1999, even though the audit exemption thresholds were increased in 2006 and 2012. The lack of statistical data in the public domain on the size of Irish companies (see above), coupled with the absence of any research findings on the effects of audit exemption, made it difficult to have any informed discussion on the regulatory impact.

The Review Group discussed the value of an audit, which is an indicator of compliance and can serve as a useful early warning to creditors and enforcement bodies, especially if there is a qualified audit report. The fact that financial statements have been subject to audit by an independent auditor gives some reassurance to Revenue as to the accuracy and compliance of the company involved. The extensive list in the Second Schedule to the Companies (Amendment) (no.2) Act 1999 of companies that are excluded from the audit exemption, is evidence of the role of audit in providing reassurance, and support to compliance, in the case of financial companies and other undertakings with a wide range of stakeholders. Revenue considers that there is a similar public interest in ensuring that more company accounts, on the basis of which taxes are computed, are not exempted by an easing of the current requirements. Any increase in the number of companies entitled to an exemption from the requirement to audit would obviously increase the number of cases without this support to compliance. Accordingly, Revenue did not support the proposal to reduce the criteria and so bring in more companies within the scope of the exemption. The Irish Congress of Trade Unions supported this view, pointing out that this is a time when the public interest generally and stakeholders, including employees, customers and all who interact with companies and organisations need confidence in the probity of Irish business. This is particularly so when, to date, we do not know to what extent, if any, failures of compliance or in the audit process generally, have contributed to the economic crisis. ICTU argued further that it is not at all clear that current requirements are being complied with.

Secondly, the Review Group heard the ODCE's view that the absence of audit has led to poorly constructed financial statements. While the Review Group had reflected on the view expressed by the ODCE concerning the deterioration in the quality of accounts, it was noted that only anecdotal evidence had been supplied to support this.

As part of this discussion, the developments in iXBRL for filing financial statements (at present it is proposed that this will be mandatory for all companies, including audit exempt companies, from 2015), were noted and described as facilitating a more focussed risk assessment for Revenue, although Revenue confirmed that its view on who should qualify for the audit exemption, as set out above, was unchanged by the move to iXBRL.

Related to this point, the ODCE has argued in the past that the lack of any professional oversight of the activities of thousands of small companies leaves them exposed to the potential for poor business practice, and even illegal practice, perhaps unknowingly. There was reference too to the benefits of an audit report where the company had a diverse shareholder base or fluid investment. In those cases, there are many and varied people with a stake in a company's success, including employees and consumers, who would find audited accounts very useful. ICTU agreed with this view. The counter argument is that the audit exemption already provides protection for such a company as a qualifying minority may require an audit, although it was pointed out that this is neither open to other groups of stakeholders nor has a bearing on the public interest.

The Review Group then considered the legal obligations on the auditor, in particular the obligation to report certain irregularities to law enforcement bodies. It was argued that where there is no auditor, there may be no report, for example to the ODCE, of irregularities, and no independent witness if those irregularities become the basis for legal action. The contrary view is that most small companies have their accounts drawn up with the assistance of external accountants even where they avail of audit exemption, and such accountants owe obligations under section 59 of the Criminal Justice (Theft and Fraud Offences) Act, 2001 to report offences coming to light in the preparation of accounts. ICTU pointed out here that the duty of accountants under this provision is in respect of suspected criminal offences as defined within the Act (with certain exclusions) and, taken in the round, this is a narrower duty than that owed by an auditor in general.

Finally, the Review Group looked at the experience abroad and noted the UK's consultation paper, published in October 2011. At that time, the UK required companies to comply with both monetary criteria only. When they were proposing to make it easier for companies to meet the criteria by including a third optional criterion (average number of employees) while maintaining the number of criteria that must be satisfied at two, the UK authorities said that they were not aware of any obvious risks in the proposal.

The difficulty in assessing the effect of change in Ireland, the impact for enforcement of allowing even more companies to be exempted, and the benefits of an audit were considered the main reasons in favour of maintaining the law as it is.

ICTU noted that the evidential deficiencies in all of the areas already enumerated above are serious concerns.

6.2 The case for change

As before, the Review Group began with a discussion on the value of an audit, noting that its primary purpose is for the shareholders, with the interests of other stakeholders being secondary. A specified minority of members have the right to require that the statutory accounts be audited. Moreover, regardless of whether a company's accounts are audited, the Committee heard that most small private companies would have their accounts prepared by outside professional accountants, in line with the appropriate standards. The Review Group also recognised that an audit is no guarantee that a company will survive.

The Review Group then considered the claim that reducing the number of criteria would reduce the costs and administrative burdens on business. It is often argued that audit is an unjustified and disproportionate requirement for small companies and that audit exemption does not relieve the directors from the responsibility of presenting financial statements which give a true and fair view of the company's financial position. While representatives of the accountancy profession on the Committee were unable to confirm the average cost of an audit, they did consider that earlier estimates, prepared for the High Level Group on Business Regulation, putting the average cost at €2.2 k, seemed low.

Another consideration was that there would continue to be many reasons why companies would choose to have their accounts audited even where they could qualify for the exemption. For example, companies that incur borrowings from banks or are parties to public procurement contracts may be obliged to furnish audited accounts. Although opinions were divided on this point, the majority felt that in such cases market forces alone should determine whether the accounts of such companies should be audited.

The Review Group, having already noted the reporting obligations on auditors, also noted the obligations under section 59 of the Criminal Justice (Theft and Fraud Offences) Act 2001 on "a relevant person" to report information to the Gardaí. Therefore, there may be people other than the directors who would be required to report wrongdoing coming to light in the preparation of accounts even where the accounts are not audited.

Looking again at international experience, the Review Group noted that Ireland is almost unique within the EU in requiring companies to meet all three criteria. From a competitiveness perspective, it could be argued that Irish companies are at a disadvantage vis-à-vis their counterparts in other parts of Europe. Since August 2012, Ireland has gone to the maximum thresholds allowed under EU law, and therefore aligning itself with the other Member States on the number of criteria would be consistent with recent developments. It was also mentioned that in the USA, subject to certain exceptions, there is no requirement for an audit of any company that is not listed, regardless of size.

The costs of an audit, the position of Ireland as unusual within the EU in requiring companies to meet all three criteria and the fact that directors would continue to have a duty to produce annual accounts that give a true and fair view coupled with the reporting obligations on any accountant preparing those accounts were considered the main reasons for change.

6.3 Should any of the criteria be mandatory?

The next question was whether any one or two of the criteria should be made mandatory. Here, the Review Group discussed each criterion in turn. It was noted that, until last year, the UK had made both monetary criteria mandatory. As a general rule, turnover and employee numbers could be seen as indicators of the level of business activity, while the balance sheet total was indicative of the value of a company. While Revenue did not support change, if change is to be recommended, it proposed that the requirement for no more than 50 employees be made mandatory, as the number of employees gives an indication of day to day operational activity and is an indicator of potential direct tax and fiduciary tax liabilities. While section 285 of the Companies Act 1963 already provides a Revenue preference for fiduciary taxes in the winding up of an insolvent company, the amount recoverable is dependent on the funds remaining in the company at the time of liquidation. The greater the number of employees in the company, the less likely it is that the PAYE / PRSI liability will be recoverable. If the requirement for no more than 50 employees was made mandatory, then in Revenue's view this would greatly reduce the risk of lost tax to the State. Another argument in favour was that any company with more than 50 employees should conduct an audit as a matter of good practice and corporate governance.

It was noted that this issue is particularly difficult to assess, because the information on the likely effect of making any one of the three thresholds mandatory is so patchy.

A small majority of the Review Group was in favour of allowing the company to meet any two of the criteria without further restriction. However, there was a significant minority in favour of requiring the company to meet the criterion of not having more than 50 employees and the Review Group recognised that there is not necessarily an objective right or wrong position on this point that will ultimately be decided by Government policy.

6.4 New safeguards

The Review Group then turned to the question of whether there might be a need to put new safeguards in place if the criteria were reduced to two out of three. The Review Group began with a survey of the existing safeguards and noted that the legal obligations on companies to file annual accounts and on directors to ensure that those accounts give a true and fair view would remain in place. Indeed this obligation is made even clearer in the Companies Bill 2012.

Another safeguard is the fact that the exemption is limited to certain types of companies, with others excluded regardless of size.

Perhaps the most significant safeguard is the fact that a company will lose the right to claim the exemption for two years if it does not file its annual return on time. This is considered by many to be disproportionate, and was mentioned in several of the submissions made to the Department of Jobs, Enterprise and Innovation under the public consultation that was undertaken alongside the CLRG's consideration. However, the Review group, in 2011, examined this measure and concluded that it was appropriate, a view that was reflected in this discussion.

It was also noted that it is always open to a qualifying number of members to require an audit if they wish.

The European Commission's survey of regimes in the Member States did not reveal any additional safeguards in the other 26 countries. The Review Group also received information, courtesy of ISME, on the regimes that are in place in 9 other EU Member States (i.e. UK, France, Sweden, Italy, Finland, Germany, Belgium, Spain and the Netherlands). Most other EU countries require companies to meet two of three criteria.

In any case, four possible new safeguards were considered. The first was the Revenue's proposal that companies benefiting from the audit exemption would be required to have an audit at intervals of, say, 3 or 5 years. A counter argument to this approach is that an auditor could not stand over the opening figures, so the final report would contain substantial caveats. The representatives of the accountancy profession on the Review Group were of the opinion that an occasional audit would be impractical.

The second possibility was to restrict the new style exemption (i.e. meeting just two criteria) to just a few company types, rather than to all company types that currently benefit from the exemption, or to introduce the new rules on a phased basis, starting with the private company limited by shares. However, given that the private company limited by shares is the largest group of companies by far, it was considered that any phased approach that started with that group would be meaningless. As noted above, the Companies Bill 2012 proposes to extend the existing exemption to companies such as guarantee companies, so this would need to be taken into account in shaping such a new restriction. A phased approach was not considered useful.

Another possibility for a new safeguard concerned groups of companies. It was noted that, although section 17 of the Companies (Amendment) Act 1986 is solely concerned with exemption from the requirement to annex accounts to annual returns, it could be a basis for requiring parent companies of groups to provide guarantees for subsidiary undertakings seeking audit exemption. This is an approach taken in the UK. However, this will need more thought as the Irish regime for groups is different from the UK's. Here, we require that the entire group be under the thresholds, while the UK only considers the size of the subsidiary. The Review Group did not have sufficient time to examine this possibility fully.

Finally, the Review Group examined a proposal that the ODCE be given a power to investigate whether a company was falsely claiming an audit exemption. Where a company claims audit exemption, it is also entitled to file abridged financial statements. As such, it is not possible to ascertain from the filed financial statements whether the company's claim to audit exemption is valid since, for example, annual turnover is not required to be disclosed in abridged accounts. Under the Company Law Enforcement Act 2001, the ODCE can only require the production of documents where (in broad terms) the Director forms the opinion that there are circumstances suggesting fraud or prejudice. Alternatively, if the ODCE wishes to enter a premises to obtain relevant documentation, it must do so on foot of a Court Order after demonstration to the satisfaction of a District Court judge that there are reasonable grounds for so doing. The ODCE's legal advice is that this sets a relatively high threshold before the books and records of a company may be inspected. As such, the power of the ODCE to review a claim to audit exemption (where it had a suspicion that a company was not entitled to claim exemption from audit because it did not meet the criteria) under the current law is very limited. The suggested proposal would provide the ODCE with the power, without the difficulties set out above in relation to the making of a Court application, to ascertain whether a claim to audit exemption is valid. This is similar to the current powers of the ODCE to inspect the minutes of meetings of companies, and to inspect the register of directors' interests in contracts.

The Review Group recalled that this issue was aired at the CLRG before, possibly in 2005 or 2006. However, it was agreed that, given the passage of time, it was worthy of new consideration.

In this latest discussion, there were strong views both in favour and against this proposal.

Those in favour saw this as appropriate in light of the possibility that the qualification for the audit exemption would be changed to allow more companies to benefit. Already, the majority of companies may claim the exemption, with more due to come into scope under the Companies Bill 2012. At present it is not possible to know whether a company meets the criteria or not as they are not legally obliged to furnish the supporting evidence. Given those facts, it was argued that an enforcement power is needed. Moreover, as the role and oversight of auditors is enhanced in legislation, it is proper that there would be a similar enhancement of the oversight of the many companies that are not audited. They also argued that this would not represent an additional burden on companies. However, as things stand, the requirements placed on the ODCE to pursue this type of abuse, in particular to have some independent evidence, represent a significant barrier to any investigation.

Those against said that there was no evidence of abuse of the exemption and that giving the ODCE this new power would be a disproportionate response. Other EU countries that have the exemption and only require companies to meet two of the three criteria do not seem to need additional safeguards. The aim of the exemption is to simplify the running of business and introducing such a new power would run against that intention. Furthermore, the ODCE, whether working on its own or following consultation with the Revenue, has sufficient powers to identify and pursue such abuse.

In the end, a majority of the Review group agreed that it would be appropriate for the ODCE to have a limited power to ascertain whether or not a company was entitled to claim the audit exemption. This power would have to be framed with reference to constitutional protections. A minority considered that it was not warranted.

6.5 Should any company type be excluded?

Financial companies listed in the Second Schedule to the Companies (Amendment) (No.2) Act 1999 do not qualify for the audit exemption regardless of whether they meet the exemption criteria. Securitisation companies falling within section 110 of the Taxes Consolidation Act 1997 are not specifically listed in the Second Schedule. This is not an issue at present as it is unlikely that such companies qualify for the audit exemption as they would not generally be in a position to satisfy all three criteria. However, if the requirements are changed, then many such companies could qualify for the exemption which is of concern to the Revenue. Section 110 companies often hold large amounts of financial assets on their balance sheet, but may have little turnover and no employees. It is important, in the case of companies raising finance backed by financial assets that high quality financial information be available. For these reasons, the Review Group recommended the inclusion of section 110 companies in the Second Schedule.

The Review Group clarified that it was recommending that section 110 companies be included in the Second Schedule for the purposes of the audit exemption only. There are other consequences of being listed in that Schedule, such as the requirement to notify an application for examinership to the Central Bank, that were not the subject of this discussion but will need to be kept in mind when it comes to drafting any new legislative provisions.

7 Findings

A difficulty encountered by the Review Group was the lack of statistical information on the number and types of companies that currently meet each of the three criteria. The Review Group considered itself hampered by this lack of information and the inability to assess the types and numbers of companies that would come within scope if they could avail of the audit exemption by meeting just two of the criteria. Given that information deficit, the Review Group tried to identify risks in extending the exemption. Here, the reservations of the Revenue and the ODCE were considered.

The majority of the Review Group agreed that the benefits of allowing more companies avail of the audit exemption outweighed the risks. This was based on a number of factors. Firstly, the Review Group found no firm evidence of abuse of the existing audit exemption, although it was pointed out by the ODCE that, in the absence of investigative powers, it was all but impossible for such abuses to be discovered. Similarly, the Review Group found no evidence of widespread deterioration in the quality of financial information following its introduction in 1999.

Secondly, exemption from audit is not an exemption from the directors' duties to provide annual accounts that give a true and fair view. Indeed it was argued that this duty, together with related duties on directors, will be strengthened by the Companies Bill 2012.

Another factor supporting the majority view was the EU regime. Irish companies may be at a competitive disadvantage vis-à-vis their EU counterparts in having to meet all three criteria, and there was no evidence from the other Member States of abuse as a result of reducing the criteria to two out of the three. Moreover, the recently adopted Accounting Directive (Directive 2013/34/EU) removes the requirement for audited accounts from virtually all small companies, the exception being "public interest entities", such as financial institutions and insurers. In national law, we have restructured company law in the Companies Bill 2012 to place the private company limited by shares in primary position. This is to reflect the fact that this is the most popular company form by far. On the subject of EU law, ICTU said that it was worthy of note that

that there are few exemptions with regard to health and safety compliance, regardless of organisational size. In this context, an audit of company accounts could be said to deal with the financial health and safety of a company, of interest to a potentially wider range of stakeholders than obtains under the health and safety legislation.

With regard to the question as to whether any one or two of the criteria should be made mandatory, opinion was divided almost equally as to whether or not any one or two were more important that the others. The Revenue's proposal to make the number of employees mandatory was considered, as was the counter view was that it should be left to the company to decide which of the two criteria to meet.

Turning to the question of new safeguards, the Review Group agreed that most of the safeguards that it had considered would not be warranted if the criteria are reduced to two. Here, the proposal to give the ODCE an additional new power to ascertain the validity of a claim to audit exemption, was supported by the majority of the Review Group.

In looking at the existing law, the Review Group considered that there were a few areas that warranted review. The first of these is the types of companies that are currently excluded from availing of the audit exemption. These include companies listed in the Second Schedule of the Companies (Amendment) (No.2) Act 1999. The Review Group recommends that such companies should not be permitted an audit exemption.

In addition to the specific questions referred to the Review Group, some other features of the audit exemption were examined and findings made.

The Review Group also considered whether it was advisable to review the provisions that allow members to object to a company taking up the audit exemption. In the case of private companies (whether limited by shares or, under the Bill, by guarantee), 10% of the members must object, but in the case of a public guarantee company, only one member may object. This provision gives effect to an earlier CLRG recommendation. In the time allowed, the Review Group did not come to any conclusion on the implications of this distinction for an extended audit exemption. However, it did consider that this difference in approach should be taken into account if the audit exemption is changed to allow companies meet just two of the criteria. This would be a matter for the Department to examine in the course of implementation.

The Review Group also considered the qualification period for the exemption. Irish law requires that a company satisfy the criteria for a year, but the Fourth Directive refers to a period of two years before becoming eligible. The Review Group understands that the Department is examining this point with a view to amending the legislation if necessary.

8 Recommendations

1. The majority of the Review Group recommends that the Companies Acts be amended to allow companies that meet two of the three criteria to qualify for the audit exemption. Revenue and ICTU had a strong preference for maintaining the qualifications as they are.

2. A small majority of the Review Group recommends that a company will be allowed to meet any two of the three criteria. However, there was a significant minority in favour of requiring a company to meet the criterion of not having more than 50 employees. The Review Group recognised that there is not necessarily an objective right or wrong position on this point that will ultimately be decided by Government policy.

3. That the audit exemption should continue to be available to all the company types that it is currently open to, including those that will come within scope once the Companies Bill 2012 is enacted.

4. That the definition of the types of companies excluded from audit exemption should be amended. Accordingly, as set out above, the Review Group recommends that section 110 companies should be listed in the Second Schedule to the Companies (Amendment) (No.2) Act 1999 in order to ensure that they cannot qualify for the audit exemption. This should be done at the same time as the first recommendation above is given effect. This recommendation does not extend to the other provisions of company law that affect companies on the Second Schedule.

5. That the Department considers the provisions in the Companies Bill 2012 that extend the audit exemption to private guarantee companies, with a view to deciding whether the requirement for 10% of members to object to the uptake of the exemption should remain intact in light of the changes proposed in the first two recommendations above.

6. On the question of new safeguards, the Review Group recommends that company law be amended to give the ODCE a new limited power to ascertain whether or not a company is in fact entitled to claim the exemption, without the need to first get a court order but having regard to the constitutional limitations inherent in the granting of an extra-judicial power to a State agency.

7. While the Review Group did not find any need for any other new safeguards for companies generally, it did consider that the possibility of allowing parent companies to provide guarantees for groups, might merit further consideration. Time did not permit a full consideration of this option.

Appendix 1 to Report on Item 8

Statistics supplied to the Review group by Vision-Net

Shareholders Funds –

- 95,456 companies are under €4.4 million
- 1,343 companies are between €4.4 million and € 7.62 million
- 4,065 companies are over € 7.62 million

Turnover – Figures available for 9,046 companies

NB: Companies that are not required to include turnover in their accounts rarely do include it

- Of the companies with a turnover figure, 5,022 are under €8.8m
- 491 companies are between €8.8m and €15.24m
- 3,531 companies are over €15.24m

Employees – Figures available for 10,310 companies

NB: This figure includes all employees, whether employed in Ireland or not

- 6,307 of them have 50 or fewer employees
- 1,936 of them have more than 50 and up to 250 employees
- 2,067 of them have more than 250 employees

All three types of information available for 5,322 companies

- 1,330 of those meet all three criteria
- 147 meet the turnover and balance sheet criteria but fail the employee count
- 233 meet the employee and balance sheet criteria but fail the turnover criterion
- 174 meet the employee and turnover but fail the balance sheet criterion

June 2013

Appendix 1 to the Annual Report 2013

Committees: Chairs and Members

Item 2 Committee –

To examine the feasibility of amending the Companies Acts to introduce a new structured and non-judicial debt settlement and enforcement scheme for insolvent companies

Chair:	William Johnston
Members:	Jonathan Buttimore
	Jim Byrne & Tom Murphy (Revenue)
	Marie Daly
	Mark Fielding
	Noel Gaughran (Irish Banking Federation)
	Brian Hutchinson
	Esther Lynch (ICTU)
	Ralph MacDarby
	Vincent Madigan
	Kathryn Maybury
	Theresa O'Connor (Central Bank of Ireland)
	Mark Pery-Knox-Gore
	Kevin Prendergast & Conor O'Mahony (ODCE)
	Nóra Rice & Helen Dixon
	Conor Verdon

This Committee was assisted by Ms. Naomi Clohisey and Ms. Aoife Kavanagh who provided legal research.

Item 3 Committee –

To examine whether it is necessary or desirable to provide for amendments to the legislation transposing Directive 2005/56/EC on cross border mergers into Irish law

Chair:	Deirdre-Ann Barr
	Jim Byrne & John Browne (Revenue)
	Stephen Dowling
	Paul Egan
	Joseph Gavin
	Brian Kelliher & Brian Higgins (IFIA)
	Conor Verdon & John Moynihan (Department)

The Committee was assisted by Ms. Gina Conheady of Matheson and by Ms. Marie Dempsey of the Department of Jobs, Enterprise and Innovation

Item 4 Committee –

To examine whether it is necessary or desirable to provide for amendments to the law relating to the representation of a company before the courts

Chair:	Brian Hutchinson
Members:	Jonathan Buttimore
	Helen Dixon
	Stephen Dowling
	Tanya Holly
	Brian Boyle & Marie Hurley (Revenue)
	Ralph MacDarby
	Vincent Madigan
	Kevin Prendergast
	Jon Rock

Noel Rubotham

Conor Verdon

This Committee is assisted by Ms. Naomi Clohisey of the Department of Jobs, Enterprise and Innovation, and has been supported by Mr. Philip McDonald, legal intern with the Department and by students of the UCD Masters in Common Law.

Item 6 Committee –

To examine the need for provisions regarding the re-use of Companies Registration Office Information

Chair:	Helen Dixon
Members:	Jim Byrne
	Paul Egan
	Ralph MacDarby
	Vincent Madigan
	Kathryn Maybury
	John O'Neill (Revenue)
	Kevin Prendergast (ODCE)
	Nóra Rice
	Jon Rock
	Conor Verdon

This Committee was assisted in its work by Mr. Chris Bollard of Arthur Cox.

Item 8 Committee –

To examine the possibility of allowing companies that meet 2, rather than all 3, criteria to qualify for the audit exemption

Chair:	Mark Pery-Knox-Gore
Members:	Jim Byrne & Marie Hurley
	Marie Daly
	Mark Fielding
	Michael Halpenny
	Ralph MacDarby
	Vincent Madigan
	Conall O'Halloran & Aidan Lambe
	Kevin Prendergast
	Jon Rock
	Conor Verdon

This Committee was assisted by Ms. Aoife Kavanagh of the Department of Jobs, Enterprise & Innovation.