COMPANIES
AND
SECURITIES
LAW REVIEW COMMITTEE

DIRECTOR'S STATUTORY DUTY TO DISCLOSE INTEREST (Companies Act S.228) AND LOANS TO DIRECTORS (Companies Act S.230)

DISCUSSION PAPER NO. 8

August 1988

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Preface

Function and Membership

The Companies and Securities Law Review Committee was established late in 1983 by the Ministerial Council for Companies and securities pursuant to the inter-governmental agreement between the Commonwealth and the States of 22nd December 1978.

The Committee's function is to assist the Ministerial Council by carrying out research and advising on law reform in relation to legislation concerning companies and the regulation of the securities industry.

The Committee consists of five part-time members, namely:

Mr. Geoffrey W Charlton
Mr. David A Crawford
Professor H A J Ford (Chairman)
Mr. Anthony B Greenwood
Mr. Donald R Magarey

The Committee's office is at the office of:

National Companies and Securities Commission
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General Aims of the Committee

To develop improvements of substance and form in such parts of companies and securities law as are referred to the Committee by the Ministerial Council and for that purpose to develop proposals for laws:

* which are practical in the field of company law and securities regulation;

* which facilitate, consistently with the public interest, the activities of persons who operate companies, invest in companies or deal with companies and of persons who have dealings in securities; and

* which do not increase regulation beyond the level needed for the proper protection of persons who have dealings with companies or in relation to securities.

In the identification of defects and the development of proposals to have regard to the need for appropriate consultation with interested persons, organisations and governments.

The Reference from the Ministerial Council

The Ministerial Council for Companies and Securities has referred to the Committee "for inquiry and review the following questions relating to directors and officers of companies:

(a) standards relating to their conduct and performance".

Aims of the Discussion Paper

The paper deals with two aspects of the fiduciary duties of directors, the statutory provisions relating to the duty to disclose interest and the statutory regulation of loans to directors. There are some problems in the operation of the existing provisions that have been drawn to the Committee's attention. In the course of looking at those problems the Committee has identified others. The Committee wishes to elicit the view of interested persons on matters raised in discussion paper.

Responses Invited

The Committee invites written submissions on the matters dealt with in this discussion paper.

The Committee will assume that it is free to publish any submission, in whole or in part, unless the respondent indicates that the submission is confidential. All respondents will, in any event, be listed in any report made by the Committee to the Ministerial Council.

Submissions should be sent to:

Companies and Securities Law Review Committee
GPO Box 5179AA
MELBOURNE VIC 3001

By 31 October 1988.

DIRECTOR'S DUTY TO DISCLOSE INTEREST
(Companies Act S.228)
LOANS TO DIRECTORS (Companies Act S.230)

Introduction

The principle that each director occupies a fiduciary position in relation to the company is given effect by well-established rules requiring the director to avoid unauthorised conflict of his duty to the company with his interest as well as unauthorised conflict of his duty to the company with a duty owed by him to a third person.

The Companies Act contains no detailed statement of those rules apart from the very generally expressed requirement in the penal provision in s 229(1) that "an officer of a corporation shall at all times act honestly in the exercise of his powers and the discharge of the duties of his office". But there are scattered provisions which, in whole or in part, are based on the principle of avoidance of conflict. Examples include s 229(3) dealing with improper use of information acquired by virtue of position and s 229(4) dealing with improper use of position. Section 128 of the Securities Industry Code dealing with insider-dealing is a cognate provision. This paper is concerned with two other examples of legislative gloss on the case law. They are s 228 dealing with declarations of interest and s 230 dealing with loans to directors.

This paper is about ss 228 and 230 only. The fiduciary principle underlying those sections is so well established and beyond any possibility of being abolished that it is possible to consider the two sections in isolation. Apart from posing a suggestion that the Companies Act be amended to provide a statement of the duty of directors to apply company resources only for the benefit of the company as a whole, the paper leaves for another time the question whether companies legislation should take over from the case law the statement of fiduciary duties of a director.

DIRECTOR'S DUTY TO DISCLOSE INTEREST (Companies Act S.228)

The position under general law on the effects of director's interest

1.1 An interest of a director in a transaction with his company can make the transaction voidable at the election of the company unless:

(i) the company in general meeting or all the members informally authorise or affirm the transaction after being fully informed; or

(ii) the rights of innocent third parties have intervened.

1.2 Under the general law and in the absence of contrary provision in the articles an interested director's abstention from the board's deliberations about the transaction in which he has an interest will not validate the transactions or cure the director's breach of duty. The company is entitled to have the benefit of his participation in the deliberations of the board: Benson v Heathorn (1842) 1 Y & CC 326, 341.

1.3 In relation to particular companies the position under the general law may be modified by provision in the company's articles. Articles may provide that a transaction in which a director is interested is not to be invalid on that account and that a director is not liable to account for a profit made. That article may make those results depend on the fulfilment of certain conditions. Common conditions are that the interested director declare his interest to the board, that he not be counted in determining whether there is a quorum of the board and that he refrain from voting. The last condition is essential for a listed company since the ASX Main Board Official Listing Rules 3L(6) requires that "a director (including an alternate director) shall not vote at a meeting of directors in regard to any contract or proposed contract or arrangement in which he has directly or indirectly a material interest". The rule is not entirely clear. The Committee takes it to mean that a director is not to vote if he is interested and that an alternate director is not to vote if he is interested.

Statutory disclosure requirements for interested directors

2.1 Section 228 of the Companies Code is primarily a penal provision requiring interested directors to declare their interest at a meeting of the board of directors. It is derived from legislation first enacted in the United Kingdom in 1928 to meet the growing practice of writing extremely wide exemption clauses into articles.

Should materiality be a test of matters required to be disclosed?

3.1 Section 228(1), for the most part, requires a declaration of interests whether or not they are material. But section 228(2) excludes an interest as a member or creditor of a corporation interested in a contract if the director's interest "may properly be regarded as not being a material interest". Section 228(2) has no counterpart in the United Kingdom.

3.2 The South African Companies Act 1973 s 234(1) requires a disclosure only where a director is "materially interested" and s 234(2) confines the required disclosure to "any contract or proposed contract which is of significance in relation to a company's business".

3.3 The Ontario Business Corporations Act 1982 s 132(1) requires disclosure where a director "is a party to a material contract or transaction" or "is a director or an officer of, or has a material interest in, any person who is a party to a material contract or transaction".

3.4 It might be argued that the board should have all interests disclosed to it for fear that an interested director might take a mistaken view of the materiality or otherwise of an interest. However, that argument has not held sway in the framing of s 228(2).

3.5 Should disclosure be required only in respect of a material interest?

3.6 How should the word "material" be defined for this purpose? Would it be appropriate to provide that it means an interest that a reasonable person would regard as creating a real sensible possibility that the director could not consider the transaction without being influenced by that interest?

Conflicting Duties

4.1 Where a director has a duty to some third person which conflicts or may conflict with his duty to the company that conflict of duties can constitute a declarable interest within s 228(1). The express reference to conflict of duties found in s 228(5) may be contrasted with the language of s 228(1) which refers only to interest. In the background case-law on civil matters a conflict of duties is as significant as a conflict between the director's personal interest and his duty to the company. It seems desirable to make the position clear in order to provide clear guidance to the commercial community. In referring to conflict of interest and duty it might be better to use language referring to financial interest and also to refer explicitly to conflict of duties.

4.2 Should s 228(1) expressly advert to both types of conflict?

Transaction other than contracts and proposed contracts

5.1 Section 228(1) requires a declaration only in respect of a contract or proposed contract. It does not cover dispositions of property unrelated to a contract, such as a trust.

5.2 In the United Kingdom in the equivalent of s 228 the Companies Act 1985 s 317(5) provides:

"A reference in this section to a contract includes any transaction or arrangement (whether or not constituting a contract) made or entered into on or after 22 December 1980".

5.3 Should s 228(1) require a declaration in respect of a "transaction or proposed transaction"?

Transactions that do not come before the board

6.1 The mischief at which s 228 is aimed would seem to be the existence of a director's unauthorised interest in a company transaction whether it comes to the board or not.

6.2 The Ontario Business Corporations Act 1982 s 132(4) requires that a director shall disclose in writing to the corporation or request to have entered in the minutes of meetings of directors the nature and extent of his interest in a contract or transaction that, in the ordinary course of the corporation's business would not require approval by the directors or the shareholders, forthwith after he becomes aware of the contract or transaction.

6.3 Should s 228 be so worded as to make it clear that a declaration is required regardless of whether the particular transaction comes before the board?

Director's investments in the company

7.1 If a director takes up shares, options or debentures in the company, he is interested in a contract with the company and his interest is required to be declared under s 228(1). That is clearly unnecessary and should be excepted from s 228(1). There are already provisions in ss 231 and 232 under which a director's interest in investments in the company can become public.

7.2 Compare the United Kingdom's Table A regulation 94 excluding from the prohibition on an interested director voting the case where:

"(c) his interest arises by virtue of his subscribing or agreeing to subscribe for any shares, debentures or other securities of the company or any of its subsidiaries, or by virtue of his being, intending to become, a participant in the underwriting or sub-underwriting of an offer of any such shares, debentures or other securities by the company or any of its subsidiaries for subscription, purchase or exchange;"

7.3 The exclusion of a director's investments in the company prompts the possibility that there should be an exclusion of the duty to declare where it appears from the face of any document that comes before the board at a meeting of directors that a director is a party and the board is aware of that fact. The legislation could provide that in those circumstances a reference to the document in the minutes of a meeting of the board shall be prima facie evidence that the board was aware that the director was interested in the transaction. On it being alleged that the board was not aware, the director concerned should bear the onus of proving that the board was aware of his interest.

7.4 Should a director's investments in the company be excluded? Should there be an exclusion of transactions evidenced by documents which come before the board and which show on their face that a director is interested?

Director's guarantee of loan to the company

8.1 Section 228(3)(a) excludes from the interests to be declared an interest of a director who has guaranteed a loan to the company. It does this by deeming him not to have an interest in the contract of loan. In the absence of s 228(3)(a) the guarantor-director could have a personal interest in the company agreeing to give security because, if the guarantor has to pay the debt, he will be subrogated

to the lender's rights against the company. It will often be the case that the availability of a guarantee from a director is the determining factor in favour of the company obtaining the loan.

8.2 Given that the exclusion of guarantees is sound, is there any reason why the exclusion should not apply beyond a guarantee of repayment of a loan to a guarantee of any obligation of the company?

8.3 Section 228(3)(a) allows a director's interest to be ignored where he has given a guarantee for repayment of a loan. For clarification it may be thought that it should also refer to the earlier stage where the director proposes to give a guarantee.

8.4 Should section 228(3)(a) apply in respect of guarantees of any obligations of the company? Should section 228(3)(a) expressly include the case where the director proposes to give a guarantee?

Contract with or for the benefit of a related corporation

9.1 Section 228(3)(b) declares that being a director of a related corporation which contracts with the company or for whose benefit or on behalf of which a contract is made or proposed to be made with the company does not count as an interest.

9.2 Where the company and the corporation are related there is wholly or substantially an identity of interests which effectively excludes any conflict of duties.

9.3 It has been suggested that the exclusion in s 228(3)(b) should be extended to the case where the director is another type of officer of the other corporation.

9.4 It has also been suggested that the exclusion in s 228(3)(b) should be available where the director's interest in the related company is a shareholding which does not exceed a specified proportion of the issued shares of the related corporation.

9.5 Alternatively, it has been suggested that if s 228 is not to be amended so as to reach only material interests, at least s 228(3)(b) should exclude a shareholding in a related corporation that is not a material interest. At present, there are some cases where only a material interest has to be disclosed : see s 228(2).

9.6 The suggestion has in view the wide operation of s 228(3)(b) in relation to validation of a transaction. The limitation to material interests in s 228(2) goes only to the penal effect of s 228. If an arithmetical test is to be used, it might be constituted by an explicit boundary test, as in the Companies (Acquisition of Shares) Code section 11, or it could take the form of a prima facie presumption of materiality once the threshold is crossed.

9.7 An altogether different approach would be to restrict section 228(3)(b) to wholly-owned subisidiary companies, it being necessary in other types of related company to protect the interests of minority shareholders.

9.8 Yet another approach would be to repeal s 228(3)(b) on the basis that the emerging duty of directors to the company to have regard to the interests of creditors of the particular company means that the interests in a parent company and its wholly-owned subsidiary are not necessarily identical.

9.9 In what way, if at all, should section 228(3)(b) be amended?

Interests of persons connected with a director

10.1 Section 228(1) requires a declaration only in respect of a director's own interest. Should it require disclosure of any interest of a relative (as defined in s 5(1)) of the director that is known to the director? Such an extension would be warranted as ensuring disclosure of all material factors which could theoretically cloud or influence the Judgment of a director.

10.2 The United Kingdom Companies Act 1985 s 317(6) requires disclosure of a loan, quasi-loan etc. made by a company "for a director or a person connected with such a director". Section 346 defines a person connected as covering a spouse, child, step-child, associated body corporate, a trustee for the director and a person acting in his capacity as a partner of the director or of a person connected. The United Kingdom's Table A regulation 94 which provides that an interested director shall not vote, deems the interest of a person connected with a director to be an interest of the director.

10.3 It is to be noted that s 230 operates on company loans to director's relatives. If a director is to be identified with his relatives for that purpose, is there any reason why he should not also be so identified with relatives for the purposes of s 228?

The standard of disclosure

11.1 Section 228(1) requires a declaration of the nature of the interest. The remaining directors, in the performance of their duty to act for the benefit of the company, when approving the transaction on its behalf, need sufficient information to enable them to perform that duty.

11.2 Should some standard of disclosure be laid down? At least in a public company should the legislation require that the remaining directors be given as much information as will enable them to consider the transaction with the care that a reasonably prudent person would exercise when acting for himself in a transaction at arm's length?

General notice in advance of possible conflicts

12.1 Section 228(4) enables compliance with s 228(1) by a general notice of future interest by reason of being an officer or member of a specified corporation or member of a specified firm with which any contract may later be made. The general notice can no longer be deemed a sufficient declaration of interest if, by the time of the later contract, the director's interest as declared has increased.

12.2 The Committee notes that because s 228 does not limit the duty to declare interests to a duty to declare only material interests, the general notices provided by directors are often cluttered with irrelevant detail, such as minor shareholdings. There can be an information overflow: directors may, when a particular item is being considered, overlook a declaration made many months earlier in a general notice. Additions to shareholdings through dividend investment plans can also be overlooked. These difficulties would be reduced if s 228 were confined to material interests or conflicts of duties as discussed in para 2 above.

12.3 Should s 228(4) be amended to make it clear that a general notice may be amended from time to time?

Lack of quorum of disinterest directors

13.1 Should s 228(1) require that the declaration be made to members where there is no quorum of disinterested directors?

13.2 Under case law in Australia there is no legal principle that a director having a conflict of interest or a conflict of duties should not be counted in the quorum required for a meeting of directors. Whether he should be counted depends upon whether the articles exclude interested directors: A M Spicer & Son Pty Ltd. (in liq) v Spicer & Anor (1931) 47 CLR 151 at 186-187 per Dixon J (as he then was) followed in Anaray Pty Ltd. v Sydney Futures Exchange Ltd. (1982) 6 ACLC 271. In the Spicer case Dixon J explained English

cases that had held that an interested director could not be counted as cases where there was provision in the articles of association that no director should vote upon any matter in which he should be interested, and the article requiring a quorum was interpreted to mean a quorum of directors none of whom was disqualified by this provision from voting.

13.3 ASX Listing Rule 3L(6) requires that a director (including an alternate director) shall not vote at a meeting of directors in regard to any contract or proposed contract or arrangement in which he has directly or indirectly a material interest.

13.4 Should the principle be that the quorum can only be made up of persons who are not disqualified from voting?

13.5 Disqualifications from voting whether imposed by the articles or the ASX Listing Rules pose the question whether it is only a material interest or a material conflict of duty that disqualifies.

13.6 Should the legislation provide that in those circumstances only a material interest or conflict of duties will disqualify?

Directors with similar individual interests in separate contracts and having mutual voting arrangements

14.1 Where director X, having an interest in a transaction with the company, arranges with director Y who has an interest in a similar transaction that each will vote the same way, each thereby becomes interested in the other's transaction and they are both interested in each transaction. It can happen that there is no disinterested director able to vote. In these circumstances the transaction really requires the approval of the company in general meeting.

14.2 Should s 228 include a statement of that position?

Acquisitions from or disposals to directors and their associated of substantial assets.

15.1 The problem of corporate approval for transactions in which a director is interested is dealt with to some extent by ASX Listing Rule 3J(3). That rule is based on the premise that there are some transactions with directors or their associates which should be considered by shareholders in general meeting regardless of whether there is a quorum of disinterested directors on the board and regardless of dispensations in the articles. Rule 3J(3) is concerned with acquisitions or disposals of assets where the consideration or the value of the assets exceeds 5 per cent of the total issued capital and reserves. It requires shareholders to be furnished with reports, valuations or other material from independent qualified persons sufficient to establish that the purchase or sale price of the assets is a fair price.

15.2 Should that rule, or something like it, be incorporated in legislation so as to provide better sanctions for non-observance than can be provided for non-observance of a listing rule? Given that incorporation, should there then be no disturbance of the position that unless the articles forbid it, an interested director may be counted for the composition of a quorum?

16.1 Articles may provide that if all the directors entitled to vote have signed a document containing a statement that they are in favour of a resolution set out in the document, such a resolution may be deemed to have been passed at a directors' meeting. See Table A regulation 77 and Table B regulation 61.

16.2 Should it be made possible for declarations to be made in resolutions in writing signed by all directors entitled to vote?

16.3 The South African Companies Act 1973 s 236 expressly excludes that way of making a declaration regardless of any provision in the articles.

16.4 Is the facility appropriate only to an exempt proprietary company?

Recording a declaration

17.1 Section 228 imposes duties on a secretary of the company. It implies that the secretary has right to be in attendance at the meeting of directors. Should that right be conferred explicitly?

17.2 Should there be a statutory duty on directors to supply the relevant information to the company secretary? Alternatively, should the secretary's obligation be removed and replaced by a statutory duty on affected directors to record or cause to be recorded the relevant information in the minutes?

Significance of a 228 in civil law

18.1 Although s 228 is primarily a penal provision, parts of it have a bearing on the validity of a company transaction in which a director is interested. Those parts of s 228 are best considered after looking at the general law on the validity of such a transaction.

18.2 The Companies Act does not state the effect on a transaction of the company in which a director is interested. Under case law such a transaction is voidable at the option of the company unless:

(i) the articles provide that the transaction shall be valid; or

(ii) the company in general meeting approves the transaction or all the members assent to the transaction after being fully informed, in either case.

18.3 Section 228 is superimposed on that case law. Section 228 is primarily a penal provision concerned with creating an offence of failure to declare interest. However, s 228(3) operates to save some transactions from invalidation.

18.4 Section 228(3)(a) deems a director-guarantor of a loan to the company not to have a personal interest in the contract of loan. Hence, the contract of loan is not invalid. The suggestions for amendment of s 228(3)(a) set out above in para 6 are applicable also to the operation of s 228(3)(a) as a validating provision.

18.5 Section 228(3)(b) declares that being a director of a related corporation (which contracts with the company or for whose benefit or on behalf of which a contract is made or proposed with the company) does not count as an interest. This provision has a validating effect on the transaction. The suggestions for amendment contained in para 7 above apply to s 228(3)(b) in its validating operation.

18.6 The concluding words of s 228(3) - "but does not affect the operation of any provision in the articles of the company" - seem to allow the articles to provide that being a guarantor and a cross-directorship can still constitute an interest with two results. The failure to declare could be an offence under s 228(1) and would invalidate the transaction. The exact result intended should be put beyond doubt.

18.7 There might be merit in re-drafting the provisions in s 228 so as to make entirely separate provision for the criminal offence and the validity of the transaction. The provision relating to the validity of the transaction could allow for the articles to be stricter than the legislation.

18.8 In any such re-draft should the opportunity be taken to make it clear that non-compliance with the penal provisions has no bearing on the question whether the transaction is valid? Should the object be to leave the civil law principles to apply as if there were no penal provision?

Protection for third parties

19.1 Section 68A protects an innocent third party against prejudice where an officer of a company exceeds his actual authority but keeps within his usual authority and where an officer abuses his authority. It has been suggested that where a director fails to observe s 228 the third party may not be protected by s 68A because none of the assumptions in s 68A(3) clearly covers the case.

19.2 Would there be merit in making some special provision in s 228 which confirms that s 68A applies?

Common seal affixed by person interested in transaction

20.1 When considering the matter of a director's interest in a company transaction one should note also s 80(3). Section 80(3) declares that a contract or other document executed under the common seal is not invalid by reason only that a person attesting the affixing of the common seal was in any way, directly or indirectly, interested in that contract or other document or in the matter to which that contract or other document relates.

20.2 There is a question whether any provision is needed for the case where an interested director executes a contract not under seal on behalf of a company.

20.3 It is to be noted that in relation to transactions authorised by the board and the execution of documents under seal there are really three stages:

(1) the board of directors authorises the transaction;

(2) the board of directors authorises the affixing of the seal; and

(3) the document is executed.

Section 80(3) deals with the third stage. There is a question as to whether legislation is needed in relation to the second stage.

LOANS TO DIRECTORS (Companies Act s.230)

Prohibition of loans to directors as a facet of broad principle

21.1 As noted earlier, the general law permits a director to be interested in a contract with his company if:

(1) the articles allow that;

(2) the company in general meeting approves the transaction after being fully informed; or

(3) all the members assent to it informally after being fully informed.

In general, the Companies Act does not disturb that position. But there is one type of contract between a director and his company which the Companies Act prohibits. That is a contract of loan by which the director becomes a debtor to the company. The prohibition does not apply in respect of exempt proprietary companies.

21.2 Section 230 imposes the prohibition and then allows certain exceptions. It applies to a loan to a director or to certain persons connected with a director. Section 230 also reaches the giving of a guarantee by the company in respect of a loan made by a third person to a director and the provision of security by the company in respect of such a loan.

21.3 The section appears to exist for the benefit of shareholders rather than creditors, since exempt proprietary companies are not covered. The rationale of s 230 appears to be that directors of companies other than exempt proprietary companies should be prevented from mis-using the company's resources.

21.4 There is a question whether s 230 should be replaced or supported by a broad statutory statement of the duty of directors to apply company resources only for the benefit of the company as a whole. At the present time s 230 appears as a measure directed to only one type of breach of that duty. There is a possibility that the very detail of s 230 may divert a person who lacks a grasp of the fiduciary character of a director's office from appreciating the broad underlying principle: it is possible that some directors think that since s 230 is black letter law, loopholes can be exploited. That attitude would involve overlooking s 229(1) which requires a director to act honestly. But s 229(1) may not have the necessary impact because it is expressed in very general terms. Something in between the broad statement in s 229(1) and the very detailed prescriptions in s 230 may be needed.

21.5 Section 230 is aimed at only one way in which the directors' control of company assets can be abused. It does not reach cases where the company purchases property and allows a director to use that property. Even so, the case of a loan is deserving of special treatment in that loans can lead more readily to dissipation of company assets. But should s 230 be changed to appear as part of a measure more general than s 230 but more specific that s 229(1)? The aim would be to remind directors of their responsibility to apply the company's property and to commit the company to obligations only as required by law or where they honestly and reasonably believe that that action will be for the benefit of the company as a whole. What is now s 230 could then appear as an exemplary provision regulating the particular action of making loans to directors. Section 233 could be similarly subsumed. To make clear the position of innocent third parties the new provision could indicate that the protection given by s 68A extends to a case where the directors have been in breach of duty.

Should s 230 extend to financial accommodation for directors and persons connected with them given in a form which is substantially debt but theoretically equity?

22.1 If loans to directors are undesirable then other forms of financing that are similar in function to debt might also have to be covered by s 230. An issue of redeemable preference shares by a company connected with a director might be thought worthy of inclusion where the terms of issue are from a commercial point of view such as to make the issue comparable with a loan.

22.2 Should s 230 be widened to cover investment in redeemable preference shares? Should it extend to all redeemable preference share financing or only certain types? If so, how should those types be defined?

Should the concept of a 'loan' for the purposes of s 230 be defined more widely

23.1 By being confined to 'loans', as normally understood, s 230 may not cover the whole field of the mischief aimed at. Should it be expressly stated that s 230 extends to any credit transaction under which the director would become obliged to pay money to the company? If that were done, presumably, some exception should be made for relatively trivial transactions.

Is the home-purchase exception too narrow?

24.1 The exception by which the company in general meeting may approve the giving by the company of assistance to a full-time employee to enable him to purchase a home may be too narrow in that it does not extend to assistance in making improvements to a home.

24.2 Should there be an extension to meet that case?

Is the provision for certification too narrow?

25.1 So far as the power of a third person to enforce an offending guarantee or security is concerned, s 230(8) allows enforcement only in certain cases. Enforcement will be possible where the company is a proprietary company if the company is certified to be an exempt proprietary company by a director and a secretary before the provision of the guarantee or security. In relation to any type of company, enforcement will also be possible if a director and a secretary have certified the company's freedom from s 230's prohibition before provision of the guarantee or security and the third person did not know, and had no reason to believe, that the certificate was incorrect.

25.2 It has been suggested that s 230(8) is unsatisfactory in that it is not explicit in relation to the effect of a certificate where loans are intended to be rolled over, or where the director will operate on an overdraft or a "come and go" basis, or where the terms of the loan facility are subsequently varied.

25.3 Should s 230(8) be amended to refer to those cases?

Should the exemption in respect of related companies be extended beyond related companies?

26.1 By s 230(3)(b) the prohibition in s 230(1) is stated not to apply:

"(b) to a loan made by a company to, or a guarantee given or security provided by a company in relation to, a corporation that is related to the company if the making of the loan, the giving of the guarantee or the provision of the security has been authorized by a resolution of the directors".

26.2 The exception would seem to be attracted to:

* a loan to a related corporation even though a director of the lending company (or other connected person) has a relevant interest in shares of the borrower corporation of not less than 10 per cent;

* a guarantee or security provided in respect of such a loan.

26.3 The exclusion from the statutory prohibition of loans, guarantees or security which would benefit a related corporation has its rationale in the common control of the lender-company and the corporation which is to benefit.

26.4 A question has been raised as to whether s 230(1) should apply where a loan, guarantee or security is given by a company for the benefit of another corporation that, although not related, is not controlled, on a test of effective control, by any director of the lending company. It has been suggested that there is excessive inconvenience in the present law for a lender to a company affiliated with, but not related to, another corporation which gives a guarantee or security in respect of the loan. It may be that even where a director (or connected person) holds more than 10 per cent of the share capital of the corporation benefited, he will not himself be in a position to benefit because his holding does not carry effective control. On that basis and noting the 20 per cent threshold adopted in relation to sale of control in the takeovers legislation (Companies (Acquisition of Shares) Act s 11), it may be that s 230(1)(a)(iv) should be amended so as to substitute 20 per cent for 10 per cent? It has also been suggested that as a safeguard against improper influence by the director in question, the exclusion should be conditional on that director not taking part in and not voting on the matter at a meeting of directors of the company when the matter is considered. A resolution of the other directors should be required for the loan, guarantee or security to be given.