Commercial Practices and the Consumer Protection Act 2007

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The Consumer Protection Act was passed into law on 1st May 2007. This Act is the most comprehensive reform of consumer legislation in Ireland in the last thirty years. It replaces much of the existing body of law and provides for a range of measures designed to establish a high level of consumer protection in Ireland. The Act is restricted to "Business to Consumer Transactions" and therefore will not affect "Business to Business contracts". A newly formed body known as the National Consumer Agency (NCA) has also been established.

Its function is to promote and protect the interests and welfare of consumers by enforcing this new legislation against non-compliant businesses. It will also educate consumers on their rights and entitlements under the Act and provide up-to-date information to the general public in relation to any changes in the law in this area.

Commercial Practices

Under the new legislation, the hitherto *ad hoc* regime of prohibited offences is now strictly codified. The Act differentiates between the types of "commercial practices" and seeks to ensure that sharp practices of certain unscrupulous traders are punished.

A commercial practice means any conduct by a trader in relation to a consumer transaction, which is made before or during that transaction. Some practices may directly affect and influence a consumer's decision to buy certain products or services and the Act seeks to address those deemed to be unfair, misleading or aggressive.

Unfair Commercial Practices

An unfair commercial practice is a catch-all phrase for illegal practices utilised by traders which may impact on the average consumer's ability to make an informed choice in relation to a product or service. The "average consumer" is a person who is reasonably circumspect, informed and commercially aware. Certain members of the public such as the very young or the elderly are automatically deemed more susceptible to influence by certain commercial practices. A higher standard of care must be exercised by traders when dealing with them.

A commercial practice is deemed unfair if it is contrary to the requirements of professional diligence expected of the trader and if this activity distorts the economic behaviour of the average consumer. Unfair commercial practices comprise both "misleading commercial practices" and "aggressive commercial practices".

Misleading Commercial Practices

A commercial practice is misleading if it contains false or deceptive information which in any way seeks to deceive the "average consumer", causing him to enter into a transaction which he would not otherwise have done. The main characteristics of misleading action are false or inaccurate information such as:

- Displaying a quality mark without having obtained the necessary authorisation;
- Usage and prior history of products;
- Falsely stating that a certain product will only be available for a very limited time, in order to elicit an immediate response from consumers without giving them ample time to make an informed choice.

Aggressive Commercial Practices

Harassment, coercion or exercising undue influence over consumers in an attempt to close a transaction are all prohibited. Pressurising, intimidating and taking advantage of vulnerable consumers are examples of harassment. Other types of aggressive practices include:

- Creating the impression that the consumer cannot leave the premises until a contract has been finalised;
- Conducting personal visits to the consumer's home and ignoring requests to leave;
- Engaging in persistent and unwanted solicitations by telephone, fax or e-mail to that consumer.

Prohibited Commercial Practices

In total, the Act lists 32 commercial practices which have been "black listed" and are prohibited in all circumstances and examples of these include:

- False claims that the trader is about to cease trading;
- Running promotions or competitions without awarding the prizes described;
- Demanding payment for unsolicited goods.

Defences

A trader who sells a product in good faith relying on a representation made to him by a third party can avoid prosecution under the Act. However, the onus is on him to show that he had taken all reasonable steps to check the truth and veracity of any information before releasing this to the general public.

Penalties

A trader found to be acting in breach of the Act can potentially face a fine of up to €150,000 and/or up to five years imprisonment. As the aim of the legislation is the protection of consumers, the NCA and individuals are empowered under the Act to seek an injunction to prevent the continuance of the unlawful activities. The Courts also have the right to order the payment of compensation to those consumers who have suffered loss at the hands of any convicted traders.

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Management Companies

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It is estimated that up to 750,000 residents in Ireland are presently living in apartments or multi-unit developments. There are approximately 4,600 property management companies which own and control the common areas such as gardens, car parks, entrances, corridors and stairwells in these developments. These management companies also arrange for the insurance on the premises, waste disposal, general security and building maintenance.

However in the recent past, the Office of Director of Corporate Enforcement has reported a sharp increase in complaints about the governance of these common areas and in particular the action, or in some cases inaction, of the apartment management companies to solve problems for the residents. While certain progress has been made to improve matters, the Law Reform Commission has recommended that regulation of the multi-unit development sector is imperative.

The current practice is for the management company to be set up as a public company limited by guarantee and having shares. There was no requirements to file accounts and this structure also provided for ease of change of members.

A private company limited by shares is usually not suitable because, as the law stands, it must have a share capital and be limited to 99 members. Many multi-unit developments will comprise more than 99 apartments or other units, all the owners of which should become members of the management company. Despite this, the Law Reform Commission has been made aware of a number of management companies having been incorporated as private companies.

A new set of proposals from the Company Law Review Group makes provision for management companies to be set up as either Designated Activity Companies (DAC) or as a Company Limited by Guarantee (CLG). These new corporate entities are seen as more convenient and appropriate to use as vehicles to set up management companies.

A DAC is a private company which is either limited by shares or by guarantee and will have the capacity to do only those acts that are set out in its constitution. The Objects clause in a management company will be strictly limited and will be sufficiently confined to encompass only activities necessary to the performance of the companies' duties.

Alternatively, a management company could be incorporated as a CLG. This means that the company would not have a share capital. The liability of its members would be limited by the constitution to the amount which the members undertake to contribute to the company in the event of it being liquidated. Thus, if a member guarantees to contribute €10 to the company, their ultimate liability to the company will not exceed this amount.

Whichever vehicle is used to incorporate the management company, it is proposed to have a new definition of it included in the constitution of the company. Furthermore, any company incorporated under the new scheme will be required to adhere to a strict set of objects and not to diverge from these. Management companies which have already been incorporated will be obliged to change their status as the old company classifications will become obsolete.

It should be noted that these proposed legislative changes will not solve the age-old problem of how commercial and residential tenants who occupy the same development should have their management fees apportioned. Typically, commercial tenants will want the right to vote in relation to issues which solely relate to the commercial units and this will hold true for those tenants in the residential units. Therefore it will be necessary to distinguish between the number of members and the number of votes held by each member. This could be achieved by apportioning management fees between commercial and residential tenants according to the square footage which they occupy or on the basis of the specific location which the tenant occupies in the development

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Audit Exemption

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All limited liability companies are required by law to have their accounts audited annually. The audit is an independent examination of the accounts of a business, which verify that they have been prepared in accordance with company law and that they show a true and fair reflection of the company's financial state of affairs. The audited accounts are then annexed to the company's annual return, which is filed in the Companies Registration Office.

The requirement for every company to have their accounts audited was seen as imposing an onerous burden on many small and medium enterprises (SME's). The associated cost was perceived to outweigh the attendant benefits given that in many SME's, the managers and shareholders were the same people. However, subject to your company fulfilling criteria, it is possible to avail of an exemption from the statutory audit requirement. In order to do so, your company should:

- Have a turnover of less than €1.5 million;
- Have a balance sheet total not exceeding €1.9 million at the end of the financial year;
- Employ no more than 50 people;
- Be up to date in its filing requirements;
- Not be part of a group of companies.

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Management Companies (Cont'd)

It is also proposed to set up a Regulatory Body which will have as its remit to assist management companies, register all multi-unit developments and to investigate any complaints involving these developments.

It is to be hoped that these legislative changes will lead to an improvement on the present *status quo* when the new Company Law Consolidation Bill comes into force in late 2008.

Loans between Companies and Directors

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Section 31 of the Companies Act 1990 prohibits a company from making a loan to a director (or a person connected with a director) of the company or of its holding company.

This prohibition is not solely limited to loans and includes certain specified transactions:-

(a) quasi-loans i.e. transactions where one person pays or agrees to pay a sum for the borrower;
(b) credit transactions e.g. hire purchase agreement. This would include the supply of goods or services where the money due is deferred or payable by instalments. It also includes a licence or lease of land;
(c) guarantees in connection with a loan, quasi-loan or credit transaction;
(d) or the provision of security in connection with loans, quasi-loans or credit transactions – this would include a mortgage, charge, or lien against an item of property made by a person e.g. a bank to or for the benefit of directors or persons connected with directors.

Who is a "director"?

The definition of director under the Act includes shadow directors. A shadow director is a person in accordance with whose directions or instructions the directors of a company are accustomed to act. It also includes a *de facto* director. This is someone who acts as a director of a company although he has not been formally appointed as such.

So who is connected with a director?

A person is connected with a director of a company if that person is a:-

- spouse;
- parent;
- sibling;
- or child of that director; or
- a person acting as a trustee of a trust, the principal beneficiaries of which are that director or someone connected with the director; or
- a person who is in partnership with that director; or
- a body corporate controlled by that director.

A director controls a body corporate if he either on his own or together with another person connected with him has

- an interest in 50% or more of the shares of the body corporate; or
- is entitled to exercise or control the exercise (either directly or indirectly) of 50% or more of the voting power at general meetings of that body.

In other words, the director must "own" shares in the body corporate. A director does not have to be the legal and registered owner of the shares; beneficial ownership is sufficient.

Body corporate is a much wider expression than "company" and can include a company registered outside Ireland.

What are the consequences if a transaction contravenes Section 31?

- the transaction is voidable at the instance of the company;
- the directors may be made personally liable for the debts of the company if the company goes into liquidation; and
- officers of the company may be found guilty of a criminal offence.

THE EXCEPTIONS

There are five exceptions to the basic prohibition set out in Section 31.

1. Section 32 – *de minimis*

Section 32 provides:-
Section 31 shall not prohibit a company from entering into an arrangement with a director or a person connected with a director if the value of the arrangement is less than 10% of the company's relevant assets.

This exception applies only to loans,

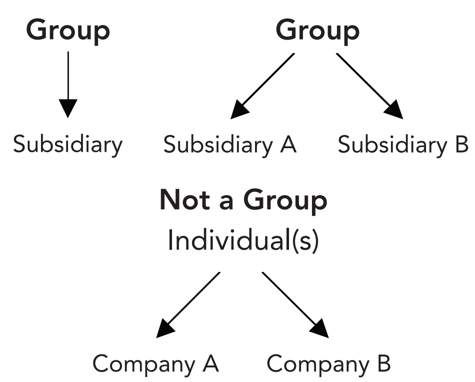
Loans between Companies and Directors (Cont'd)

quasi loans and credit transactions. It does not apply to guarantees or other securities. Basically, small arrangements may be entered into without breaching Section 31 if the value of the transaction is less than 10% of the value of the relevant assets of the company.

If it is intended to use this section, great care should be taken in valuing the transaction in the first place and subsequently reviewing that value on a regular basis.

2. Section 35 – the Group exception

Any member of a group of companies can make or enter into any of the transactions prohibited by Section 31, provided the transaction or arrangement is in favour of any other member of the group i.e. parent or subsidiary. However, the section only applies where there is a true group of companies.



3. Section 36 – Director's expenses

This exception saves transactions where a company guarantees a director's credit card or loans him money to pay expenses. However any such loan must be repaid to the company within six months from the date on which the liability was incurred.

This exception only applies where the director is liable to repay the company in respect of credit provided to discharge business expenses. However, if the company discharges the expenses itself and the director has no liability to repay, then Section 31 does not apply as there is no loan, quasi-loan or credit transaction.

4. Section 37 – Business Transactions Exception

Section 37 provides that Section 31 shall not prohibit a company from making a loan if the company enters into the transaction concerned in the ordinary course of its business. The value of the transaction should not be greater than and the terms in which it is entered into should not be, more favourable than those which the company ordinarily offers to a person of the same financial standing who is unconnected with the company.

"Ordinary course of business" is not defined but it would have to be usual for that company to enter into such a transaction. The exception would apply, for example, to loans and quasi-loans made by money lending companies, banks and other financial institutions.

5. Section 34 – "Whitewash procedure"

Section 34 allows a company to give a guarantee or other security in respect of a loan, quasi-loan or credit transaction to a director or connected person of the company or its holding company provided that the members pass a special resolution to approve the transaction and provided that prior to passing the special resolution, the directors have made a statutory declaration of solvency.

Section 34 does not allow the company to make a loan to a director - the company is confined to providing a guarantee of such a loan.

It is imperative that the requirements of Section 34 are strictly observed because

i) The statutory declaration has no effect unless it is accompanied by a report (in the prescribed form) by an independent person (who may be the auditor) as to whether in their opinion the statutory declaration is reasonable; and
ii) Any director making the statutory declaration without having reasonable grounds for being of the opinion that the company, having carried out the transaction, will be able to pays its debts in full as they become due may be made liable for some or all of the debts or other liabilities of the company. There is a presumption that if a company is wound up within the period of 12 months after the making of the declaration and the debts are not paid or provided for in full, the director did not have reasonable grounds for his opinion.

With the introduction of the Investment Funds, Companies and Miscellaneous Provisions Act 2006, the threshold figures for turnover and balance sheet assets were revised upwards to €7.3 million and €3.65 million respectively. The effect of this revision is that many more SME's can now avail of this exemption as they will fall under these thresholds. This will have the effect of cutting administrative costs which were in many instances seen as superfluous in the first place. This new regime will apply to companies whose financial year commences on 1st January 2007 or ends not earlier than 24th February 2007.

To avail of the audit exemption, a board resolution should be passed allowing the company to waive the requirement to appoint an auditor and this decision should be specifically recorded in the minute book of the company. In order to protect members' interests, once the auditor receives notice of his termination, he is under a duty to declare that there are no accountancy matters which should be brought to the members' or creditors' attention. Furthermore, a member holding not less than one tenth of the voting rights in the company may request that the exemption be waived for the financial year in question if he or she is of the opinion that an independent audit on the company's books is necessary.

This is seen to be a positive step to remove some of the administrative red tape for a large number of SME's and has been roundly welcomed as a sensible and practical development to the audit requirement.