Article

The position and liabilities of the partners

The rules governing the rights and duties of the unlimited partners are similar to those governing the partners in an ordinary commercial partnership (sensu Handelsgesellschaft, OHG). Thus the unlimited partners are normally entrusted with the management and representation of the partnership in accordance with paragraphs 114 et seq and 125 et seq of the Commercial Code and are not permitted to compete with the partnership. In addition, unless the articles provide otherwise, they have a right to withdraw funds from the partnership (Einschlusserlös) similar to that enjoyed by the partners in an ordinary commercial partnership.

The limited partners are excluded from the management of the ordinary business of the company (Commercial Code, para 164) but their assent to extraordinary transactions is required. They are granted certain controlling rights by paragraph 166, for example the right to examine the balance sheets and the partnership books. Sometimes a limited partnership which invites subscriptions from the public has a supervisory board made up of limited partners which exercises the rights to assent to extraordinary transactions and the controlling rights given by paragraphs 164 and 166 respectively. It is possible for the articles of the partnership to grant more extensive rights to the limited partners than those given by paragraphs 164 of the Code, the limited partners may thus be given the right to issue instructions to the unlimited ones. The limited partners as well as the unlimited ones have the duty of acting in good faith towards the partnership. This duty of the partners does not seem so far-reaching as that of the unlimited ones. Unless the articles provide otherwise, the limited partners (unlike the unlimited ones) are not prohibited from competing with the partnership (in this sense Kübler and Assmann, Geschäftsgesellschaft, 16th ed., F Müller Verlag 2005, p 105). Clauses restricting such competition must be compatible with German competition law and European Community law.

The assets of a limited partnership are in the collective ownership of all the partners, including the limited ones. The amount of a partner’s share in the partnership’s capital determines his participation in the partnership profits and losses; the shares of the individual partners in a limited partnership may differ in amount. That of a limited partner is dependent on the amount of his contribution to the partnership’s assets, and may not exceed the amount of his contribution. Each partner is entitled to a 4 per cent dividend from the annual profits. The remainder of such profits, together with any losses to be allocated (ingenorens), in accordance with paragraph 168(2) of the Commercial Code. Any losses are written off as a reduction of the partners’ share value. If the value of a limited partner’s share falls below his original contribution, or becomes negative, it has to be restored to its original amount before any dividends may be paid (Commercial Code, para 169(1)). A limited partner is only required to pay any outstanding amount of his contribution in the dissolution of the partnership.

According to paragraph 170, a limited partner has no right to represent the partnership. If he is permitted to represent it in respect of transactions with third parties, he loses his limited liability. However, it is possible to grant him a power of attorney (Handlungsbefugnis) or a full power of representation (Vollmacht) in accordance with paragraphs 48 et seq of the Commercial Code. Certain transactions of a fundamental nature, including the sale of the business and all its assets require the consent of the limited partners (Kühler and Assmann, op cit, p 106).

The creditors of the partnership may demand satisfaction from the unlimited partners out of their own assets, in accordance with paragraphs 124(1) and 161(2) of the Commercial Code. The liability of the limited partners to such creditors is governed by paragraph 171(1) of the Code, and only extends to the amount of the contribution. The limitation of liability is dependent on the partnerships being entered in the Commercial Register. Unlimited liability will be imposed on limited partners in respect of pre-registration of transactions if after such registration the relevant entity has engaged in commercial transactions and such limited partners had then agreed to the continuation of business.

The limited partner is no longer liable once the relevant contribution is made. This may take the form of the provision of cash, things, rights or services. Such contributions have effect as against creditors in accordance with their market value. Contributions may take other forms, for example the set-off of a debt due from the partnership or the failure to accept dividends due to the limited partner. It follows from paragraph 172(4) of the Commercial Code that the limited partner’s liability in respect of his contribution revives if this, or part thereof, is returned to him, for example through the payment of dividends to him when the value of such contribution has been reduced as a result of losses incurred by the partnership. If the other partners agree to the release of such liability this has no effect against the partnership’s creditors. Paragraph 172(3) of the Code provides that dividends which have been distributed in good faith on the basis of a proper balance sheet and payments thereof received in good faith do not have to be returned to the partnership by a limited partner.

If a person becomes a limited partner in an existing commercial partnership, he has limited liability for the latter entity’s debts which have already been incurred, in accordance with paragraph 173(1) together with the claimant agency will issue a claim form and make an application supported by a witness statement setting out the evidence to establish the claim;
The German limited and silent partnerships

by Frank Wooldridge

INTRODUCTORY REMARKS

Both the above types of entities exist in France as well as Germany. The limited partnership exists in the United Kingdom, but not at present, however it has been found valuable in the North Sea continental shelf oil industry. The German limited partnership is defined in paragraph 161 of the Commercial Code as a partnership carrying on a commercial activity under a common name by which at least one partner has unlimited liability towards the creditors, whilst at least one of the other partners is liable only for the amount of his capital investment. A silent partnership is defined in accordance with paragraphs 230(1) and 231(2) of the Commercial Code as a personalistic entity in which the silent partner participates in the commercial enterprise conducted by the active partners. Such a way an interest is made by the silent partner in the assets of the active partner, and the silent partner participates in the profits of that undertaking. No such corresponding entity is provided for under United Kingdom law.

In the text below the German limited partnership is considered before the silent partnership, both entities, especially the former, are of considerable economic importance in that country.

THE LIMITED PARTNERSHIP

Nature and some important characteristics

The limited partnership is simply a special form of the ordinary commercial partnership. In principle, the ordinary partners (Kömplenare) are responsible for the running of the partnership, and have unlimited liability, whilst the limited partner(s) are excluded from the management and representation of the partnership. However, the special rules governing the limited partnership, which are principally contained in paragraphs 161-177a of the Commercial Code, are of a flexible nature and may depart from this model. In addition to these special rules, the limited partnership is also governed by the rules contained in paragraphs 105-60 of the Code, which are made applicable to the commercial partnership. The members of the partnership may be natural persons, or corporations having legal capacity or personalistic associations such as the GmbH (Geschäft mit beschränkter Haftung) or private limited liability company. A civil partnership may be the limited partner or Kommanditist. A limited partnership does not have a legal personality, but is instead treated as a community of joint owners. Many of the rules applicable to the limited partnership are the same as those governing the ordinary commercial partnerships; see paragraphs 105-160 of the Commercial Code, to which paragraph 161 makes reference.

The articles of a limited partnership must state the nature of the contributions and stipulate that the liability of a limited partner is limited to a specific amount of money, or that he is required to provide certain things for the partnership, which have to be given a specific value therein. A limited partnership requires entry in the Commercial Register, which is maintained by the local commercial court. It has to be given a name, followed by a suffix which indicates its legal form.

According to paragraphs 123(1) and (3) and 161(2) of the Commercial Code, the limited partnership comes into existence once it has been entered in the Commercial Register. However, if an entity has been carried on transactions before registration, and it has the characteristics of a commercial enterprise, such transactions are binding on the limited partnership and third parties in accordance with paragraph 123(2) of the Commercial Code. A different approach is taken when the relevant transactions are not of a commercial nature, when they are not so binding. By paragraph 176(1), if a limited partner agrees to the commencement of business before registration, he (or it) will incur unlimited liability in respect of the transactions concluded before such registration unless the relevant creditors are aware that he (or it) is only a limited partner. It is obviously generally in the interests of such a partner to endeavour to ensure that no pre-registration transactions take place.

The German limited partnerships have grown in importance in recent years. Various forms of the GmbH & Co KG, in which the GmbH is frequently the unlimited partner and the directors thereof may be the limited partners, have long been in use in that country. Originally the use of this type of business entity was motivated by considerations of taxation. The limited partnership is also used for the purpose of family businesses. Certain KG, the so-called Puhlmann-KG, have a considerable number of members whose membership has resulted from the

(a) It is decided that there is not to be a prosecution, either for lack of evidence or by way of public interest grounds, and civil recovery requirements are met.

(b) A prosecution fails and civil recovery requirements are met.

(c) Where defendant absconds (before or after conviction) or dies.

(d) Civil recovery may be a primary means of recovery when the corporate entity has changed beyond all recognition from its predecessor.

(e) The above criteria are not to be treated as conclusive and each case will need to be considered on its special facts and merits.

What would not happen, I believe, is to use civil recovery as a substitute for criminal confiscation where the latter is possible, especially where there are victims to compensate from the alleged offending (see also the Attorney General’s Guidelines on civil recovery).

It is worth mentioning here that:

(i) Cases should not be taken on by a prosecuting authority only for civil recovery purposes. In other words, the prosecuting authority should not become a substitute Asset Recovery Agency.

(ii) There are serious risks of costs and damages if civil recovery fails, unlike in most criminal confiscation cases. For this reason, however, there is a temptation to go down the civil recovery route, especially given the ruling in the cases of R v David Gale [2009] EWHC 1015 (QB) (currently appeal to the Supreme Court) and R v Ayberg [2009] 3 WLR 110 (HL).

(iii) In Gale, SOCA alleged that all the property was the proceeds of drug trafficking (largely taking place in Spain & Portugal in the 1980s and 90s) associated businesses, and may depart from this model. In addition to these

(iv) In R v Ayberg there has been both an expansion and contraction of the scope of confiscation orders. It gives the green light for confiscation for offences for which there has been no conviction and the use of evidence for an extremely wide purpose, but at the same time introduces a contradiction because such matters have to be proved beyond reasonable grounds – the criminal standard, and that is a threshold which few confiscation proceedings will be able to meet.

(v) It also important to ensure that civil recovery is not pursued because it is the easier option and that there are not double standards where large and rich corporations are self-reporting unlawful activity “buy their way” out of criminal proceedings. There will be cases where, prima facie, civil recovery seems appropriate, but if the offence is serious then justice demands that there is adequate punishment for the offence beyond depriving the offender of ill-gotten gains.

CIVIL RECOVERY AND MUTUAL LEGAL ASSISTANCE TO FOREIGN JURISDICTIONS

If assets within the English jurisdiction are obtained by unlawful conduct in a foreign state then these can be forfeited provided there is sufficient evidence from that foreign jurisdiction that the assets located here were obtained by unlawful conduct in that foreign state even without a conviction in the foreign state. It is strictly therefore not mutual legal assistance to a foreign state as in criminal cases of mutual legal assistance. Civil recovery will only be pursued if evidence is provided by the foreign state that the assets were obtained by unlawful conduct.

COMPENSATION TO VICTIMS

This area is not without its difficulties. Compensation is envisaged in the criminal regime. Under the civil recovery route there is no mechanism to compensate victims of crime. The only available option would be under section 281 Proceeds of Crime Act 2002 (POCA) where the “victim” would need to make a declaration acceptable to the court that he/she has an interest in recoverable property or property subject to civil recovery. It is the “victim” who has to make the declaration. In pursing civil recovery cannot do so. Section 281 of POCA may be an answer to this particular difficulty read in conjunction with sections 281 and 286 of POCA. The authority conducting civil recovery may, if satisfied, ask for a declaration of a victim’s interest in recoverable property. If it is the policy to compensate victims of fraud, particularly those who, unlike large organisations, are without the financial resources to pursue civil confiscation then civil recovery would meet this policy if it was to be a substitute for criminal confiscation.

IMPLICATIONS IN TERMS OF HUMAN RIGHTS

Civil recovery proceedings are both civil in domestic and European Convention law. In Arik v He & Chen [2005] EWCH 3021 (Admin) the point was taken that civil recovery proceedings represent an unfounded threat of property rights contrary to Article 1 of Protocol 1 of the ECHR. The submission was rejected.

However, this should not be taken to imply that there are no ECHR implications Article 1 (protection of property) and Article 8 (right to respect for private and family life) may well be engaged. Furthermore, the investigator in each case on whom the powers are conferred must fall within a description specified in an order made for these purposes by the Secretary of State under section 455 Proceeds of Crime Act 2002. The powers in question fall within Article 8.2 (e) of virtue of being necessary for the prevention of crime, and accredited financial investigators have functions in the prevention of crime.
business rescue provisions in Chapter 6 of the new Companies Act apply also to close corporations. Any reference in Chapter 6 to a company must be regarded as a reference to a close corporation. Any reference to a shareholder of a company, or the holder of securities issued by a company, must be read as a reference to a member of a close corporation.

Other arrangements incorporated by reference

The provisions of the new Companies Act are applied also to regulate the names, dissolution and deregistration of close corporations as well as the administration and enforcement of the Act.

CONCLUSION

The main impact of the new Companies Act on the South African close corporation may be summarized as two-fold.

First, the proscription of new close corporations: this not only translates into the phasing out of close corporations, however gradual, but leaves small entrepreneurs with only one avenue for new incorporations and that is under the new Companies Act.

If the new “exempt” private company is really so much more deregulated and simplified than the present close corporation it only serves to beg the question why the present choice of incorporation has perhaps to be limited and why it is necessary to overburden the close corporation with additional regulation. The philosophy is apparent: “out with the old in with the new.”

Second, there is the clearly discernible tendency to subject the close corporation to more and more onerous administrative duties and arrangements. A prime example is the introduction of annual returns, with their attendant duties and liabilities. This impact is significantly added to by the approach to supplant numerous arrangements in the Act by that of the new Companies Act, by repealing some of the provisions and by incorporating large tracts of the latter by reference.

It is unfortunate that the new Companies Act will proscribe new close corporations and ceramic existing close corporations by duties and obligations contrary to their very nature and fundamental design philosophy.

Civil process to confiscate property obtained through unlawful conduct is too good to waste. It hurts criminals in the most effective way. The importance of civil recovery should not be underestimated.

RETROSPECTIVE EFFECT

The powers given to prosecuting authorities as of April 1, 2008 can be used retrospectively. This is clear from section 316(5) of POCA. This sub-section with this interpretation is referred to in the judgment of Waller LJ in [1999] 3 All ER 501.

The redistribution of civil recovery powers is irrelevant to this issue; it simply alters the identity of the claimant not the scope of the action. However, it should be noted that the new cause of action was made retrospective subject to a limitation period of 12 years. Time runs from the date of the cause of action accrues (see ss 27952 and 53 of The Limitation Act 1980).

LESSONS TO BE LEARNED FROM BALFOUR BEATTY CASE

Background

In civil recovery, property obtained by unlawful conduct can be recovered. The provisions do not require a specific offence to be established against any individual or company. Balfour Beatty voluntarily brought to the attention of the SFO certain unlawful conduct.

The unlawful conduct related to irregular payments and inaccurate accounting which failed to comply with the requirements of section 221 of the Companies Act 1985. These irregularities were in connection with the Bibliotheca project in Alexandria, Egypt. Once the matter was reported to the SFO by Balfour Beatty, the SFO commenced an investigation and it was determined that the SFO certain unlawful conduct.

A consent order was agreed before the High Court on October 6, 2008. Balfour Beatty agreed a settlement of £2.25 million, together with a contribution to costs of the civil recovery order proceedings.

In simple cases where an agreed sum is to be received by the authority which conducted civil recovery proceedings, the Director of that authority is required to appoint a trustee to receive the agreed sum and deal with it (ie transfer it to the Home Office). In complex cases it may be necessary to appoint a receiver. A substantial part of that sum returns to the prosecuting authority under the incentive scheme. The trustee is nominated under section 266(2) of POCA and must be indemnified by the Director against any claim or action brought against the trustee.

This was the very first civil recovery under the new powers made available since April 2008 to the Serious Fraud Office and other prosecuting authorities – powers which were available only to the now abolished Asset Recovery Agency.

Civil process to confiscate property obtained through unlawful conduct is too good to waste. It hurts criminals in the most effective way. The importance of civil recovery should not be underestimated.

Main lessons

The main lessons to be learned from this case are:

(a) Encourage corporates and individuals to self-report wrongdoing so that the prosecuting authority may consider whether civil recovery is appropriate as opposed to criminal prosecution; the latter always remains an option.

(b) If civil recovery is appropriate then long and protracted criminal investigations can be avoided with obvious implications with regard to costs and resources. This case showed the importance of these new powers and how they can be used effectively. There were also some lessons to be learned with regard to overseas corruption (the SFO’s policy in regard to overseas corruption is set out in the booklet SFO Policy in dealing with overseas corruption).

(c) If there are parallel civil recovery and criminal investigations then the costs of the criminal investigation cannot be claimed from any civil recovery settlement but there is nothing to stop prosecuting authorities from negotiating costs.

(d) If there are victims to be compensated (and there were none in the Balfour Beatty case) then criminal confiscation may be the best option as a compensation order can be made through a confiscation order on conviction.

(e) If civil recovery proceedings the victim has to ask for a declaration from the High Court for compensation from unlawfully recovered property. However, there is nothing in the legislation to stop the prosecuting authority, if satisfied, to do this on the victim’s behalf and include it in any settlement or successful civil recovery proceedings.

The second case of civil recovery conducted, once again by the SFO, is that of AMEC Plc (an international engineering and project management firm). It was AMEC that brought the matter to the attention of the SFO in March 2008 following an internal investigation into receipt of unlawful payments.

There was an investigation and it was determined that the payments/credits were contrary to section 221 of the Companies Act 1985. AMEC paid nearly £5 million under an agreed consent order and also costs of the civil recovery proceedings.

The lesson to be learned from both the Balfour Beatty and AMEC cases, in particular, is that corporates are bringing irregular conduct to the attention of the appropriate authorities and improving their internal practices to stamp out unlawful conduct rather than face criminal proceedings. It is interesting to note that unless an undertaking is given that there will be no criminal fraud office and other prosecuting authorities – powers which were available only to the now abolished Asset Recovery Agency.

Legal Studies, University of London.

Professor J J Henning

Distinguished Professor of Comparative Law and Dean of the Faculty of Law, University of the Free State, South Africa, Senior Research Fellow and previous Director of the Centre for Corporate Law, Institute of Advanced Legal Studies, University of London.
The new Companies Act introduces a compulsory audit of the financial statements of certain close corporations. A close corporation may be required by the regulations made in terms of the Act to have its annual financial statements audited. The Minister may make regulations prescribing the categories of close corporations that are required to have their respective annual financial statements audited, taking into account whether it is desirable in the public interest, having regard to the economic or social significance of the company, as indicated by its annual turnover, the size of its workforce, or the nature and extent of its activities.

A qualifying close corporation’s financial statements must comply with sections 30(1) to (6) of the new Companies Act and not section 55(2) of the Close Corporations Act.

The annual financial statements may also be audited voluntarily at the option of a close corporation.

Financial reporting standards

The Department of Justice and Constitutional Development has been developing uniform insolvency legislation for quite some time which may conflict with the regime set out in the present Companies Act for dealing with and winding-up insolvent companies. In order to avoid any future conflict, the new Companies Act provides for transitional arrangements that retain the current disposition set out in Chapter 14 of the present Companies Act for the winding-up and liquidation of companies until such time as the new uniform insolvency legislation is enacted. However, if there is any conflict between the provisions of Chapter 14 of the present Companies Act and Part G of Chapter 2 of the new Companies Act, concerning the winding-up of solvent companies and deregistration of companies, the provisions of the latter prevail. The Minister may by notice in the Gazette determine a date on which this arrangement ceases to have effect. This may not be effected until the Minister is satisfied that alternative legislation has been brought into force adequately providing for the winding-up and liquidation of insolvent companies. The Minister may prescribe ancillary rules as may be necessary to provide for the efficient transition from the present provisions to the provisions of the alternative legislation.

This transitional arrangement, with the changes required by the context, also applies to the liquidation of a close corporation in respect of any matter not specifically provided for in the Act or the provisions for substitutes’ service of the application for the restraint order and the letter of direction disqualification of a director of a company specified in section 69(9) to (11) of the new Companies Act.

Despite being disqualified on one of the grounds detailed in section 69(9)(b) of the new Companies Act, a person may participate in the management of a close corporation if 100 per cent of the members’ interest in the company is held by that disqualified person or the disqualified person and other persons who are all related to that disqualified person, and each person has consented in writing to the disqualified person participating in the management of the corporation.

The provisions of the new Companies Act relating to an application to declare a director disqualification or unpaid probation apply to a member of a close corporation. A reference in section 162 of the new Companies Act to a company must be regarded as referring to a company or a corporation, while a reference to a director must be regarded as referring to a director of a company, or a member participating in the management of a close corporation.

A person who has been placed under probation by a court in terms of section 162 of the new Companies Act or section 47(1)(C) of the Act may not participate in the management of the corporation, except to the extent permitted in the probation order.

Winding-up and liquidation

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Furthermore, it might defeat the policy of self-reporting unlawful conduct and in practical terms may be self-defeating.

INTERNATIONAL MATTERS

The Proceeds of Crime Act 2002 (External Requests and Orders) Order 2005 has been made under section 444 of POCA and came into effect on January 1, 2006. Now any country can make a request to the UK jurisdiction for a restraint order or registration of a confiscation order made in the requesting state. The designated countries requirement has been abolished. As a consequence of this the SFO has been able to give assistance to countries such as the Islamic Republic of Iran in restraint proceedings (see judgment of Gross J in Al-Emar [2008] ENWIC 315 (Cmm)).

Principal definitions

An external request is a request to restrain relevant property identified in the request (s 447(1)). An external order is one which is made by an overseas court against property obtained as a result, or in connection with, of unlawful conduct, and is for the recovery of specified property or money (s 447(2)). Unlawful conduct is “criminal conduct” as defined by English law (s 447(3)).

Action required on receipt of request

When a request is received the Secretary of State will refer it to the appropriate prosecuting authority. The restraint order may be made under Article 8 of the external order if the conditions in Article 7 are satisfied, ie either an investigation has begun or criminal proceedings have commenced in the requesting state; there is reasonable cause to believe that the offender named in the request has benefited from unlawful conduct; relevant property in England & Wales has been identified and such property is required to satisfy any confiscation order that may be made in the requesting state; that there is a risk of dissipation without a restraint order.

Provided these conditions are satisfied the court cannot determine the merits of the proceedings in the overseas jurisdiction: see Government of India v Quarmbsh [2004] EWCA Civ 40. But should be noted here that only property located within the domestic jurisdiction can be restrained. A world wide restraining order cannot be made (unlike a domestic restraint order) King v Senex Fraud Fund [2008] EWCA Civ 310.

The order may make exceptions for living expenses and legal fees from restrained assets provided no other assets elsewhere are available. The order may also require disclosure of any further assets believed to be within the jurisdiction and may only be made on the application of the relevant Director of the prosecuting authority. It cannot be applied for directly by the requesting state: Article 9(1)(b).

There is a duty of full and frank disclosure. Any material fact not disclosed may result in the discharge of the order. The procedure is to prepare a witness statement in support of the application for the restraint order and the letter of request from the requesting state may be disclosed. Once the order is made, the requesting country must file the witness statement in the UK jurisdiction. If the conditions named by the witness statement are not satisfied the order may be revoked by the court.

Innocent third parties having an interest (legal or beneficial) in property restrained may also be provided from dealing with restrained property. There can be, and frequently are, provisions for substitutes’ service of the order if parties are outside the jurisdiction.

Registration of an external order

This is governed by Article 21(1). The external order may be registered if the conditions in Article 21 are satisfied (see Article for details). It should, however, be highlighted that one specific requirement is that the external order complies with the Human Rights Act 1998. So, for example, if a confiscation order is made in a foreign jurisdiction and a request to register it to confiscate property located in the English jurisdiction is received it cannot be registered if it can be shown that the confiscation order did not comply with ECHR requirements.

This is in contrast to the making of restraint orders as the latter orders only preserve property for the satisfaction of a confiscation order. A restraint order does not transfer property rights or deprive the owner of it. A confiscation order deprives the defendant of the property, see Al-Emar v Government of the United States of America [2004] UKHL 17 for the application of Article 6 of ECHR to the registration of external confiscation orders.

To satisfy the external order a receiver may be appointed, and time to pay may be allowed – see Article 26(2) of the 2005 order.

The assistance that can be provided amounts to:

(a) protecting property from dissipation by obtaining a restraint order;
(b) managing property by appointing a management receiver;
(c) enforcing an external confiscation order.

UK requests to foreign jurisdictions

These are made pursuant to section 74 of POCA if the conditions in section 40 have been satisfied. The UK can make requests to apply for restraint orders obtained in the domestic court for registration overseas if property is located in the overseas jurisdiction and for registration of a domestic confiscation order. The request is forwarded to the Secretary of State via the Home Office by a letter of request setting out details of the request and any court order made. It will be governed by the legal requirements of the overseas jurisdiction.
close corporation's debts in terms of the Close Corporations Act which arose before its registration as a company remains the liability of that person as if the conversion had not occurred.

For the conversion of a close corporation into a company section 29C(4)(b) of the present Companies Act requires a statement by the close corporation's accounting officer, based on the performance of his duties under the Act, that he is not aware of any contravention of the Act by the close corporation or its members or of any circumstances which may render the members of the close corporation together with the close corporation jointly and severally liable for the corporation's debts. Interestingly enough, Schedule 2 of the new Companies Act does not contain a similar requirement.

Loans and the provision of security by or to a close corporation

Section 55(1) of the Act provides for the mutatis mutandis application of the provisions of section 17 of the present Companies Act to the employment of funds of a subsidiary company in a loan to its holding corporation or fellow subsidiary company, or the provision of security by a subsidiary company to another person in connection with an obligation of its holding corporation or fellow subsidiary. Where a subsidiary company makes such an "upward" or "sideward" loan, or provides an "upward" or "sideward" security, the subsidiary company must furnish detailed particulars of the loan or security in its annual financial statements for every year during which the loan or security is in operation. The directors and officers of the subsidiary company and the members and officers of the holding corporation who authorise or permit or are party to the transaction, are personally liable to the subsidiary for damages, should the terms of the loan or security be unfair to the subsidiary or not provide reasonable protection for its assets.

Subject to certain exceptions, section 226(1) of the present Companies Act, as applied by section 55(1) of the Close Corporations Act, prohibits loans or the provision of security by a subsidiary company to:

(a) a member or officer of its holding corporation; or
(b) a director or officer of its fellow subsidiary company; or
(c) a close corporation, company or other body corporate controlled by one or more of the members or officers of its holding corporation; or
(d) a close corporation, company or other body corporate controlled by one or more of the directors or managers of its fellow subsidiary company.

A loan or provision of security contrary to the prohibition is fatal to the validity of the transaction.

Unless the express prior consent in writing of all members to the particular transaction is obtained, loans and the provision of security by a close corporation to another corporation in which one or more of its members hold more than a 10 per cent interest, or to a company or other juristic persons controlled by one or more members of the corporation, is prohibited by section 52 of the Close Corporations Act. This provision is in effect a simplified version of the prohibition in section 226 of the present Companies Act.

The new Companies Act provides for the repeal of section 55 of the Act in toto. The definitions of “holding company” and “subsidiary” in the Act are amended to reflect the corresponding definitions in the new Companies Act.

Section 45 of the new Companies Act regulates loans or other financial assistance by a company to directors or prescribed officers of the company or of a related or inter-related company, or to a related or inter-related company or corporation, or to a member of a related or inter-related corporation, or to a person related to any such company, corporation, director, prescribed officer or member.

In contrast, section 52 of the Close Corporations Act (dealing with loans and the provision of security by a close corporation) will not be repealed by, or even amended to refer to, section 45 of the new Companies Act. Section 52 will therefore not only continue to reflect the arrangement contained in the then repealed section 226 of the present Companies Act, but will continue to refer pertinently to (the then repealed) section 226(1A)(b) for the definition of control.

This does not augur well for the attainment a “seamless match” between the various statutory arrangements regulating the provision of loans and security by and to companies and close corporations.

Accounting and disclosure

Annual financial statements

Within six months after the end of every financial year, annual financial statements in one of the eleven official languages will have to be prepared by the close corporation’s members. Presently the period is nine months.

Compulsory audit of financial statements

Presently a close corporation must appoint an accounting officer who has to report on the annual financial statements. A formal audit of annual financial statements is, however, presently not required. Although chartered accountants qualify for an appointment as accounting officers, quite a number of other sufficiently qualified professions have also been permitted. It should be emphasised that it is quite possible to have audited annual financial statements for instance where the members need it for their own purposes or because a potential creditor requires it. Hence audits are carried out where they serve a meaningful purpose.

CONCLUSION

Civil recovery is an important tool in the armory of prosecutors to deprive those who have obtained property through unlawful conduct. Its importance must not be under-estimated. Mutual legal assistance is also very important as without it assets can be transferred overseas, and the person who obtained these ill-gotten gains cannot be deprived of those assets.

The whole purpose of civil recovery and criminal confiscation is to deprive offenders of their ill-gotten gains; its purpose is not to enrich the state. Asset recovery is important because it deters offenders from committing financial crime, disrupts the criminal economy and does not allow offenders to enjoy the benefit of their crimes.

Philip F J Malloch
BARRISTER, SENIOR RESTORER AND CONFISCATION LAMPI, SERIOUS FRAUD OFFICE