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LOANS TO COMPANY DIRECTORS AND CONNECTED PERSONS

It is a well-known fact that a company has its own legal personality distinct from its members/shareholders. A company's legal personality has no physical existence, and that is why all operations of the company are run through the company directors. In simple language, directors are referred to as custodians of the company. They are thus mandated with the key duty of managing all affairs of the company. Some refer to directors as the company's human agency.

Company directors are vested with many duties imposed by both the law and practice. Pursuant to section 182 of the **Companies Act, Cap. 212 (hereinafter referred to as "the Act")**, directors have a duty to act in good faith and in the best interests of the company. In this way, directors while executing their duties to the company, are strictly prohibited to exercise the same in their own personal interests or engage their personal activities under the umbrella of the company.
Section 200(1) of the Act prohibits a company to make a loan to a director, enter into any guarantee or provide any security in connection with a loan made by a director, director of its holding company or a connected person(s). However, prohibition on loans to directors and connected persons shall not apply in circumstances where:

- Company's ordinary business is lending of money or giving guarantees in connection with loans made by other persons;
- Loan intends to meet expenditure incurred or to be incurred for purposes of the company or for the aim of enabling the director to perform duties as an officer of the company as well as to anything done by a subsidiary; and
- Director seeking loan is a holding company.

For purpose of clarity, connected persons have been defined under section 200(3) of the Act to include the following:

- Director's spouse, child or step-child;
- A body corporate in which the director has a direct or indirect interest of twenty per cent (20%) or more in the share capital;
- A trustee to any trust of which beneficiaries include director's spouse, child or step-child, or a body corporate in which the director has a direct or indirect interest of twenty per cent (20%) or more in share capital; or
- A partner to the director.

However, in case of funds to meet expenditure incurred or to be incurred for purposes of the company, a loan, guarantee, or any security shall be made upon prior approval of the company at a general meeting. During such general meeting, the purposes of expenditure, amount of a loan, together with the extent of guarantee or security must be disclosed.
Where approval of the company is not given at or before the next following annual general meeting, the loan shall be repaid or the liability under the guarantee or security shall be discharged, within six (6) months from the conclusion of that meeting pursuant to section 200(2) of the Act.
Generally, it is illegal for a company to make loan to a director, act as guarantor for director's personal loan or connected persons. This prohibition provided by the law, ensures accountability and fair dealings in operations between the company and its human agency (directors), since there is also liability in acting to the contrary. Pursuant to section 200(3) of the Act, directors are liable to indemnify the company against any loss arising out of director's authorization in making of loan, or entering into of a guarantee to a loan, or provision of security where company approval is not given as required by the law.

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