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Directors Liabilities

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Who is a director?

- Anyone occupying the position of a director by whatever name called
 - De iure (the list at Companies House)
 - 288 not conclusive: SEM Connections
 - De facto (assumes functions of a director)
 - Shadow (on whose directions directors are accustomed to act)
- Title doesn't matter
 - Director PSU Sales: No: SMC Electronics
- No difference between executive and non executive directors



But shurely not shareholders?

- Mr Justice Parker highlighted that very problem in *Secretary of State for Trade and Industry v Jones* in 1999 when he said

“if a substantial shareholder wishes, as well he may, to take an active part in running the affairs of the company in order to protect his investment, that raises the very question of whether in doing so he may not be constituting himself a de facto director of the company”



The danger for Banks

In *Re a Company (No 005009 of 1987), ex p Copp*. Knox J refused to strike out a claim against Natwest, holding that the claim that the bank acted as a shadow director was not obviously unsustainable.

□ *BUT Triodos Bank NV v Dobbs*

- 'a creditor acting to protect its own interests is unlikely to have become either a shadow director or a de facto director'.
- The financial package negotiated by the bank was not forced on the company, which was free to accept or reject the terms.
- Directors not accustomed to act on the bank's terms
- Watching brief v Directing play



Tort

- Directors may have
 - no fiduciary
 - nor contractual duties
 - nor any duty of care
- to those they contract with through a company

- : The Swan



But.... Quasi Tort



The Cheques in the Post And Now it is!

- Director could not escape liability in deceit by saying he was speaking on behalf of the company
- Would he be separately liable in tort?
- Standard Chartered Bank v Pakistan National Shipping Corp (2002) HL



Personal Services

- They may be personal liable where the company provides their *personal services* which can only be provided through their skill and care and they perform this negligently: Fairline Shipping v Adamson [1975] QB 180



Koninklijke Philips Electronics v Princo Digital [2004]

- A close involvement in the day to day running of the company and independent authority in respect of actions amounting to the patent infringement could render a director a joint tortfeasor
- Pumfrey J
 - director had knowledge of the relevant facts
 - director had a role of a business manager “beyond merely sitting in board meetings”
- the fact he was an officer was only relevant “in that it provided opportunity”



The Companies Act 2006

- largest act of parliament ever
- 1300 sections
- 16 schedules



Directors Duties

- It will also provide a statutory code for director's duties.
- They have duties
 - To act within their powers: section 171
 - To exercise independent judgement: section 173
 - To exercise reasonable care, skill and diligence : section 174
 - To avoid direct and indirect conflicts of interest: section 175
 - Not to accept benefits from third parties conferred by reason if his being a director or because of something he did or failed to do as a director: section 176
 - To declare an interest in proposed transaction or arrangement of the company to the other directors: section 177



Duty to promote success of the company

- Directors also now have a duty to promote the success of the company but at the same time will also have to have regard to:-
 - The long term consequences of the decision
 - The interests of company's employees
 - The need to foster relationships with suppliers and customers and others
 - The impact on the community and the environment
 - The desirability of the company maintaining a reputation for high standards of business conduct
 - The need to act fairly between members of the company
- (Section 172)



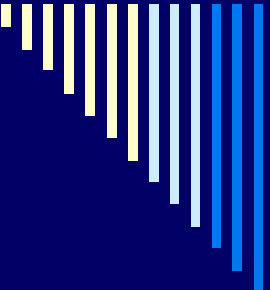
And if you don't...

- Breaches are actionable as breaches of fiduciary duty: section 178.



Who can bring an action?

- Derivative claim
 - Shareholders through the company
 - For the benefit of the company
- Not, say, to the employees directly.
- “have regard to” not = bound to give equal weight to the interests of members.



When can a director be disqualified?

- Automatically if bankrupt
- By the criminal courts
 - for offences relating starting running and ending companies
- By the civil court's
 - For persistently breaching the CA 2006
 - Company and conduct unfit
 - Company in breach of competition law



When is one unfit?

□ Grounds include

- Commercial impropriety or incompetence
- Trading at the risk of creditors
- Phoenix trading
- Failure to maintain adequate accounting records
- Failure to file returns
- Breach of fiduciary duty
- Transferring assets at an undervalue
- Breach of Competition Law: EA



Other matters justifying disqualification

- Director's disregard for consumer law: *OR v Mitchell* [2006]
- Non payment of Crown debts
 - Not more serious than other debts: *Sevenoak Stationers*
 - Issue = Policy of discrimination in favour of trade creditors: *Re Verby Print*
 - Short period may be a policy but less likely to be unfit: *OR v Dhaliwall*
 - Promises kept / broken
 - HMCR shouts loudest



The Advice defence

- *McNulty's Interchange*

- 3 reasons

- Someone else's fault = director substituted the professional's perceived superior and expert views for his own.
- Evidence of a responsible reaction of a director who recognises and wishes to remedy the limitations in his own skills.
- Reasonable in the light of how matters were independently perceived to be at the time.



Limits

- ❑ Not if advice obviously wrong: *Park House*
- ❑ Clear failure to observe proper commercial standards: *Re Keypark*
- ❑ Abdication of responsibility: *Re Bradcrown*



How long for?

- Starts 21 days after the order
- *Sevenoaks Stationers*: 3 bands
 - 2-5 years
 - 5-10 years
 - 11-15 years
- Old case law not relevant: *DTI V Zwirn*



Permission to act

If asked, the court can give permission to a defendant to remain as a director of a company provided he can assure the court that there are adequate safeguards are in place.



Directors Disqualification

- *Carecraft procedure*
- *The Insolvency Act 2000* - disqualification undertakings
- Introduction on 2nd April 2001
 - 24% increase in director disqualifications since
 - 57% have been by way of undertakings given.



The effect of disqualification

- On disqualification, s 1, CDDA 1986:-
 - (a) **he shall not be a director of a company, act as receiver of a company's property or in any way, whether directly or indirectly, be concerned or take part in the promotion, formation or management of a company unless (in each case) he has the leave of the court, and**
 - (b) he shall not act as an insolvency practitioner



Management: grey area

- You don't have to be a director or an employee to manage: R v Campbell



The price of not getting permission

- Sentencing benchmark: *R v Attenbury* – immediate custodial sentence even where no dishonesty



Confiscation Orders

- Court can order D to hand over proceeds of crime
- Defence pleads:-
 - I didn't make any money out of this office
 - I and my family are very poor
 - I am no richer than I was before I started in a life of crime
 - Confiscation will cause me and my family great hardship



An example

- Directors Disqualification
- What is the benefit?
- The treasury argument: Benefit =
Turnover for duration of directorship
- R v Blatch (2009) No
 - NO - benefit not necessarily the turnover of the relevant company or companies but the real benefit the offender had obtained personally.



Section 15 CDDA

- Whilst disqualified, is involved in the management of the company, or
- Is involved in the management of the company and acts or is willing to act on instructions given by a person whom he knows at that time is disqualified
- Jointly and severally liable with the company and anyone else caught by section 15
- All debts and other liabilities of the company as are incurred whilst involved in the management of the company
- Presumption willing if acted on any instructions given by a disqualified person.



Piercing the veil

- Where the company has been set up as a “sham or cloak” to evade liability
 - Gifford Motor Co v Horne (company set up to circumvent employee’s covenant not to compete or solicit)
 - Jones v Lipman (sold property to company to avoid order for specific performance)



The Elephant Test

□ Common factors:-

- Created the company / bought the company
- Controlled allocation of shares
- Controlled allocation of directorships
- Used the company to avoid legal obligations he would have otherwise borne personally



Insolvency Act 1986

- Powers to reopen past transactions
- Section 423 – Transactions defrauding creditors



You don't have to show

- ☐ The company is insolvent
- ☐ That there was fraud



You do have to show

- You are a victim
- The transaction was for
 - no consideration or
 - a gift or
 - in consideration of a marriage
 - Or to form a partnership
 - Or for consideration significantly less than the value provided
- Intended to put assets outside the reach of creditors or prejudice their present / future claim



section 212 IA 1986

- **The summary Procedure**
- Is available to creditors as well as liquidators
- Only recovers assets to the collective pot.



Targets

- ☐ is or has been an officer of the company,
- ☐ has acted as liquidator, administrator or administrative receiver of the company, or
- ☐ is or has been concerned, or has taken part, in the promotion, formation or management of the company,



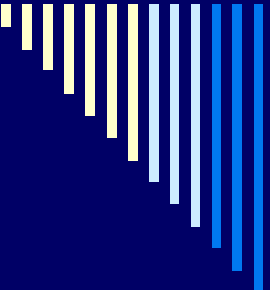
Grounds

- has misapplied or retained, or become accountable for, any money or other property of the company
- been guilty of any misfeasance
- breach of any fiduciary or other duty in relation to the company.



S 212

- No new right of action but is a cheap and cheerful recovery procedure: Re Simmon Box Diamonds Ltd [2002] BCLC BCC 82.
- Cannot be used for contractual debt enforcement: Re Etic [1928] Ch 861
- Supplements common law remedies: A & J Fabrications v Grant Thornton [1999] BCC 807



Section 216, Insolvency Act 1986

- ❑ Old company has gone into insolvent liquidation
- ❑ he had been a director or shadow director in the period of 12 months leading up to the liquidation.
- ❑ The re-use of the company name is prohibited in relation to such a person if-
- ❑ It was a name the liquidated company in the 12 month period
- ❑ Prohibited name =
 - A similar name
 - A name suggesting association with that company



Prohibition

- Unless he has leave of the court, a person to whom section 216 applies cannot in the time period of 5 years starting on the day of liquidation
 - Be a director of a company known by the prohibited name
 - Be in any way linked with the promotion, formation or management of any such company
 - Be in any way concerned with the carrying on of a business carried on under a prohibited name.



Acme Equipment instead of Acme Components?

- *Rickets v Ad Valorem Factors* [2004]
- the test = whether the two companies in the context of the circumstances that their names would be used are sufficiently similar to suggest *some kind of association* in view of
 - The types of products they produce
 - Their location
 - Their types of customer
 - The persons involved



He will be liable for Newco's debts incurred during any period

- ❑ involved in the management of Newco despite being prohibited
- ❑ willing to act on the instructions of someone who is prohibited to be involved in the management of Newco
- ❑ Section 217 IA 1986



The end.....





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