Briefing Sheet

Directors' Legal Considerations

The Company Directors Disqualification Act (CDDA) contains significant powers to ban 'unfit' directors from holding office. Taking excessive remuneration whilst insolvent, trading whilst knowingly insolvent and continuing to take credit when there is 'no reasonable prospect' of creditors being paid are included in the list of actions that can lead to disqualification.

The Insolvency Act 2000 included provisions to speed up the process, and increase the volume of directors' disqualifications. In a 'fast track' approach directors can admit culpability in return for disqualification for shorter periods of time. If disqualified, a director may not act as a director in the disqualification period: to do so is a criminal offence that may lead to imprisonment for up to two years, or a fine, or both.

The CDDA only applies where the company has gone into liquidation or administration and putting in place a Company Voluntary Arrangement could have a mitigating effect, provided the Directors take all reasonable steps to safeguard creditors' interests. Below are some of the many points to consider for Directors aiming to stay on the right side of the law in relation to insolvent trading:

- Be sure to build a detailed picture of the company's financial position, including sales prospects and an assessment of the company's assets and liabilities. Do not rely on guesswork or believe that the financial details are not important.
- Hold regular management and board meetings, minute the decisions taken and file the minutes carefully; take notes where important decisions are made outside meetings. Do not ignore essential legal paperwork.
- Be honest with all concerned (including employees, customers, creditors and the bank). Do not hide the truth from those close to the business or the bank.
- Formulate an action plan and get all relevant parties to buy into it. Do not keep changing plans.
- Only make promises to creditors that you can keep. Do not prioritise creditor issues incorrectly.
- Be prepared to take advice from professional advisors and to consider even the most unpalatable options. Do not bury your head in the sand, be unrealistic and ignore closure as a possible solution.

Executive summary

Director disqualification is a serious business with courts able to disqualify for between two and fifteen years for unfit conduct. A Director facing disqualification proceedings should take advice immediately from an expert and look at how mitigating factors might assist a defence. Even a director or manager acting on the instructions of a person who is disqualified may be made personally liable for the company's debts.

Director's disqualifications are still relatively rare but a public web site now aims to put rogue directors in the public domain and stop them continuing to act illegally. Avoiding disqualification is a matter of being beyond reproach in the conduct of the company's business, especially when financial difficulties are faced.

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