Mercian Law

Commercial Debt Recovery Specialists

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# MAXIMISING A RECOVERY OUT OF CORPORATE INSOLVENCY

Personal liability of directors is pursued by either:

- Proceedings for breach of fiduciary duty
- Personal liability due to fraudulent or wrongful trading

## Disqualification

The court is required to disqualify a director if:

- They are or were a director of a company which has become insolvent, and
- Their conduct as a director of that company makes them unfit to be concerned in the management of a company

The minimum period of disqualification is 2 years and the maximum is 15 years. Directors may give undertakings not to be directors, rather than face formal court proceedings.
Disqualification means the director may not take part in the management of a company without leave of court. Breach leads to criminal liability and civil liability for the company debts.
A manager could also become personally liable for the debts if they take instructions from a person who they know to be disqualified.
Ten days notice must be given before commencing disqualification proceedings. Applications can only be made by the Secretary of State or sometimes the Official Receiver.

Badges of unfitness:

- Trading while insolvent
- Excessive remuneration
- Trading with revenue money
- Failure to keep records and accounts

Arguments to avoid disqualification or reduce the period:

- Misjudgment rather than lack of commercial probity
- Reliance on professional advice
- Putting own money in

- Regular production of, and reliance on, budgets and management accounts
- Involvement of chartered accountant as co-director

The office holder of an insolvent company must within 6 months send to the Secretary of State a return relating to any person who was a director within the last 3 years. The office holder can also send an “unfitness report” to the Secretary of State.
Proceedings must be supported by either a written report of the Official Receiver or affidavit. Service is deemed 7 days after posting. The summons will include an acknowledgement of service, requiring the respondent to indicate whether or not:

- They deny directorship
- Denies alleged conduct
- Denies conduct makes them unfit to manage a company
- They intend to produce mitigating evidence

The acknowledgement must be filed at Court within 14 days, and the affidavit evidence within 28 days from date of issue.
The first hearing will take place within 8 weeks of issue.
A Disqualification Order takes effect 21 days after being made.

**Directors Liability for Wrongful Trading**

Incompetent directors can be ordered on the application of the liquidator to pay a contribution towards the company debts if:

- The company goes into insolvent liquidation and
- When a director knew or ought to have concluded that there was no reasonable prospect that the company would avoid going into insolvent liquidation.

Director defence, they must show that as from that moment they took every step with a view to minimising the potential loss to the company creditors as they ought to have taken.

**Prohibited Names**

Where a company goes into insolvent liquidation any person who was a director in the previous 12 months cannot, without leave of the Court, take part in the management of another company with a similar or same trading name for the next 5 years.
If they breach this rule there is a criminal liability and personal liability for the debts of the new company.

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