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Disqualification Newsletter

Newsletter Editor
Dr. John Tribe

Dear Subscriber,

Welcome to the latest newsletter. The Newsletter contains an important news item: the issue of the new draft Insolvency Rules 2016. It also contains various summaries of cases on disqualification.

Some of the shorter case summaries have been taken from the Government website.

Dr John Tribe

Newsletter Editor

FEEDBACK

We would be pleased to hear from subscribers who have any comments or suggestions regarding the content of this Newsletter, or any comments or queries on disqualification law, practice and procedure in general. Letters which raise issues of interest may be published in the Newsletter. Please address letters to the editor of this newsletter: Dr John Tribe, Kingston Law School, Kingston University, Kingston Hill, Kingston upon Thames, Surrey, England, KT2 7LB; Email: j.tribe@kingston.ac.uk.

NEWS

Draft Insolvency Rules 2016

On 20 July 2015, the Insolvency Service met with members of the Insolvency Rules Committee ('IRC') to discuss the draft Insolvency Rules 2016, which have been updated as part of a modernisation project and to take forward policy changes under various pieces of primary legislation.

The IRC will be liaising with the IRC, whose role is to review the changes to rules before reporting to the Lord Chancellor (who is responsible for making these rules). Subject to this work, it is anticipated that the Rules will be made in Spring 2016, with a commencement date of 1 October 2016.

The draft Insolvency Rules 2016 may accessed on the Government website at www.gov.uk/government/uploads/system/uploads/attachment_data/file/447426/Insolvency_Rules_2016_PDF_for_IRC.PDF. There is also an extremely helpful explanatory note of the policy changes which underlie the proposed new Rules. That note can also be accessed on that website at www.gov.uk/government/uploads/system/uploads/attachment_data/file/448152/Explanatory_note_to_Insolvency_Rules_2016.pdf.

CASE LAW

(1) Re F G Hawkes (Western) Ltd, sub nom Secretary of State for Business, Innovation and Skills v Hawkes

[2015] EWHC 1585 (Ch), [2015] All ER (D) 73 (Jun), His Honour Judge Keyser QC, sitting as a Judge of the High Court, Chancery Division, Cardiff District Registry

Directors' disqualification – section 6 unfitness – false representations regarding company's finances – submission of false VAT returns – whether allegations proved – whether defendants unfit to be involved in the management of a company.

FACTS:

F G Hawkes (Western) Ltd ('the company') was incorporated on 2 March 1987. Its principal business was the importing of plywood and sheet materials. It entered into administration in October 2011. Throughout the relevant period, its directors were the defendants, GH and JH. The Secretary of State for Business, Innovation and Skills sought disqualification orders against the defendants pursuant to s 6 of the Company Directors Disqualification Act 1986 ('CDDA 1986').

The Secretary of State alleged that: (a) the defendants had produced materially misleading accounts for the period between May 2008 and 2009 and for the year ending in July 2010 ('the 2010 accounts') and had made misleading statements in the 2009 accounts, and the 2010 accounts, both of which had been signed by GH on behalf of the board of directors of the company, and a letter of representations in respect of the 2010 accounts, which had been signed by both of the defendants. The 2010 accounts showed that there was a sum of around £4.5m in respect of money loaned by the company to Amadora, a company owned by it; (b) that the defendants had been responsible for the submission of false VAT returns between April 2010 and April 2011, involving under-declarations of VAT of around £1.5m. The issue was whether the under-declarations had been made by the defendants to enable the company to continue to trade, or by E, the company's financial manager; and (c) the defendants had caused or allowed the company to commit substantial breaches of contract relating to an invoice discounting service provided by Barclays Sales Finance ('BSF'), resulting in losses to BSF of over £900,000.

HELD:

(1) On the evidence, the 2009 accounts, the 2010 accounts and the letter of representations had been materially misleading. Although GH alone had signed the 2009 and the 2010 accounts, he had done so on behalf of the board of directors. Both GH and JH had been equally responsible. Regarding the misleading accounts in respect of money loaned to Amadora, the absence of any mention of the events of late 2010 in the 2010 accounts rendered those accounts misleading. The omission had been deliberate and for the purpose of avoiding the inclusion of information that would have placed a question mark against the financial status of the company. The directors' conduct in respect of the treatment of Amadora in the company's accounts made them unfit to be concerned in the management of a company;

(2) GH's evidence was wholly incredible, and would be rejected. The defendants' conduct in respect of the false VAT returns made them unfit to be concerned in the management of a company;

(3) On the evidence, it was not unlikely that BSF had been aware that contra-trading had been taking place, and had merely been surprised at the level of contra-charges. The Secretary of State had not made out the ground of claim in that regard;

(4) It followed that disqualification orders would be made against both defendants. The period in each case would be ten years.

Mr Richard Cole (instructed by Howes Percival LLP) for the Secretary of State.

Mr David Harris (instructed by Blackfords LLP) for the defendants.

(2) Re Fima Consulting Ltd, Official Receiver v Malik

Mr Registrar Briggs, High Court of Justice, Companies Court, 10 June 2015

Directors' disqualification – section 6 unfitness – MTIC fraud – period of disqualification order.

FACTS:

The Official Receiver sought a disqualification order under s 6 of the CDDA 1986 against the defendant. He alleged that the defendant had, from at least from 1 March 2006 to 30 June 2006, caused or allowed the company to participate in transactions which were connected with the fraudulent evasion of VAT.

The Official Receiver alleged that the company had participated in a form of VAT fraud known as Missing Trader Intra Community (MTIC) fraud – or 'carousel fraud' – and that the defendant was a director of the company at the time it engaged in those activities. The fraud involves large consignments of electrical or other small item size high value goods being invoiced rapidly and repeatedly around trading chains, speeded up by movement on paper, with actual movement of goods only taking place as they enter or exit the

UK. Indicators of such fraud included the rapid succession of same day trades without deliveries within the UK of goods sitting at a shared freight forwarder; the common use of the same (usually offshore) bank; and entering into payment arrangements involving third parties who were neither suppliers nor customers. In the present case, all the relevant traders banked with the First Curacao International Bank which was shut down by the Netherlands Antilles authorities in September 2006 in order to prevent money laundering.

HELD:

(1) The court accepted the substance of the written evidence of the Official Receiver that the defendant had been involved in MTIC fraud. The company had acted as a wholesaler of mobile phones and CPUs and the trade involved MTIC fraud in which the company had been a 'buffer' company in a chain of 156 and a 'broker' in a deal chain of 23 in the period of 1 March 2006 to 30 June 2006. The court found that the defendant had, as a director of the company: (a) caused the company to make third-party payments despite being advised that it was trading in a 'high risk' sector; (b) completed deals before clearances had been received from the Redhill Verification Unit of HMRC about the genuineness of VAT registration numbers for some of the companies; and (c) failed to undertake proper enquiries concerning the authenticity of the various transactions, for example by failing to undertake appropriate site visits or carry out inspection reports. The company was fully aware of the matters by reference to which the MTIC fraud was involved as a result of communication it received from HMRC and the 'PN 726 form', which highlighted in the clearest terms the risks taken by traders in this industry and the reasonable steps that should be taken to ensure that transactions were not fraudulent;

(2) The defendant was a director in control of the day to day running of the company at the time of insolvency. He was, therefore, responsible for the trade and consequent insolvency of the company for the losses which had been incurred by the company;

(3) The company was involved in MTIC fraud involving hundreds of millions of pounds. The company had participated in contrived transactions with a view to gaining VAT refunds of substantial sums of money;

(4) The defendant knew or ought to have known about the company's participation in the MTIC fraud as this was the only reasonable explanation for the circumstances of purchases, sales and the method of the transactions;

(5) The conduct of the defendant warranted the making of a disqualification order of 13 years.

Mr Paul Warner, deputy Official Receiver, appeared on behalf of the Official Receiver.

The defendant did not appear and was not represented.

(3) Re Inspire Real Estate Ltd, Secretary of State for Business, Innovation and Skills v Ogden

His Honour Judge Roger Kaye QC, the County Court at Leeds, 24 April 2015

Directors' disqualification – section 6 unfitness – acting in breach of disqualification undertaking and/or while an undischarged bankrupt – whether defendant was a de facto director – whether defendant unfit to be concerned in the management of a company – period of disqualification order.

FACTS:

The Secretary of State ('SoS') brought disqualification proceedings under s 6 of the CDDA 1986 against the defendant in respect of his conduct as a director of Inspire Real Estate Limited ('Inspire').

The core allegation against the defendant was that he had acted or, as amplified in the charge, continued to act 'as a director of Inspire' without the permission of the court while he remained disqualified by virtue of a four-year disqualification undertaking given to the SoS with effect from 26 August 2010 or, during the period of 12 January 2011 to 11 January 2012 while he was an undischarged bankrupt.

Inspire was incorporated on 11 February 2004 as a private company limited by shares for the purpose of buying and selling real estate. The company commenced trading in that month as property dealers.

On 18 February 2004, the defendant was appointed sole director of Inspire. He resigned on 15 April 2008 being replaced by a Mr Vincent Garcia ('Mr Garcia') from 17 April 2008 to 31 October 2008, was reappointed on 31 October 2008 and resigned again on 25 August 2010. With the sole exception of Mr Garcia (above) and Mr Robinson (if validly appointed – see below), the defendant was Inspire's sole director throughout its trading existence. It was a small company having no formal corporate governance structure as such. The defendant conducted its affairs on an informal basis. No minuted decisions were kept.

The defendant was previously a director of Inspire (Nelson St) Limited, a general construction and engineering company ('Nelson Street') and of Inspire Real Estate Construction Limited, a building contractor ('Construction'). These two companies went into compulsory liquidation on 9 September 2008 and 14 October 2008 respectively.

On 26 August 2010, the defendant gave a disqualification undertaking to the SoS in respect of his conduct of Nelson Street and Construction based on an allegation of abrogation of his duties as a director of those companies. The disqualification undertaking expired on 26 August 2014. The thrust of the allegations against the defendant was that, during the relevant period in respect of each company, he had abrogated his duties as a recorded director of each company by failing to maintain, preserve or deliver up adequate accounting records to the Official Receiver and had allowed his co-director to cause each company to fail as regards its obligations with regard to the payment of taxes.

A Mr Edward Robinson ('Mr Robinson', referred to above) was, according to the Companies Register, appointed director of Inspire with effect from 23 August 2010 and remained sole registered director when Inspire went into administration on 15 May 2012. According to the defendant, Mr Robinson was Inspire's sole contractor of the company's sole on-going enterprise (and as such an unsecured creditor), namely the redevelopment of property at 145–151 Town Street, Stanningley into shops and apartments. At that time, Inspire held a small property investment portfolio (mostly charged to secured lenders) including the one development property at Stanningley requiring completion. After his resignation, the defendant, while a resident of Monaco, remained an employee of Inspire and, according to him, continued day-to-day administration.

Until 10 April 2008, the defendant was the sole shareholder of Inspire. On that date, the defendant transferred the shares to his wife, Mrs Belinda Katie Kew ('Mrs Kew'), who thereby became and was (and remained) the sole shareholder of Inspire and, between November 2006 and September 2008, the company secretary. She was also the sole shareholder of and a creditor of Inspire, namely Schnu Property Limited ('Schnu'). According to the defendant, Mrs Kew was also the major unsecured creditor of Inspire.

The defendant was also adjudged bankrupt on 12 January 2011 upon his own petition. He was automatically discharged from this bankruptcy after one year on 12 January 2012.

It was not disputed that the defendant was a director of Inspire between February 2004 and April 2008, and between October 2008 and August 2010. Nor was it disputed that Inspire subsequently became insolvent as evidenced by its being placed in administration. It was thus not disputed that the first two requirements of CDDA 1986, s 6 were fulfilled. It was also not disputed the defendant did not seek or obtain permission to act as a director of Inspire having given the disqualification undertaking. What was disputed was whether the defendant ever acted as a director in the relevant period, still less (and even if he did) whether his conduct 'as a director' of Inspire after he purportedly appointed Mr Robinson as director made him unfit to be concerned in the management of a company.

The relevant period for the purposes of the allegations against the defendant was, therefore, 26 August 2010–26 August 2014. The overlap period between the disqualification undertaking and the bankruptcy was 26 August 2010 (when the disqualification undertaking was given) and 26 August 2014 (when it expired). Inspire went into administration on 15 May 2012. The bankruptcy (from 12 January 2011 to 12 January 2012) was within this period and hence, it was common ground, added nothing of substance to the core allegation of acting as a director while disqualified.

HELD:

(1) The court found that after the defendant's purported resignation, the defendant: (a) had failed to ensure Mr Robinson was validly appointed by securing a clear unequivocal signed consent from him; (b) had

determined the policy or strategy to be followed in respect of the conduct of Inspire and the division of responsibility and tasks between him and Mr Robinson; (c) attempted to distance himself from banks and creditors by telling them that Mr Robinson had been appointed, but he remained in control and on the mandate; (d) maintained accounts in which the company's moneys were mixed with Schnu's without Mr Robinson's consent; (e) decided when and how much to repay Mrs Kew; (f) decided and informed the banks that no further repayments could be made, thus effectively determining that Inspire went into administration; (g) renewed the property insurance policies without Mr Robinson's knowledge or approval; (h) issued instructions to Mr Robinson as to what jobs needed attending to. These may have been minor, but the cumulative picture presented was something else. They were and are consistent with him being in reality the person in charge; and (i) retained the password to enable him to file annual returns and the like and had accepted this was something a director should be responsible for and for which he did not have Mr Robinson's approval;

(2) The cumulative effect of these and other matters and the reality was that the defendant, while attempting to abrogate himself of responsibility, in fact continued much as before throughout the crucial period. He was more than a mere administrator. He was in a superior role to Mr Robinson. He assumed the responsibilities of and acted as the director (ie as *de facto* director) of Inspire throughout the period in question even if he called them acts as an administrator. As the judge observed: 'An administrator is not a consultant. An administrator administers. In a small company this is exactly what a director does. There simply was no corporate governance at all, save as conducted by him.'

(3) The allegation of the SoS that the defendant had acted as a *de facto* director of Inspire during the relevant period as made out: *Holland v Revenue and Customs* [2010] UKSC 51, [2011] 1 All ER 430, [2010] 1 WLR 2793 and *Smithton Ltd (formerly) Hobart Capital Markets Ltd v Guy Naggar* [2014] EWCA Civ 939, [2015] 2 BCLC 22, [2015] 1 WLR 189 applied;

(4) Given the fact that the defendant had given the disqualification undertaking and attempted to do something about the fact that it would mean that he could not act as a director of Inspire, he well knew the risks he was running and chose to run them. The overall circumstances of the conduct of the defendant made it serious enough to fall below the standards expected of a director and a disqualification order would be made against him;

(5) The court agreed with the SoS that the starting point should be a disqualification order for a period of nine years. However, the court made a disqualification order for a period of seven years commenting that: '… it has to be remembered that [the defendant] was aware of his

responsibilities, of the impending effect of the disqualification undertaking and did take steps to try and do something about that. These are both aggravating features (the former) and also extenuating circumstances (albeit limited, the latter). His choice of Mr Robinson, with due respect, was a poor choice. [The defendant] was anxious to keep Inspire going for the reasons previously stated, not least because of the mixture of Schnu's funds and Inspire's and the indebtedness to his wife. He also abandoned the company effectively by dealing with matters mainly in Monaco where he resided and sought to do most of the work by email or telephone. I accept [the defendant] thought that he had found someone to be in charge and that Mr Robinson equivocated. That however did not relieve him of the responsibility to ensure that Mr Robinson's appointment was validly and properly achieved. Yet he accepted he did not even consider the company's articles of association when deciding Mr Robinson should be appointed or on the £100 monthly payment [he agreed to pay Mr Robinson].'

Mr David Mohyuddin (instructed by Wragge Lawrence Graham & Co LLP) appeared for the Secretary of State.

Ms Lesley Anderson QC and Miss Eleanor Temple (instructed by Clarion Solicitors) appeared for the defendant.

(4) Re Emach International Ltd, Secretary of State for Business, Innovation and Skills v Tricklebank

His Honour Judge Mithani QC, the County Court at Walsall, 10 August 2015

Directors' disqualification – section 6 unfitness – false representations – trading while insolvent – taking deposits with no reasonable prospect of supplying goods – period of disqualification order.

FACTS:

The Secretary of State ('SoS') brought disqualification proceedings under s 6 of the CDDA 1986 against the defendant in respect of his conduct as a director of Emach International Ltd ('the company').

The company was incorporated on 29 September 2009 and commenced trading in the middle of 2010. It was concerned in the design and manufacture of automated machine tools. The defendant was the only director and shareholder of the company. It went into liquidation on 19 March 2013. The Statement of Affairs showed a deficiency to creditors of £442,055.

The grounds upon which the SoS sought a disqualification order against the defendant were as follows:

(a) the defendant allowed the Company to use funds totalling £8,000 received from a customer, the company having represented to the customer that the item had been purchased when in fact it had not been purchased;

(b) the defendant allowed the company to take a pre-delivery payment in the sum of £4,400 upon the representation that the goods were complete when they were not;

(c) the defendant allowed the company to take monies totalling £40,345 when he knew or ought to have known that there was little or no reasonable prospect of the company being in a position to supply the goods; and

(d) the defendant caused the company to fail to comply with its statutory obligations with regard to VAT for a period in excess of 12 months up to the cessation of trade, with an estimated loss to HMRC in the sum of over £41,279.

The defendant wrote to the court stating that he did not intend to contest the proceedings and conceded that a disqualification order against him was 'inevitable'.

HELD:

(1) In the absence of receiving any written evidence, or hearing oral evidence, from the defendant, the allegations made by the SoS were established;

(2) The court accepted the SoS' submission that the defendant had failed to ensure that the company complied with its statutory obligations in respect of VAT and PAYE, while at the same time taking receipt of customer's money in circumstances where false representations had been made that the goods had been ordered/completed and/or paid for and at a time when the defendant knew or ought to have known that the company was not in a position to meet its obligations;

(3) The court agreed with the SoS that a disqualification order for a period of eight years should be made against the defendant. The court indicated that its starting point was that a disqualification order against the defendant for a period of nine to nine and a half years was appropriate. However, it took into account the fact that the defendant had indicated that he did not intend to contest the proceedings and in fact had sent a letter to the SoS' solicitors accepting that a disqualification order against him should be made. In the circumstances, the court gave him a discount for effectively having admitted his wrongdoing and reduced the period from its proposed starting point to a period of eight years.

Miss Lydia Pemberton (instructed by Shepherd and Wedderburn) appeared for the Secretary of State

The defendant did not appear and was not represented

(5) Re Ultra Green Group Ltd, Secretary of State for Business, Innovation and Skills v Anthony Clive Blakey

District Judge Gamba, the County Court at Brighton, 23 July 2015

FACTS AND OUTCOME:

The Secretary of State sought a disqualification order under s 6 of the CDDA 1986 against the defendant. He alleged that the defendant had: (a) caused the company to trade at unreasonable risk and to the detriment of its creditors; and (b) caused the company to enter into transactions to the detriment of its creditors.

The Secretary of State alleged that on 28 April 2010, by which time the company was insolvent and unable to pay its debts as they fell due, the defendant transferred the company's contracts and all its green energy technologies to a connected overseas company for £1. Despite this, he then caused the company to carry on trading and to incur new debts of over £629,000 in a failed proposal to clean up oil from the May 2010 Gulf of Mexico oil spill. With no income and no means to generate funds in the short term, creditors were left unpaid and the company ceased trading in December 2010.

The court found that the company was used in a reckless manner to incur liabilities in pursuit of speculative projects, the effect of which was to place creditors at high risk and exacerbated the losses ultimately incurred. A disqualification order against the defendant was clearly warranted, and the court made it for a period of seven years.

Mr Tiran Nersessian (instructed by Howes Percival LLP) for the Secretary of State.

The defendant appeared in person

(6) Her Majesty's Secretary of State for Business, Innovation and Skills v Patrick Joseph Bradley

Sheriff Principal Marysia W Lewis, Perth Sheriff Court, 29 July 2015

Directors' disqualification – s 6 unfitness – appeal challenging findings of fact – whether findings made by lower court erroneous.

FACTS AND OUTCOME:

The respondent had been a director of a company ('A'), the assets of which, including book debts owed to it, had been transferred to a newly incorporated company ('B') of which the respondent was also a director. B collected the book debts and used them to pay the creditors of A, with the exception of HMRC. The Secretary of State's case in short was that the respondent had caused A to treat HMRC unfairly as compared to A's other creditors. On appeal, the respondent sought to argue that the Sheriff's finding that the assets of A had been transferred to B made the remainder of her findings (generally to the effect that the respondent, as a director of A, had caused

HMRC to be treated unfairly by B paying all of A's creditors other than HMRC) erroneous. That is to say, the respondent argued that, since A's assets had been found to have been transferred to B, when the creditors of A were paid, that was a gratuitous step taken by B, for which neither it nor the respondent could be criticised.

The Sheriff Principal refused the appeal. She accepted the argument advanced for the Secretary of State that it would be unfair to allow such a radical departure from the position advanced at proof to be acceded to on appeal: *Jones v MBNA International Bank* [2000] EWCA Civ 514 applied.

The proof had been conducted on the footing that there was no dispute between the parties that the respondent had put in place a composite transaction which involved the transfer of assets on the basis that B would collect A's book debts in order to pay A's creditors other than HMRC. Further and in any event, the Sheriff Principal accepted the Secretary of State's subsidiary argument that, on a fair reading of the Sheriff's judgment, it was quite clear that she had understood and applied the correct legal test and that she had not made the elementary errors which the respondent, by his appeal, sought to attribute to her: *Henderson v Foxworth Investments Ltd* 2014 SC (UKSC) 203, [2014] UKSC 41, 2014 SCLR 692, [2014] All ER (D) 19 (Jul); and *Novus Aviation Ltd v Onur Air Tasimacilik A/S* [2009] EWCA Civ 122, [2009] 1 Lloyd's Rep 576, [2009] All ER (D) 275 (Feb) considered and applied.

The Sheriff Principal agreed that the respondent's argument depended upon a 'narrow textual analysis' of the Sheriff's judgment. That was both inappropriate and incorrect: *Piglowska v Piglowski* [1999] 3 All ER 632, [1999] 1 WLR 1360; and *McGraddie v McGraddie* 2014 SC (UKSC) 12, [2014] UKSC 58 considered and applied.

Mr D Thomson (instructed by Burness Paull LLP, Solicitors) appeared on behalf of the Secretary of State.

Mr Anderson (instructed by TLT Solicitors) appeared for the respondent.

CASE LAW