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Disqualification Newsletter

Newsletter Editor
Dr John Tribe

Dear Subscriber,

Following the news section, this Newsletter contains an interesting analysis on permission to act under s 17 of the Company Directors Disqualification Act 1986 (CDDA 1986). Following the decision in *Re Liberty Holdings Unlimited, Re Copperidge Developments Ltd, sub nom Owen v Secretary of State for Business Innovation and Skills* [2015] Lexis Citation 244, [2015] All ER (D) 119 (Oct), Omar Ensaff examines the court's approach to an application for permission to act under s 17 where a disqualification order is made under s 2 of the CDDA 1986.

Four case reports on directors' disqualification then follow. The Scottish opinions are given in full.

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. Letters which raise issues of interest may be published in the Newsletter. Please address letters to the editor of the 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

Coming into force of the new regime for directors disqualification

The amendments to the CDDA 1986 by Pt 9 of the Small Business, Enterprise and Employment Act 2015 to strengthen the regime for disqualifying came into force on 1 October 2015: see Small Business, Enterprise and Employment Act 2015 (Commencement No 2 and Transitional Provisions)

Regulations 2015, SI 2015/1689, (C100), reg 2. The principal changes brought about by the new provisions have been considered in past issues of the Newsletter and have also been summarised in recent issues of the main work. However, they will be incorporated fully, and considered in detail, in the forthcoming issues of the main work.

ANALYSIS

Exploring permission to act under Company Directors Disqualification Act 1986, s 2

Following the decision in Re Liberty Holdings Unlimited, *Re Copperidge Developments Ltd, sub nom Owen v Secretary of State for Business Innovation and Skills* [2015] Lexis Citation 244, [2015] All ER (D) 119 (Oct), Omar Ensaff, a barrister at No 5 Chambers, explains how the court approached an application for permission under s 17 of the CDDA 1986 where a disqualification order under s 2 of the CDDA 1986 was made. In essence, the court decided to approach such an application in the same way as any other application for permission under s 17.

Chief Registrar Baister allowed the applicant's application for permission under CDDA 1986, s 17, to be involved in the management of two companies, notwithstanding that he had at that time been subject to a disqualification order for a period of seven years for falsifying accounts. The court held that, in the exceptional circumstances of the case, permission would be granted.

What was the background to this case?

The applicant was subject to a seven-year disqualification order arising out of CDDA 1986, s 2 following his guilty plea to three counts of falsifying accounts. As well as the disqualification order that had been made against him, he had also been sentenced to three years' imprisonment and he had, in addition, been subject to a confiscation order in the sum of £3m. The background that gave rise to that disqualification, imprisonment and confiscation order was that while he was a director of a company, he had allowed or caused that company to supply eggs that were purportedly free range or organic, but in fact were eggs that came from caged hens.

What was the application that the Chief Registrar was asked to rule upon?

The applicant sought the court's permission, pursuant to CDDA 1986, s 17, to be involved in the management of two companies (one of which was an unlimited company) as a project manager of each. The first company was, for want of a better term, a property development company, while the second was a construction company.

What were the specific issues that arose in this case?

There was one main issue and a subsidiary issue.

The main issue was how the court dealt with an application for permission to act where the disqualification order against the applicant was made under s 2 of the CDDA 1986 (disqualification on conviction of an indictable offence), and whether the court's approach in those circumstances was different from the approach it adopts in considering permission where there has been a disqualification under, for example, s 6 of the CDDA 1986 (disqualification for unfitness). The Secretary of State appeared to contend that, as a matter of principle, permission should not be granted where a disqualification order was made under s 2. Relating to this was the interplay between the purpose of the criminal proceedings and the purpose of the permission to act regime.

The subsidiary issue was the issue of 'need' (and whether it is a threshold requirement in an application for permission); and the role of 'need' in such an application, particularly in the context of the rehabilitation of people who had been convicted of offences.

What did the Chief Registrar decide on each issue, and why did he reach his conclusions?

On the main issue, it was decided that an application for permission that arises from a CDDA 1986, s 2 disqualification should be treated like any other application for permission. The court would not adopt the Secretary of State's blanket policy. In short, had Parliament intended such a blanket policy then Parliament could have legislated for an exclusion from CDDA 1986, s 17 applications where there had been a CDDA 1986, s 2 disqualification, but it had not. Moreover, the court had to be careful to distinguish between the purpose of the criminal proceedings (which are essentially penal) and the purpose of the disqualification regime (which is primarily concerned with public protection) though the court was to have regard to the deterrent function of disqualification. Even though the same approach is to be adopted when seeking permission in relation to a CDDA 1986, s 2 disqualification, such applications are highly fact-specific and so the seriousness of the offence giving rise to the disqualification is plainly a factor that the court takes into account.

On the subsidiary issue – confirmation that 'need' was not a threshold requirement. In addition, as part of the 'need' requirement, the need to rehabilitate people who had been convicted of offences was relevant.

What should practitioners take away from this judgment regarding applications brought following the making of a disqualification order under CDDA 1986, s 2 or any form of allegation of dishonesty leading to disqualification?

The evidence in support of any application for permission to act is critical and needs to address the relevant issues. Even if the disqualification arose from a conviction or from dishonesty, that does not mean that the application is doomed to fail. However, the evidence in support of the application is the key to success.

ANALYSIS

What should practitioners take away from this judgment with regard to how the 'need' of the applicant is being dealt with in applications in practice?

Although need is not a threshold requirement, the practical reality is that it still has to be addressed in the evidence in detail.

CASES

(1) Re Liberty Holdings Unlimited, Re Copperidge Developments Ltd, sub nom Owen v Secretary of State for Business Innovation and Skills [2015] Lexis Citation 244

High Court of Justice, Chancery Division, Companies Court, Chief Registrar Baister.

Company – Director – Disqualification – O running egg farming business – O allowing sale of eggs from caged hens as free range or organic eggs – O being investigated and pleading guilty to three counts of falsifying accounts – O serving term of imprisonment and being disqualified as director – O applying for permission to work as director of two companies – Whether application should be allowed – Company Directors Disqualification Act 1986, s 17(2)(a).

FACTS:

O had carried on business as a wholesaler of free range and organic eggs through a private unlimited company (HEE). The traceability of free range and organic eggs was an important aspect of the trade in such products. O was responsible for securing the necessary traceability. He turned a blind eye to the fact that some of the eggs sold to HEE came from caged hens. He caused the company to switch labels, falsely indicating to consumers that the eggs were organic or free range. In 2006 and 2008, HEE was investigated by the Department for Environment, Food and Rural Affairs. Eleven criminal charges were brought against O. O did a deal under which he pleaded guilty to three counts of falsifying accounts. He was sentenced to three years' imprisonment, a confiscation order was made for £3m, and a disqualification order was made for seven years. He was released from prison on curfew after serving 11 months of the sentence. He paid £2m under the confiscation order. He applied unsuccessfully for remission of the balance and was ordered to serve a further 32 months in prison. Prior to his disqualification, O had been a director of two companies, LHU and Copperidge (together, 'the companies'). The directors of LHU were AO, O's brother, and CO, O's wife. Copperidge was a construction company that worked solely for LHU. Its sole director was DO, O's son. O intended to work for LHU as a project manager, and to have a similar role at Copperidge. He would earn a modest salary working for LHU, but would work for Copperidge for free. He applied for permission to be concerned in the management of Copperidge and LHU under s 17(2)(a) of the CDDA 1986.

O submitted that, first, it was highly unlikely that the defects that had given rise to the disqualification would reoccur if permission was granted. Second, there was no defect of which there was a risk of repetition, and, in any event, the companies appeared to be on a sound financial footing, the Revenue and Customs Commissioners liabilities were up to date and in the respect of LHM, it was an unlimited company, so the members had unlimited liability to any creditors. Third, there was plainly a need for O to be involved in the management of the companies. Fourth, the companies were trading successfully, which was a factor that weighed in O's favour. Finally, the mere fact that the disqualification had arisen as a result of s 2 of the Act was not, in itself, enough to refuse the application. The Secretary of State submitted that it opposed the application on policy grounds rather than the intrinsic merits of the application. O's fraud had been very sizeable, and the companies had been running successfully without his input.

HELD:

The application would be allowed.

Any court faced with an application for permission had to be careful to distinguish between the purposes and effects of the criminal law and civil law in relation to the making of a disqualification order. The court also had to have regard to the deterrent function of disqualification. Plainly, an applicant who sought permission following conviction of an indictable offence faced an extremely steep uphill struggle in persuading the court to exercise its discretion to permit him to act in the management of a company (see [28], [31], [33] of the judgment).

While the offences that had resulted in D's conviction had been very serious, in the exceptional circumstances of the case, permission would be granted: (i) having regard to the need or desirability of rehabilitation; (ii) having regard to the factors in O's submissions; (iii) bearing in mind the unlimited liability status of one of the companies in respect of which permission was sought; and (iv) having regard to the safeguards proposed by O. Further, giving limited permission to act and subject to conditions in exceptional circumstances was unlikely to detract from the deterrent function of disqualification (see [30], [31] of the judgment).

Re Cargo Agency Ltd [1992] BCLC 686 considered; *Re Gibson Davies Ltd* [1995] BCC 11 considered.

Mr Omar Ensaff (instructed by Simon Burn Solicitors) for O.

Ms Genevieve Parke (instructed by Howes Percival LLP) for the Secretary of State.

(2) Secretary of State for Business, Innovation and Skills v Pawson [2015] EWHC 2626 (Ch)

High Court of Justice, Chancery Division, Manchester District Registry, His Honour Judge Hodge QC, sitting as a judge of the High Court.

Company – Director – Disqualification – Claimant applying to disqualify defendant director in respect of conduct of affairs of nine companies wound up – Operating scheme which conferred no commercial benefit – Excessive remuneration and fees charged by Defendant – Whether application should be granted – Whether defendant should be disqualified – Company Directors Disqualification Act 1986, s 8.

FACTS:

The defendant, P, was a qualified chartered accountant and non-practising barrister, aged 58. He had acted as a director of nine companies, which he had formed and controlled. Each of the companies had been formed as a vehicle for the promotion of recovery schemes, arising out of a number of unlawful collective investment schemes. Winding-up petitions were presented against all nine companies, which led to the making of winding-up orders being made against them. At the time the winding-up orders were made, none of the companies was insolvent. The claimant Secretary of State for Business, Innovation and Skills brought a claim, under s 8 of the CDDA 1986, for the disqualification of P as a director concerning his conduct of the affairs of the nine companies. The conduct complained of included P charging repeat legal opinion fees from the nine companies and charging each of the companies the same amount on the basis of a letter from accountants. P had received a minimum of £158,000, by way of remuneration and legal opinion fees over a three-year period, equating to some £52,000 a year, or £4,000 a month. The sums represented just under 69% of the total shareholders' funds in the companies.

The Secretary of State submitted that P had caused the companies to operate schemes in a manner which, due to his actions/inaction, had provided no commercial benefit to the shareholder members of the schemes and which had become unsustainable in view of the level of remuneration and benefits taken by him as against the available shareholder funds and the likelihood of obtaining further funding and the actual steps taken to progress the schemes. P's conduct had involved both a want of probity and a lack of integrity and demonstrated more than simply mere incompetence. The case involved a professional person whose conduct demonstrated a number of breaches of duty to the company and, independently of that, demonstrated his unfitness to act as a company director.

HELD:

The claim would be allowed.

Disqualification was not mandatory under s 8 of the Act. The court had a discretion to disqualify even if it was satisfied that a defendant's conduct made him unfit to be concerned in the management of a company. The question of unfitness was one of fact. The court had to be satisfied that the director in question had fallen below the standards of probity and competence appropriate for persons fit to be involved in the management of a company. That involved a two-stage process: first inquiring whether the director had acted in a culpable manner; if he had, whether his conduct

justified a finding of unfitness. In seeking to answer those questions, by s 9 of the Act, the court was required to have regard to the statutory guidelines for determining unfitness, set out in Sch 1 to the Act (see [51], [57] of the judgment).

The Secretary of State had made out his case. It was a serious case, within the middle bracket. The present case was not simply a case of incompetence to a high degree. It went beyond that and indicated a lack of probity and integrity on the part of P. It had not been honest of P to be charging repeat legal opinion fees. Nor had it been honest, at least in the commercial context, for him to be charging each of the companies the same amount on the basis of a letter from accountants. The court was satisfied that unfitness had been made out. It was appropriate to exercise the court's discretion under s 8 to disqualify P. Dishonesty has been made out (see [192]–[194] of the judgment).

P would be disqualified for eight years (see [195] of the judgment).

Re Atlantic Computers plc [1998] BCC 200 considered; *Re Barings plc, Secretary of State for Trade and Industry v Baker (No 5)* [1999] 1 BCLC 433 considered; *Re Amaron Ltd, Secretary of State for Trade and Industry v Lubrani (No 2)* [2001] 1 BCLC 562 considered; *Re HLC Environmental Projects Ltd (in liq), Hellard v Carvalho* [2013] EWHC 2876 (Ch), [2013] All ER (D) 240 (Sep) considered.

Mr Giles Maynard-Connor (instructed by Bond Dickinson, Newcastle-upon-Tyne) for the Secretary of State.

Mr Jeremy Barnett (instructed under the Direct Public Access Scheme) for P.

(3) HER MAJESTY'S SECRETARY OF STATE FOR BUSINESS, INNOVATION AND SKILLS v OLUSEGUN OLAYINKA ADEDAPO sub nom as SEGUN ADEDAPO [2015] CSOH 152

Court of Session, Outer House, Lord Doherty.

The following is the full opinion of Lord Doherty in this case:

> '[1] Her Majesty's Secretary of State for Business, Innovation and Skills (the petitioner) seeks a disqualification order in terms of section 6 of the Company Directors Disqualification Act 1986 (as amended) in respect of Olusegun Olayinka Adedapo also known as Segun Adedapo (the respondent). The present application comes before me unopposed, as the respondent has not lodged answers. I am satisfied that the petition has been duly served and that the application is properly before me.
>
> [2] The respondent was the sole director of Bendith Engineering Limited ("the company") from 1 August 2006 until the company went into liquidation. He held eight of the ten issued shares in the company.

[3] The principal activity of the company was the provision of consultancy services to the oil industry. The company has been registered for VAT since 1 October 2008. The respondent was the company's sole employee. The company was the vehicle through which the respondent provided his services to customers.

[4] The company ceased trading in or around September 2012. It is insolvent for the purposes of section 6 of the Act. The Advocate General for Scotland on behalf of the Commissioners for her Majesty's Revenue and Customs ("HMRC") petitioned the Court of Session for the company to be wound up on the ground that it was unable to pay its debts. On 10 September 2013 an interim liquidator was appointed. The liquidator was subsequently nominated and appointed by resolution at the first meeting of creditors held on 22 October 2013. The liquidator received claims from HMRC of £76,664.20 for VAT, surcharges and interest; and £3,175.60 for deductions for National Insurance Contributions ("NIC") and Pay As You Earn income tax ("PAYE") and interest charges thereon. The sums due to HMRC at the date the company ceased to trade were £59,560.20 in respect of VAT and £2,623.60 in respect of NIC and PAYE. For the purposes of the present application the petitioner proceeded on the basis that the relevant debt to HMRC was the total sum outstanding at the date of cessation of trade, namely £62,183.80.

[5] The company had a statutory duty to account to HMRC on a monthly basis for PAYE and NIC due in respect of employee earnings paid by the company. It also had duties to submit VAT returns to HMRC and to remit the appropriate sums in respect of its VAT liability.

[6] The company did not lodge any Corporation Tax returns and no assessments to Corporation Tax were imposed upon it. In the absence of returns having being made the petitioner accepts that it is not possible to say whether any Corporation Tax was due by the company.

[7] In respect of PAYE and NIC the company submitted P35 forms for the tax years 2009/2010, 2010/2011, and 2011/2012 showing a total of £7,356.72 to be due for payment by the company to HMRC. It made payments towards that sum of £5,776. With the addition of interest, penalties and surcharges a total of £3,175.60 remained outstanding by the company at the date it entered liquidation.

[8] In respect of VAT the only payment which the company made to HMRC between 19 February 2010 and the date of the liquidation was a payment of £2,167.94 on 22 May 2012.

[9] The debts to HMRC began to accrue, at the latest, by April 2009. During the period that the debts were accruing the company generated more than enough funds to meet them but the respondent chose not to. Between 19 February 2010 and 26 September

2012 a total of £317,833.37 was paid into the company's bank accounts. In the same period £139,761.94 was paid from the accounts directly to the respondent and £172,857.70 was paid indirectly to him. During that period the only payments made to HMRC were the said £2,167.94 in respect of VAT and £3,176.17 in respect of PAYE/NIC.

[10] The company was effectively a one-man company which the respondent controlled. He must have been well aware of the company's obligations to HMRC. In the period from November 2009 HMRC issued several reminders to the company by letter, setting out the company's obligations and seeking payment of the sums due by it from time to time. Despite this knowledge the respondent chose not to ensure that the company paid the sums which were due. The sums owing were not retained within the company in order to allow it to continue trading. The respondent paid almost all of the sums generated by the company to himself, directly or indirectly. That was a course which could not be justified having regard to the company's outstanding liabilities. In proceeding as he did he must have been fully aware that he was acting to the prejudice of HMRC by removing large sums of money from the company which on any responsible view ought to have been used to meet its significant liabilities.

[11] The respondent also caused the company to submit false accounts to Companies House. On 20 July 2009 and 15 July 2011 he signed dormant accounts for the years ending 30 June 2009 and 30 June 2010 and declared that the company was entitled to exemption under section 480 of the Companies Act 2006 in respect of those years. Those accounts and declarations were false because the company was trading and was not dormant during those periods. Mr Thomson indicated that HMRC had not acted in reliance upon the false accounts.

[12] In the whole circumstances I have no hesitation in concluding the respondent's conduct as a director of the company makes him unfit to be concerned in the management of a company; and that it is expedient in the public interest that a disqualification order should be made.

[13] The remaining issue is the appropriate period of disqualification. I agree with Mr Thomson that the present case is similar to *Secretary of State for Business, Innovation and Skills v Stewart Russell* [2015] CSOH 128 in some respects. There is, of course, the additional element of the false accounts, but in circumstances where HMRC were not in fact misled by the accounts I am inclined to attach much more weight to the respondent's knowing failure to comply with the company's obligations to account for tax to HMRC. The debt to HMRC was significantly higher in Russell than it was here.

[14] Having considered Mr Thomson's submissions together with the petition, the productions and the authorities to which he referred me (In *Re Sevenoaks Stationers (Retail) Ltd* [1991] Ch. 164; *Mithani, Directors' Disqualification*, (2nd ed.), Vol. 1, paragraphs. [695] – [710], [715A] – [715B], and [1537], and the cases discussed therein; and *Stewart Russell* (supra) I have concluded that the respondent's misconduct falls at the very top of the bottom bracket discussed by Dillon LJ in *Sevenoaks* (at p. 174E-G). In my opinion disqualification for five years is appropriate. Accordingly, I shall grant the prayer of the petition, order that the respondent be disqualified for a period of five years, and find him liable to the petitioner in the expenses of the application.'

D M Thomson (instructed by Shepherd & Wedderburn LLP) appeared on behalf of the Secretary of State.

The respondent did not appear and was not represented.

(4) HER MAJESTY'S SECRETARY OF STATE FOR BUSINESS, INNOVATION AND SKILLS v STEWART RUSSELL [2015] CSOH 128

Court of Session, Outer House, Lord Doherty.

The following is the full opinion of Lord Doherty in this case:

'[1] Her Majesty's Secretary of State for Business, Innovation and Skills (the petitioner) seeks a disqualification order in terms of section 6 of the Company Directors Disqualification Act 1986 in respect of Stewart Russell (the respondent). The present application comes before me unopposed, as the respondent has not lodged answers. I am satisfied that the petition has been duly served and that the application is properly before me.

[2] The respondent was the sole director of Rusler Engineering Limited ("the company") from 7 March 2006 until the company went into liquidation. He was also the sole member of the company.

[3] The company is insolvent for the purposes of s. 6 of the Act. The Advocate General for Scotland on behalf of the Commissioners for her Majesty's Revenue and Customs ("HMRC") petitioned the Court of Session for the company to be wound up on the ground that it was unable to pay its debts. On 7 August 2013 an interim liquidator was appointed. The liquidator was subsequently nominated and appointed by resolution at the first meeting of creditors held on 16 September 2013. The liquidator received claims from creditors amounting to a total of £144,965.98 of which £128,794.52 was a claim by HMRC. The remaining claim (£16,171.46) was by HSBC Bank, the company's bankers. The liquidator has managed to make realisations totalling only £16,897.44.

[4] The principal activity of the company was the provision of consultancy services to the oil industry. The company has been registered for VAT since 2006.

[5] The company had a statutory duty to account to HMRC on a monthly basis for Pay As You Earn income tax ("PAYE") and National Insurance Contributions ("NIC") due in respect of employee earnings paid by the company. It also had duties to account to HMRC for Corporation Tax ("CT") and Value Added Tax ("VAT").

[6] In the period between 5 April 2011 until the date of the liquidation the company was obliged to make payments to HMRC in respect of PAYE, NIC, CT and VAT (and associated penalties) totalling £177,602.16. Payments of only £50,470.85 were made. The balance due and outstanding to HMRC at the date of the liquidation was £127,131.31.

[7] During the period that substantial liabilities to HMRC had accrued and were accruing the company generated more than enough funds to meet those liabilities but chose not to meet them. Between 6 January 2012 and the date of liquidation a total of £351,635.02 was paid into the company's bank account. In the same period £419,070 was withdrawn from the bank account. Of that sum £307,159 was paid directly to the respondent (dividends of £278,534 and wages of £28,625) but only £26,727.58 was paid to HMRC.

[8] The company was a one-man company. It was under the complete control of the respondent. He cannot but have been well aware of the company's obligations to HMRC. In the period from 7 March 2012 HMRC issued several reminders to the company by letter and by telephone seeking payment of the sums due to it. Despite this knowledge the respondent chose not to pay the sums which were due. This was not a case where the sums owing were retained within the company in order to allow it to continue trading. The respondent decided to take very large dividends which could not be justified having regard to the company's outstanding liabilities. In proceeding as he did he must have been fully aware that he was acting to the prejudice of the company's creditors, including HMRC, by removing large sums of money from the company which on any responsible view ought to have been used to meet its very significant liabilities.

[9] In the whole circumstances I have no hesitation in concluding the respondent's conduct as a director of the company makes him unfit to be concerned in the management of a company; and that it is expedient in the public interest that a disqualification order should be made.

[10] The remaining issue is the appropriate period of disqualification. Having considered Mr Thomson's submissions together with the petition, the productions and the authorities to which he referred me (In *Re Sevenoaks Stationers (Retail) Ltd* [1991] Ch. 164; *Mithani, Directors' Disqualification*, (2nd ed.), Vol. 1, paras. [695] – [710], [715A] – [715B], and [1537], and the cases discussed therein). I have concluded that the respondent's misconduct falls at the bottom end of the middle bracket discussed by Dillon LJ in *Sevenoaks* (at p. 174E-G). In my opinion a disqualification of less than 6 years would fail to mark adequately the seriousness of the case. Accordingly, I shall grant the prayer of the petition, order that the respondent be disqualified for a period of 6 years, and find him liable to the petitioner in the expenses of the application.'

D M Thomson (instructed by Shepherd & Wedderburn LLP) appeared on behalf of the Secretary of State.

The respondent did not appear and was not represented.