



## COVID-19: RELIEF FOR COMPANY DIRECTORS AND COMPANIES

The UK Business Secretary has announced that the Government will implement certain changes to enable UK companies undergoing a rescue or restructuring process to continue trading, giving them breathing space that could help them avoid insolvency.

# “Note that action taken too early can sometimes be as bad for creditors as waiting until it is too late!”

The changes include temporarily suspending *wrongful trading* provisions retrospectively from 1 March 2020 for three months for company directors so they can keep their businesses going without the threat of personal liability.

Existing laws for *fraudulent trading* and the threat of *director disqualification* will continue to act as an effective deterrent against director misconduct.

Here is a reminder of the key provisions relating to *wrongful trading*, *fraudulent trading* and *director disqualifications* in the UK.

## What is wrongful trading?

The UK Insolvency Act 1986 provides that if, in the course of an insolvent winding up / administration of a company, it appears that a person who is (or was) a director of the company knew or ought to have concluded before the commencement of the liquidation / administration that there was no reasonable prospect that the company would avoid going into insolvent liquidation / administration, the liquidator or administrator of the company can seek a court declaration that the director make a contribution to the company's assets.

## Note:

- Only company directors can be liable for wrongful trading. This includes a de facto director or a shadow director.
- Liability only arises if, on a net basis, it can be shown that the company is worse off as a result of the continuation of trading.
- The court will not make an order for wrongful trading if, knowing there was no reasonable prospect that the company would avoid going into insolvent liquidation or insolvent administration, the director took every step with a view to minimising the potential loss to the company's creditors as he ought to have taken.
- It may be difficult in practice to pinpoint the exact point at which the financial position of a company is such that insolvent liquidation or insolvent administration is more or less inevitable and the point at which the directors should have realised that this is the case for the purposes of the Insolvency Act.

Directors who are concerned about the financial position of a company should seek specialist advice on their legal duties and the financial position of the company at an early stage.

Note that action taken too early can sometimes be as bad for creditors as waiting until it is too late!

## What is fraudulent trading?

The Insolvency Act 1986 provides that if, in the course of the winding up or administration of a company, it appears that any business of the company has been carried on with the intent to defraud creditors, or for any other fraudulent purpose, the liquidator or administrator can seek a court declaration that anyone who was knowingly party to the fraudulent business make a contribution to the company's assets.

## Note:

- All persons who were knowingly parties to the fraudulent trading are caught by these provisions i.e. it is not only directors who may be liable for fraudulent trading.
- The court may order the relevant persons to make such contribution as it thinks proper, although it cannot be a punitive amount.

## What is a company director disqualification?

A director may be disqualified from holding the office of company director pursuant to a court order made upon the initiation of the



Secretary of State if their conduct as a director “*makes him unfit to be concerned in the management of a company*”.

The Insolvency Service of the Department for Business, Energy and Industrial Strategy (BEIS) has produced a helpful guide on this entitled: “*Company Directors Disqualification Act 1986 and Failed Companies: A Guide to Director Disqualification.*”

**Note:**

- Also applies to shadow directors.
- Disqualification can be for anything between two years and 15 years.
- When deciding whether a person is unfit to be a director the court must have regard to various issues including (1) any breach of any fiduciary duty or statutory obligation relating to directors, and (2) the frequency of any conduct resulting in any such breaches.
- It is a criminal offence for a person to act as a company director in contravention of a disqualification order and any such person will be personally liable for all the relevant debts of the company they are managing.

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