Applying for permission to be a company director whilst subject to Debt Relief Order restrictions

This month's Spotlight will consider the process for applying for 'leave of the court' to act as the director of a limited company whilst subject to Debt Relief Order (DRO) restrictions. The Lexis Nexis legal commentary text *Mithani: Directors' Disqualification* issue 84 April 2020 (*Mithani*) was a key reference source for this article.

Once a debt relief order (DRO) has been approved, it is an offence for a person to act as: director of a company or directly or indirectly to take part in or be concerned in the promotion, formation or management of a company, without the leave of the court. Pursuant to s11(1) (2)(c) (d) of the Company Director Disqualification Act 1986 (as amended) (CDDA 1986), this prohibition applies during the DRO moratorium, and the duration of any Debt Relief Restrictions Undertaking or Order (DRRU/DRRO).

The definition in s11(1) is widely drawn. The Court of Appeal made the following comments regarding s188(1) of the Companies Act 1948 upon which s11 CDDA 1986 is based in *R v Campbell (Archibald James)* - [1984] BCLC 83 at 88:

"…the wording is so widely cast that it is the opinion of this court that it is intended to insulate persons, against whom an order of disqualification has been made, from taking part in the management of company affairs generally. It is cast in the widest of terms "...

Advice to clients should therefore be cautious. For clients who may become subject to the restriction the starting point should be that any activity that may amount to taking part in the management of company affairs generally (not just acting as an officially appointed director) is prohibited and should be avoided, whilst subject to a relevant restriction. The debtor may then choose to apply for the court's permission to act as a director.

When can the application for permission be made?

Pursuant to Rule 9.25(1) of the Insolvency Rules (England and Wales) 2016 (IR 2016), an application for permission can only be made by a person to whom a DRO moratorium applies or in relation to whom a DRRU/DRRO is already in effect.

Mithani expresses the view that the s11 (1) prohibition on *acting* as a director would include a scenario where the director was appointed but was entirely inactive and passive:

"..on the well-established basis that being a director carries with it certain inescapable personal responsibilities which cannot be discharged by remaining completely inactive or passive."

Thus, upon DRO approval or the making of a DRRU/DRRO, a debtor would appear to be automatically committing an offence if they are still appointed as a director. This is punishable on indictment with two years' imprisonment or a fine; and summarily to a term of six months' imprisonment or the maximum magistrates' court fine (s13 CDDA 1986). This will be the case even if the director is entirely inactive or whilst an application for permission is pending.

It is unclear whether criminal enforcement would be taken under s13 whilst an application for permission is pending. Without further authority clients must proceed with considerable caution particularly as contravening s11 is a 'strict liability' offence to which the defence of innocent intention provided in s352 of the Insolvency Act 1986 (IA 1986) does not apply.
Whilst the court has the power to grant permission retrospectively. It is unlikely to exercise it except in '*extreme cases'* (see below).

The safest course of action for clients is to cease any activity that may amount to taking part in the management of company affairs generally prior to the DRO or DRRO/DRRU being made. Those appointed as directors should confirm termination of this appointment, again prior to the DRO or DRRO/DRRU being made (see below).

Activity in the management of company affairs can resume if the application for permission is granted, and the client may be reappointed as a director, subject to the relevant rules.

What evidence of the debtor's resignation as director is required for the DRO application?

The Citizens Advice DRO Toolkit accessible via Advisernet and WiserAdviser confirms at 13.15.29.67;

Restrictions on your client during the moratorium

"...If your client is currently a director of a limited company, and they don't obtain permission from the court to continue in this role after a DRO is made, the DRO Team will require proof that they have resigned and taken the appropriate action with Companies House. The DRO Team has said that when a client states they have been involved with a limited company, they want intermediaries to check whether the company is still live and whether the client is a director of the company. A free web check can be carried out on the Companies House website at www.companieshouse.gov.uk"

The debtor would need to file a TM01 form with Companies House to terminate their appointment. Once the register on the Companies House website has been updated to show that the client is no longer a director of the company this should be adequate proof for the purposes of the DRO Approved Intermediary to proceed with the application.

Any queries about a client's status as a director or the potential implications of terminating a directorship should be directed to a specialist in company law. Such advice is beyond the remit of the SDAS consultancy service.

Which court should the application be made to?

Section 11(2A)(d)(i) CDDA 1986 provides the appropriate court for applications relating to a DRO moratorium restriction is "*…the court to which the person would make an application under section 251M(1) of the Insolvency Act 1986 (if the person were dissatisfied as mentioned there)"*

The correct court for applications under s251M is confirmed in Rule 9.22 IR 2016. This will be the debtors own hearing centre if they are resident in England and Wales. For further discussion on s251M applications see the article '*Consultancy corner: DROs'* published in the Citizens Advice Adviser Issue 185 journal.

Section 11(2A)(c)(i) & (ii) provides the appropriate court for applications relating to a DRRU/DRRO restriction is *"… the court which made the order, or the court to which the person may make an application for annulment of the undertaking,"*

Rule 9.25(2) IR 2016 confirms applications should be supported by a witness statement and details what this should contain. See the SDAS 'Dealing with Judgment Debts' resource accessible via the IMA networking and information sharing section of the IMA website for guidance on witness statements.

What form should be used for the application?

Since 6 April 2017 there are no longer statutory forms for insolvency applications, only suggested templates. Unfortunately the publicly available insolvency templates do not provide for this application.

Mithani has template forms for the application and witness statements for undischarged bankrupts. These can be amended as necessary in accordance with Rule 9.25 IR 2016 for applications relating to DRO and DRRU/DRRO restrictions. Advisers with clients intending to make the application should submit a consultancy enquiry to SDAS through the appropriate channels and we should be able to assist.

What is the application fee?

The application fee will be £280.00 as an '*Application under the Companies Acts or the Insolvency Act 1986 other than one brought by petition and where no other fee is specified (not payable when made in existing proceedings) - fees order 3.5'.* See page 10 of the EX50 Civil Court fees form. The EX160A fee remission rules apply.

This is because in the case of a DRO there are not yet existing court proceedings. Whilst an application for a DRRO is an 'insolvency proceeding', once the DRRO is made it will be an order of the court and no longer existing proceedings.

Chance of success?

The factors to be considered by the court when exercising its discretion to give permission are the same for DROs as they would be for bankruptcy. *Mithani* outlines the seven main principles which are summarised below.

(1) The court can take any relevant factor that applies in the circumstances of a particular case into account in deciding whether permission should be granted. The discretion is wide and unfettered.

(2) Each case will be considered on its individual facts. Accordingly, the emphasis given by a judge in one particular case to the specific circumstances that apply in

that case will not necessarily be a guide to the weight to be attributed to similar circumstances in another case.

(3) The protection of the public will be of paramount importance. The court will need to undertake a detailed assessment of the risk of public harm posed by the grant of permission and decide whether this may be avoided or minimised by attaching conditions or otherwise. The risk assessment may consider several factors, with emphasis on the following:

(a) the reasons for the entering of a DRO of the applicant and whether those reasons might affect their ability to run a company;

(b) where, as will usually be the case, the application is made by an applicant who is subject to DRO restrictions, the reasons for the imposition of any such restrictions against the applicant and the length of the restrictions.

However, the assessment of risk will not be restricted to those matters. The investigation of the court will extend to a wide variety of different matters such as an enquiry into the existing and future business and affairs of the company in respect of which permission is sought.

(4) That is because the court will not have considered the case for the imposition of a DRRO against them in detail. However, this does not mean that permission will be given to them freely and without conditions. The court will still need to conduct a risk assessment of the harm posed to the public by the grant of permission. This risk of harm is likely to be greater if the person is subject to a DRRO/DRRU. Based on available evidence, if the court concludes that such risk cannot be avoided or minimised either by attaching conditions otherwise, it will refuse to grant permission.

(5) It will not be essential for the applicant to demonstrate 'need'. However, such a need will still be relevant as part of the balancing exercise that the court will be required to carry out in deciding whether permission should be granted.

(6) It is unlikely — save in an extremely rare case — that permission will be granted without any conditions. The approach of the court to the imposition of conditions is likely to be similar to its approach to the imposition of conditions under s172 IA 1986.

(7) Either pursuant to provisions the IA 1986 and IR 2016 or the Civil Procedure Rules (CPR) the court has jurisdiction to grant permission retrospectively under s 11 CDDA 1986. However, it is unlikely to exercise it, save in an extreme case.

Duty of the Official Receiver (OR) to oppose the application if public interest requires

Pursuant to Rule 9.25(3) the OR must be served with notice of the application and will be under a duty *'if he is of opinion that it is contrary to the public interest that the application should be granted'*, to attend on the hearing of the application and oppose it.

The February 2018 Insolvency Service DRO Team Newsletter (freely available via the DRO Toolkit on the Wiser Adviser resources page or via the Member Zone on the IMA website to IMA members) discusses the single application for permission which had been made as of that date. The DRO Team opposed the application (they state that generally they will oppose) and expressed the view that permission should only be granted in very exceptional circumstances.

Despite the DRO Team's opposition the court granted permission with some restrictions on the director's role during the moratorium in that case. However, the facts of the case were arguably exceptional and are discussed in detail in the newsletter. We are not aware that any applications have been made since.

It will be necessary to advise client's considering an application that it is by no means guaranteed to succeed as each application will turn on its facts as confirmed in principles 1 and 3 discussed above.

Costs issues

Debtors should be advised they could have to pay the legal costs of the OR as a result of the application, even if permission is granted but is given subject to conditions arising from the OR opposition. The court will exercise its discretion to award costs in accordance with CPR 44.2. *Mithani* comments that this discretion should be exercised as follows:

‘If the Official Receiver is of the opinion pursuant to the requirements of s 11(3) of the CDDA 1986 that it would be in the public interest for the application to be opposed, then costs are likely to be awarded in accordance with the extent to which the Official Receiver's objections to the grant of permission have been accepted by the court. If permission has been granted subject to conditions, which accept a substantial part of the objections of the Official Receiver, the court may order some or all of the Official Receiver's costs to be paid by the applicant. If on the other hand, the objections of the Official Receiver are substantially rejected, the court may order all or some of the applicant's costs to be paid by the Official Receiver or to make no order as to costs.’

Where the OR is not of the opinion that it would be in the public interest to oppose, *Mithani’s* suggested approach to costs is harsher on the applicant on the basis that the OR’s role in this context would not be adversarial but advisory. However, it is not clear under which provision the OR would be required to oppose or attend an application in an advisory capacity in in the absence of the public interest test being met. This situation seems very unlikely to arise.