

Company Lawyer

2001

Bare undertakings in directors disqualification proceedings: the Insolvency Act 2000, Blackspur and beyond

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Subject: Company law. **Other related subjects:** Insolvency

Keywords: Directors; Disqualification; Statements; Undertakings

Legislation: Company Directors Disqualification Act 1986

Insolvency Act 2000

Case: Blackspur Group Plc (No.3), Re Times, July 5, 2001 (Ch D)

****Comp. Law. 290** Following the enactment of the Insolvency Act 2000, directors' disqualification proceedings can now be settled administratively by the offer and acceptance of undertakings. This article examines the new regime and argues that, unless carefully implemented, it could undermine the overall objectives of the Company Directors' Disqualification Act 1986. In particular, the hope is expressed that the courts will not interpret the legislation as requiring the Secretary of State to accept bare undertakings without any admissions by the director as to the underlying factual basis of disqualification.*

Introduction

Over the last decade, we have seen a huge expansion in the use of civil disqualification proceedings under the Company Directors Disqualification Act 1986 (CDDA), so much so that disqualification of directors is now one of the most significant parts of modern company law. In quantitative terms, the Insolvency Service's response to the National Audit Office Report of October 1993 criticising its effectiveness in implementing the CDDA¹ has been impressive. There has been a dramatic increase in the volume of civil disqualification proceedings brought under the core unfitness provisions in CDDA, sections 6--8, with the result that the number of disqualification orders made by the courts at the behest of the Secretary of State for Trade and Industry and the Official Receiver now runs well in excess of 1,000 per annum. More specifically, according to figures taken from the Insolvency Service's Annual Reports, 1,267 orders were made under CDDA, section 6, in 1997--98, rising to 1,548 orders in 2000--01. This represents an increase of over 20 per cent in four years and compares strikingly with a figure of only 339 section 6 orders for 1992--93, the year immediately preceding the publication of the original National Audit Office report.² There will be those who say, with some justification, that the real extent and effectiveness of this expansion in activity can only be judged by comparing these figures with the numbers of formal insolvencies³ and the numbers of reports identifying elements of unfit conduct received from insolvency practitioners or official receivers over comparable periods.⁴ In relation to the latter, the most recent Insolvency Service Annual Report discloses that the Service's Disqualification Unit received a little over 5,500 positive reports during 2000--01. On the crude assumption that the numbers of reports received and orders made under CDDA, sections 6--7, were to remain constant over, say, the next five years, then taking into account the time-lag between the commencement and conclusion of proceedings, the Disqualification Unit would be taking successful action in between roughly 25 per cent and 30 per cent of all cases reported to it. This may be too little for some. However, given the sheer numbers of directors now being disqualified and the success rate of proceedings actually commenced (currently in the region of 95 per cent), it seems only fair to conclude that much has been achieved by the Disqualification Unit in recent times.

Whether this increase in crude numbers of disqualified directors makes any *qualitative* difference to the protection of creditors and the public is very much open to doubt.⁵ Nevertheless, it is clear that the authorities have been pursuing and are continuing to pursue a policy aimed at maximising the numbers of disqualifications while drawing as much public attention as possible to the regulatory effort that is being expended against those who abuse limited liability. A cursory **Comp. Law. 291* study of DTI press releases from the last five years or so suggests that pursuit of this policy has been accompanied by a sharpening of rhetoric.⁶ Moreover, there have been a number of high-profile cases.

⁷ No doubt a cynic would say that the real purpose of all this activity is to create the impression that the DTI and the Insolvency Service are taking effective regulatory action so as to inspire public confidence. Nevertheless, it cannot be denied that the expansion in the use of the disqualification regime in the period between 1993 and the present day represents a significant investment of political will. In the process, the CDDA has grown from a cottage industry into a sizeable legal enterprise.

As well as being politically significant, this process of expansion has also been legally and culturally significant. Civil disqualification proceedings are now the most visible means by which the law of directors' obligations is enforced and shaped.⁸ This is especially true in relation to the common law obligation requiring directors of companies of doubtful solvency to take account of the interests of creditors when considering whether a course of action is in the company's interests. Furthermore, disqualification proceedings are essentially a form of public interest litigation concerned in part with the advancement of standards of commercial morality throughout the whole business community. The courts have been keen to stress that the CDDA is not merely concerned with keeping errant directors "off the road" and deterring them from misbehaving in the future. Through general deterrence, disqualification also aims to encourage other directors to behave properly.⁹ It is therefore not unreasonable to claim (as, in effect, the courts have done) that the now voluminous corpus of CDDA case law serves as a source of general standards of governance for directors of struggling companies and has created a modern discourse of commercial morality within company law.¹⁰

Although its impact on company law has been considerable, the CDDA has arguably become a victim of its own success. For some time the pressure has been on to find new ways of pursuing and achieving CDDA objectives while, in the same breath, reducing the substantial amount of court time devoted to the hearing of formal disqualification proceedings. The outcome is a major reform brought in by the Insolvency Act 2000 (IA 2000) that enables directors to be disqualified under CDDA, sections 6 and 8, by administrative means without the involvement of the court. Under this "fast-track" system, which came into operation on April 2, 2001,¹¹ the Secretary of State is empowered to accept an undertaking equivalent in effect to a disqualification order in cases where the director consents to being disqualified and the parties are able to reach agreement on the period of disqualification. The purpose of this paper is to consider the policy driving the new undertakings regime and to examine some of the problems that are surfacing during its infancy. The main point to emerge is that "fast-track" disqualification by means of undertakings fits uneasily within the existing scheme of the CDDA. Consequently, while the availability of "quickie" disqualification is bound to lead to further increases in the numbers of disqualified directors coupled with savings in court time, these gains are unlikely to be achieved without some dilution of the CDDA's deterrence and standard-setting functions. It is therefore incumbent on the Secretary of State, as the effective regulator, to implement the reforms with due regard to the overall legislative scheme and also incumbent on the courts, where possible, to assist in this process. This point is developed by reference to the important decision of Patten J. in *Re Blackspur Group plc, Secretary of State for Trade and Industry v. Eastaway*,¹² the first case to arise under the new regime.

The scheme of the CDDA

CDDA, section 1A (as inserted by IA 2000, section 6(2)), only permits the Secretary of State to accept undertakings in cases brought under the core unfitness provisions.¹³ This part of the paper outlines the basic scheme of the CDDA's unfitness provisions and so sets the scene for the discussion of the new undertakings regime which follows.

CDDA, sections 6--9: the law relating to unfit conduct

Section 6 of the CDDA obliges the court¹⁴ to make a disqualification order against an individual if it is satisfied that (a) he is or has been a director of a company which has at any time become insolvent¹⁵ and (b) his conduct as a director of that ***Comp. Law. 292** company (either taken alone or taken together with his conduct as a director of any other company or companies) makes him unfit to be concerned in the management of a company. If the court makes a finding of unfitness it must disqualify the director for at least two years but for no more than 15 years (CDDA, section 6(4)). Only the Secretary of State for Trade and Industry (or the Official Receiver, if the Secretary of State so directs in the case of a director of a company which is in compulsory liquidation in England and Wales) can apply for an order and then only if it appears to her that it is expedient in the public interest that a disqualification order should be made (CDDA, section 7(1)).

There is a separate power of disqualification in CDDA, section 8. This permits the Secretary of State to apply for a disqualification order against a person where information about that person's conduct in

relation to a company has come to light in the course of the exercise of one or more of the statutory powers of investigation specified in section 8(1) and (as is the case with section 6) if it appears to her that it is expedient in the public interest that a disqualification order should be made. Under section 8(2), the court has a discretionary power to disqualify the defendant for up to 15 years where it is satisfied that his conduct in relation to the company makes him unfit to be concerned in the management of a company. In contrast to section 6, there is no requirement for the relevant company to have become insolvent.

In determining whether the defendant is “unfit to be concerned in the management of a company” under either section, CDDA, section 9, requires the court to have regard in particular to the matters mentioned in Schedule 1 which include any misfeasance or breach of fiduciary duty by the director in relation to the company, the extent of the director's responsibility for any failure by the company to comply with certain specified provisions of the Companies Act and the extent of the director's responsibility for the causes of the company becoming insolvent (which may or may not be relevant in a section 8 case). The Schedule is non-exhaustive and so the court can take into account matters not mentioned in it¹⁶ with the result that unfitness is a very broad concept. If proceedings are successful, the court will make an order in the terms set out in CDDA, section 1 (as amended by IA 2000, section 5). Among other things, a disqualification order prohibits the disqualified person from acting as a director or from being concerned in the management of a company for the period specified in the order unless he has the leave of the court. There is also an absolute ban on the disqualified person acting as an insolvency practitioner for the period of the order. A person who acts in breach of a disqualification order commits a criminal offence (CDDA, section 13) and can be made personally liable for the debts of any company in relation to which he acts in a prohibited capacity (CDDA, section 15(1)(a)). Anyone involved in the management of a company who acts, or is willing to act, on instructions given by a person whom he knows at that time to be the subject of a disqualification order also exposes himself to personal liability for that company's debts (CDDA, section 15(1)(b)).

The purpose of the CDDA

As I suggested earlier, a major purpose of the CDDA is “to raise standards in the conduct and responsibility of those who manage companies incorporated with the privilege of limited liability”.¹⁷ In other words, it is concerned in some sense to protect the public through *general* deterrence. The idea is that other directors will be influenced to behave in accordance with the standards that the disqualified director has failed to attain. This view of the CDDA emerged in *Re Grayan Building Services Ltd*,¹⁸ where it was argued on the defendant's behalf that the court should assess the question of unfitness at the date of trial rather than at the time of the relevant conduct. Reliance was placed on the use of the present tense in the wording of section 6(1) (“that his conduct *makes* him unfit”). Rejecting this argument, the Court of Appeal held that the use of the present tense “makes” means only that the court has to make a decision on the evidence *presently before it*. If the evidence of the director's past misconduct demonstrates unfitness, the court is obliged by section 6(1) to disqualify him or her for at least a minimum of two years. This is the case even if the director can demonstrate that in the intervening period he or she has been running other companies (not the subject of proceedings) successfully and responsibly and so poses no threat to the public as at the date of trial. As the CDDA obliges the court to disqualify a director in these circumstances, it follows that Parliament must have intended disqualification to do more than simply protect the public from the disqualified director. As Hoffmann L.J. put it:

“The purpose of making disqualification [under section 6] mandatory was to ensure that everyone whose conduct had fallen below the appropriate standard was disqualified for at least two years, whether in the individual case the court thought that this was necessary in the public interest or not. Parliament has decided that it is occasionally necessary to disqualify a company director to encourage the others.”

Henry L.J. added:

“The statutory corporate climate is stricter than it has ever been, and those enforcing it should reflect the fact that Parliament has seen the need for higher standards.”

Subsequently, Lord Woolf M.R. confirmed in *Re Westmid Packing Services Ltd* that disqualification is not simply concerned with keeping “bad” directors “off the road” but also seeks to protect the public in a wider sense, by deterring the disqualified director and by encouraging other directors to behave responsibly.¹⁹ If this wider function is to be carried out effectively, the process by which directors are disqualified must be visible to the business community and the public so that everyone is clear as to

the reasons for disqualification ***Comp. Law. 293** and the standards of conduct that are expected. Unless it is carefully implemented, the new undertakings regime could well reduce the visibility of disqualification proceedings and accordingly undermine the operation of the CDDA.

Disqualification undertakings: origins and purpose

The law on undertakings pre-Insolvency Act 2000

Broadly speaking, it was not possible before April 2, 2001 for the parties to settle a disqualification case on the basis of an undertaking that the director would refrain from acting in any of the prohibited capacities mentioned in CDDA, section 1, for an agreed period. In the leading case of *Re Blackspur Group plc, Secretary of State for Trade and Industry v. Davies* (“*Blackspur-Davies*”),²⁰ the Court of Appeal held that the Secretary of State's decision to continue disqualification proceedings against the defendant, despite his undertaking not to act as a director or in any other prohibited capacity, was not open to review. In the court's opinion, it was reasonable for the Secretary of State to refuse an offer of undertakings on the following grounds:

(1) Once proceedings had been commenced, it was for the court and not the parties to decide whether or not a disqualification order should be made. Under CDDA, sections 6(1) and 8(2), the court could only make a disqualification order if it was “satisfied” that the director's conduct made him unfit. As the statute required *the court* to be “satisfied” of the director's unfitness, the judge could not be asked to make a disqualification order by consent of the parties without first forming some view of the underlying merits.²¹

(2) The means by which protection of the public was to be achieved was embodied in a detailed legislative scheme that did not expressly provide for the disposal of proceedings on the basis of undertakings without any admission as to the factual basis of disqualification. The Secretary of State was therefore entitled to adhere to the statutory scheme in the interests of good regulation.

(3) The undertakings offered by the defendant did not provide the public with the same level of protection as that afforded by a disqualification order even though they were expressed to be permanent in duration. Disqualification undertakings were inferior in three respects. First, breach of an undertaking, as opposed to an order, would not trigger the enforcement provisions in CDDA, sections 13-15 (which, among other things, impose personal liability on the disqualified person for the debts of relevant companies and accessory liability on third parties). Secondly, there was no statutory procedure governing the grant of leave to act in a prohibited capacity where undertakings had been given. Finally, there was no scope for undertakings to be publicised by means of an entry in the register of disqualification orders maintained by the Secretary of State under CDDA, section 18(2).

In *Blackspur-Davies*, the Court of Appeal did not go as far as to rule that the acceptance of undertakings would be *ultra vires* the CDDA in all cases. Thus, it was possible for the court, with the agreement of the Secretary of State, to stay proceedings on undertakings without formally disposing of them.²² Equally, it was open to the Secretary of State to discontinue proceedings where undertakings had been offered if she formed the view that it was no longer in the public interest to proceed to trial. However, for the reasons given above, the Secretary of State was generally entitled to decline an offer of undertakings with the result that an application by the defendant for a stay on the ground that she was acting unreasonably in continuing the proceedings could easily be resisted. The prevailing view, epitomised by the decision in *Blackspur-Davies*, was that some form of legislative intervention would be required before the parties could dispose of cases on undertakings as a matter of routine.

Carecraft disposals

Despite the position in relation to undertakings, it was possible under the pre-IA 2000 law for civil disqualification proceedings to be disposed of on a summary basis using a procedure sanctioned by Ferris J. in *Re Carecraft Construction Co. Ltd*²³ and approved by the Court of Appeal in *Secretary of State for Trade and Industry v. Rogers*.²⁴ Under the *Carecraft* procedure, the parties can put a statement of agreed or noncontested facts before the court and invite the court to make a disqualification order for an agreed period or a period falling within an agreed range. The court is then asked to make findings and dispose of the matter without the necessity of a full trial. It is the essence of *Carecraft* that the court is not strictly bound by the agreement reached by the parties. Strictly speaking, the court must make its own findings based on the *Carecraft* statement.²⁵ In theory, the

court could hold that the conduct described in the *Carecraft* statement is of insufficient gravity to merit a finding of unfitness. Alternatively, the court might be satisfied that the agreed conduct makes the director unfit but disagree with the parties' assessment of the appropriate period of disqualification. If the court disagrees with the parties on either question, the case is adjourned to a full hearing with both sides able to adduce evidence in the normal way. The *Carecraft* procedure has proved something of a success and is used widely in CDDA, section 6 cases.²⁶ Although, in practice, *Carecraft* is something of a rubber-stamping exercise, the court is the ultimate arbiter and a summary disposal results in the making of a disqualification order. Thus, the objections raised in the *Blackspur-Davies* case could not be levelled at this method of compromising proceedings.

***Comp. Law. 294 Calls for reform**

Despite the relative success of *Carecraft*, support grew in the second half of the 1990s for the idea that the CDDA should be amended to enable the Secretary of State to settle disqualification cases in a way that achieved the same legal effect as a disqualification order without the court having to hear the matter at all, even on a summary basis. The first public call for reform was made by the then Vice-Chancellor, Sir Richard Scott, in December 1995. In a Practice Direction²⁷ aimed in part at streamlining *Carecraft*, he made the following recommendation:

"Under the 1986 Act, there is no alternative but for all applications for disqualification orders, no matter what state of agreement there may be between the parties, to be processed through the court machinery and made by a judge or registrar after a court hearing. I regard this as unnecessary and avoidable. I would recommend, accordingly, that the Secretary of State give consideration to the possibility of introducing amending legislation, under which an agreement between a director and the Secretary of State, or the Official Receiver, as to the disqualification period to be applied to the director, be given the same effect as a court order imposing the disqualification period. If the director is willing to bar himself from acting as a director for a period that the Secretary of State, or Official Receiver regards as being sufficient to protect the public interest, I do not see why time and money should be expended by insistence on bringing the case before the court."

Similar judicial recommendations were made in the course of subsequent *Carecraft* cases²⁸ and were echoed by the Court of Appeal in *Blackspur*.²⁹ There can be little doubt that this growth in judicial support for a statutory system of undertakings was a reflection of the increasing pressure that disqualification cases were bringing to bear on court resources. In particular, there was a strong feeling that *Carecraft* was little more than a rubber-stamping exercise that did not merit the amount of court time devoted to it. The government's response to these calls for reform is enshrined in section 6 of the IA 2000. The undertakings regime introduced by this provision is now considered in detail.

The new undertakings regime

Policy

It is clear from the available parliamentary materials that the government aims to increase still further the raw numbers of persons being disqualified while, at the same time, reducing the amount of public expenditure and court time devoted to disqualification proceedings. It was suggested during the parliamentary debate that undertakings will save the DTI an estimated £300,000 per annum.³⁰ Although there was praise for *Carecraft*, it was felt that the procedure still involved unnecessary costs such as the costs of negotiating the statement of agreed facts and attending court.³¹ The government's key objective is to reduce the time the courts spend dealing with the 90 per cent of cases in which proceedings are commenced but do not proceed to trial.³² As we will see below, the Secretary of State is able to accept undertakings and dispose of cases even before formal proceedings are commenced. Cases dealt with in this way will be taken out of the court system altogether. In the process, disqualification proceedings will be brought much more into line with ordinary civil proceedings.³³ It is also claimed that the undertakings regime will improve regulation by enabling more directors to be processed through the system more quickly, thus providing earlier protection for the public.³⁴

Scope³⁵

The main features of the new regime are as follows:

- (1) A disqualification case against a person can be compromised by the Secretary of State accepting

a bare undertaking in terms that, for a period specified in the undertaking, that person (a) will not be a director of a company, act as receiver of a company's property or in any way, whether directly or indirectly, be concerned or take part in the promotion, formation or management of a company unless (in each case) he has the leave of the court, and (b) will not act as an insolvency practitioner (CDDA, section 1A).

(2) The decision to accept an undertaking is exclusively a matter within the Secretary of State's administrative discretion. Hitherto, the Secretary of State's discretion has been merely prosecutorial. Disqualification proceedings can only be commenced "if it appears to the Secretary of State that it is expedient in the public interest that a disqualification order should be made" (CDDA, sections 7(1) and 8(1)). Under the new regime, the Secretary of State enjoys a wider discretion. Before an undertaking can be accepted, two criteria must be applied. First, the Secretary of State must assess whether the conditions in CDDA, sections 6(1) or 8(1) (as appropriate), are satisfied, *i.e.* it must appear to the Secretary of State from the material available that the director's conduct makes him unfit. It follows that the question of "unfitness" is no longer exclusively a matter for the court. Secondly, the Secretary of State must consider that it is expedient in the public interest to accept an undertaking instead of apply ***Comp. Law. 295** ing, or proceeding with an application, for a disqualification order (CDDA, sections 7(2A) and 8(2A)). Subject to the agreement of the parties, the upshot is that a director can be disqualified exclusively by administrative means. It is clear that the Secretary of State's decision to refuse an undertaking and press on with proceedings is susceptible to judicial review in the normal way.³⁶ In cases where undertakings are accepted, the court has power under CDDA, section 8A, to vary an undertaking by reducing the period for which it is to be in force or to discharge an undertaking altogether. By ensuring that the matter can still be reviewed by an impartial tribunal independent of the Secretary of State, section 8A amounts to a guarantee of the disqualified person's due process rights under Article 6 of the ECHR.

(3) It is clear from the wording of CDDA, sections 7(2A) and 8(2A), that the Secretary of State can accept undertakings either *before or after* proceedings are initiated. It is unlikely that the Secretary of State will consider an offer of undertakings before the point at which she would ordinarily decide to bring proceedings. This is because she is required by CDDA, sections 7(2A) and 8(2A), to form a view on the merits.³⁷

(4) An undertaking has exactly the same legal effect as a disqualification order.³⁸

Current practice and emerging problems

As the Secretary of State is required by the legislation to consider whether a director is unfit before accepting an undertaking, the Disqualification Unit continues to follow all of its usual pre-action procedures and puts together its basic case. The decision is then taken on whether to commence proceedings. The Secretary of State is obliged by CDDA, section 16(1), to give not less than 10 days' notice of her intention to apply for a disqualification order.³⁹ Her current practice is to send the director a letter before action containing a brief statement of the unfit conduct on which she proposes to rely and an indication of the period of disqualification that she considers would be appropriate. The director is also advised in the letter before action that it is possible for him to compromise the matter by offering a disqualification undertaking, which if accepted, would have the same effect as a disqualification order. The Disqualification Unit has revised its procedures to ensure that there is time between the sending out of the letter before action and the commencement of proceedings for the parties to consider a settlement.

The main problem to emerge thus far concerns the contents of a disqualification undertaking. In contrast to the position under the *Carecraft* procedure, it is clear that the parties are not formally required by the new legislation to negotiate and agree a statement of unfit conduct. The Secretary of State clearly has the power to accept a bare undertaking simply recording, in the terms of CDDA, section 1A, that for a specified period the person giving the undertaking will not act as a director etc. without the court's leave nor as an insolvency practitioner. However, in practice, the Secretary of State will only accept an undertaking where the director is prepared to admit (or, at least, not dispute) the factual basis of the disqualification, short details of which are then recorded in a schedule annexed to the undertaking. Within days of the undertakings regime coming into force, this practice was challenged in *Re Blackspur Group plc, Secretary of State for Trade and Industry v. Eastaway* ("*Blackspur-Eastaway*").⁴⁰ Having previously failed in various attempts to halt the proceedings against him, including an application to have the case dismissed on grounds that its prosecution infringed his rights under ECHR, Article 6,⁴¹ Mr Eastaway indicated that he wished to take advantage of the new

law by offering a disqualification undertaking. However, he was not prepared to give a disqualification undertaking in the form required by the Secretary of State. In particular, he was unwilling to agree that a schedule of unfit conduct should be annexed to or form part of the undertaking fearing stigma and the impact that any admissions might have on his career as an accountant. The question for the court was whether the proceedings should be stayed or dismissed on the ground that the Secretary of State was acting unreasonably in refusing to accept the bare undertaking on offer. The application was argued on the basis that the Secretary of State would only be acting unreasonably if the applicant could establish that the practice of requiring a schedule of unfit conduct containing admissions of fact was *ultra vires* and unlawful. The applicant's case was that CDDA, section 1A, empowered the Secretary of State to accept only a bare undertaking without any admission of liability, the object being to eliminate the need for and costs of court proceedings. There was nothing in the amended legislation giving the Secretary of State power to insist that a director agree to a schedule of unfit conduct before an undertaking could be accepted nor had any such requirement been imposed in regulations made under the rule-making power in CDDA, section 21(2). In a decision currently the subject of a pending appeal, Patten J. rejected Mr Eastaway's application holding that the Act confers a discretion on the Secretary of State to seek and obtain the director's agreement to a sched ***Comp. Law. 296** ule of unfit conduct in an appropriate case. The judge's grounds for reaching this conclusion were as follows:

(1) The Secretary of State must as a pre-condition to the acceptance of a disqualification undertaking form the view on the evidence that the conduct of the relevant director makes him unfit so as to justify disqualification. Although this is not a judicial process as such, it does require the Secretary of State to exercise a judgment and to form a conclusion on the material before her. It would be odd if Parliament, while requiring the Secretary of State to perform that exercise in order to be able to accept the undertaking, nevertheless intended that she should have no power either to agree and accept a statement of the grounds upon which she concluded that unfitness had been made out or in appropriate cases to insist upon such a statement before being prepared to accept the undertaking.

(2) The factual basis for the making of disqualification orders (including orders made under the *Carecraft* procedure) ensures the deterrent effect of such orders and thereby the protection of the public against those unfit to assume the role of directors. There is nothing in the CDDA as amended to suggest that Parliament did not intend that disqualification undertakings should have the same effect. Indeed, if the purpose of the amended legislation is to enable directors to give disqualification undertakings without any admission of liability, it is difficult to see why it requires the Secretary of State to be satisfied that a case of unfitness has been made out.

(3) A knowledge and understanding of the grounds upon which an undertaking was accepted is relevant in the determination of any subsequent application for leave to act as a director under CDDA, section 17, or for the variation or discharge of the undertaking under CDDA, section 8A. If the Secretary of State is able to agree a statement of grounds then this benefits both parties as the basis for disqualification is clearly defined and neither party will be required or be able to contest those matters on such an application. Parliament cannot have intended that in the case of disqualification undertakings the court could be required to decide contested issues of fitness years after the event merely for the purpose of determining whether, for example, the director in question should now be allowed to return to business.

(4) The lack of any detailed regulations made under the rulemaking power in CDDA, section 21, prescribing the form that an undertaking should take and requiring the parties to agree a schedule of unfit conduct was also immaterial. If, as Mr Eastaway contended, the Secretary of State had no power under the primary legislation to accept undertakings coupled with an agreed statement of grounds, it was difficult to see how such a power could be conferred by means of delegated legislation.

In the writer's view, Patten J.'s reasoning is compelling on both philosophical and practical grounds and should be supported on the forthcoming appeal. For reasons of efficiency, the amended legislation provides a means by which disqualification proceedings can be compromised without the need (as is the case with the *Carecraft* procedure) for the court to make findings. In this sense, it brings disqualification proceedings into line with ordinary civil litigation within the sphere of private law. However, this does not alter the fact that, both in form and substance, disqualification proceedings are brought in the public interest and so raise concerns about publicity and transparent dealing. As we saw earlier, disqualification of directors is justified on a rationale of public protection (including protection through general deterrence) and, as Patten J. rightly emphasised, the Secretary of State is required, in deciding whether to accept an undertaking, to consider this public interest. In keeping with that rationale, there is a compelling case for saying that, in the absence of exceptional

circumstances, details of the conduct forming the basis for disqualification should be a matter of public record. Disqualification orders and undertakings differ in terms of public accessibility. An order is made on the basis of a judgment given in open court. The reasons for the disqualification are readily accessible. Similarly, in *Carecraft* cases, a judgment is given and it is standard practice for the agreed statement of facts to be annexed to the order.⁴² In the absence of an agreed schedule of unfit conduct that could be publicised by means of press release, the factual basis of a disqualification undertaking is not obviously within the public domain. If the Court of Appeal rules that the only course open to the Secretary of State is to accept bare undertakings without any admission of liability, the scheme of the CDDA will accordingly be undermined. It would be tantamount to saying that the public interest in efficient disposal of disqualification cases outweighs the public interest in the process of disqualification itself.⁴³ Finally, on the philosophical point, it seems clear that the amended legislation was designed to meet the objections raised in the original *Blackspur-Davies* case. It was recognised in that case that the factual basis for making orders, whether in contested proceedings or under *Carecraft*, ensures that disqualification, based on findings or admissions of unfitness, protects the public through deterrence. Indeed, the Court of Appeal's main reason for upholding the Secretary of State's decision to press on with the proceedings was that undertakings without some admission of liability did not offer the public the same degree of protection as a disqualification order. It surely follows that Parliament must have intended that statutory undertakings provide equivalent protection, including protection through deterrence. Any concerns that the director may have about the use of admissions in other proceedings⁴⁴ can be dealt with by the parties agreeing that admissions in a schedule of unfit conduct are made solely for the purposes of the CDDA.⁴⁵

Patten J.'s decision also makes abundant sense on practical grounds. The point that it is possible within the scheme of the CDDA for a director disqualified by undertaking to make subsequent applications either for leave to act while disqualified or for the variation or discharge of the undertaking is a point well made. In those proceedings, the court will need to be given a clear idea as to the factual basis of the disqualification. On an application for leave, the critical question is whether, if leave is granted, the public will be adequately protected from the risk that the conduct that led to the applicant's disqualification might recur. Clearly, in this respect, the nature and seriousness of the applicant's previous ***Comp. Law. 297** conduct is highly material.⁴⁶ The same can be said for an application under section 8A. Take, for example, a director who gives a bare undertaking for a period of eight years but without making any admissions as to the underlying conduct. What if he subsequently applies to vary the undertaking on the ground that an eight-year disqualification is excessive? In formal disqualification proceedings (including those disposed of summarily under *Carecraft*) the question of the appropriate period of disqualification is a matter for the discretion of the court⁴⁷ to be determined in accordance with guidelines laid down by the Court of Appeal.⁴⁸ In exercising the discretion, the court is required to ensure that the period of disqualification reflects the gravity of the misconduct. While there may be subtle differences between this judicial discretion and the administrative discretion in CDDA, sections 7(2A) and 8(2A),⁴⁹ the court could not review the Secretary of State's decision to accept an undertaking in this type of case without making some reference to the original misconduct. It is therefore in the interests of efficient regulation that the parties agree and set out the factual basis of a disqualification undertaking. Otherwise, the court would be obliged to reopen the question of the director's unfitness. This seems absurd and self-defeating given that the whole idea of the undertakings regime is to allow the parties to settle such questions once and for all without recourse to the court. There can be little argument either with Patten J.'s conclusion on the secondary point concerning the rule-making power in CDDA, section 21(2). An alternative argument is that the CDDA as amended might be read as conferring a power on the Secretary of State but one subject to detailed rules in regulations that have not as yet been made. However, this point can be answered by reference to the *Carecraft* procedure which came about without the need for detailed rule-making in regulations.

Finally, there is nothing in the parliamentary materials that contradicts Patten J.'s decision. The Trade and Industry Select Committee formed the view that there could usefully be express legislative provision for a statement of facts on which the undertaking was based so as to assist the court in future proceedings.⁵⁰ Concerns about lack of transparency and publicity were also aired.⁵¹ In the government's view, there was a risk that the imposition of a mandatory requirement for an agreed schedule of unfit conduct could delay disqualification and increase costs in cases where the parties found difficulty in agreeing the schedule. However, the minister responsible did state that the normal practice of the Secretary of State would be to seek agreement as to the factual basis for disqualification before accepting an undertaking.⁵² Thus, the parliamentary materials reveal a concern for flexibility that is consistent with the notion that the Secretary of State enjoys a discretion.

Conclusion

It is now theoretically possible for the Secretary of State to accept a disqualification undertaking from a director who disputes some or all of the allegations of unfit conduct made against him. It is likely that there will be considerable political pressure on the Insolvency Service to accept undertakings without admissions so as to achieve the policy objective of disqualifying more directors at the same or less cost. However, if the Secretary of State is forced to accept bare undertakings as a matter of routine, the wider concerns of the CDDA will be undermined. The public interest in "quickie" disqualification would come to outweigh all other considerations, including the public interest in the promotion of good corporate governance. The Secretary of State's practice of refusing to accept an undertaking unless the factual basis of the disqualification is agreed is consistent with the overall scheme of the CDDA and strikes a proper balance between these different aspects of the public interest. It is to be hoped that the Court of Appeal will uphold Patten J.'s decision in *Blackspur-Eastaway* and give further guidance so that the undertakings regime can operate successfully but in a manner consistent with the wider objectives of the legislation.

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1. The Insolvency Executive Agency, *Company Director Disqualification* (1993).
2. The National Audit Office has commented favourably on the increase in the numbers of directors being processed through the courts in a second report published in 1999: see "Company Director Disqualification--A Follow-Up Report", May 21, 1999 (1998-99 H.C. 424).
3. Meaning for these purposes liquidations, administrations and administrative receiverships: see CDDA, s. 6(2).
4. Office holders of insolvent companies are under a statutory obligation to file a report on every director of the company advising the Secretary of State whether or not the conditions in CDDA, s. 6(1) (the principal one being that his conduct as a director of the company would, in the eyes of the court, make him unfit to be concerned in the management of a company) are satisfied as respects that director: see CDDA, s. 7(3), the Insolvent Companies (Reports on Conduct of Directors) Rules 1996 (S.I. 1996 No. 1909) and generally A. Walters and M. Davis-White, *Directors' Disqualification: Law and Practice* (Sweet & Maxwell, 1999), chapter 3.
5. A high percentage of disqualification orders made under CDDA, s. 6, are made against owner-managers of small companies for periods between two years (the statutory minimum) and five years. For example, while in 2000-01 there was a 27 per cent increase in orders obtained for periods between 11 years and 15 years (the statutory maximum), roughly 57 per cent of the 1,548 orders made under CDDA, s. 6, fell within the two-to-five-year bracket. It has been argued that the increase in numbers of relatively short disqualifications has done little to improve public protection and that a policy of pursuing "quality rather than quantity" with a view to disqualifying more serious offenders for longer periods should be adopted: see A. Hicks, *Disqualification of Directors: No Hiding Place for the Unfit?* (ACCA Research Report No. 59, 1998).
6. See e.g. "Dodgy Directors Top of Insolvency Service's Hitlist" (August 15, 1995), "78 Per Cent More 'Bad Bosses' Banned by Insolvency Service" (February 20, 1996), "Unfit Directors of 'Phoenix' Companies Grounded as Disqualification Orders Soar" (November 12, 1996), "Griffiths Goes Gunning Against Cowboy Directors" (June 5, 1997), "Griffiths Promises No Let Up in Campaign to Ban Rogue Directors" (April 30, 1998), "Insolvency Service is Winning Battle in Clamp Down on Dodgy Directors" (November 30, 1999) and "Clamp Down on Dodgy Directors Continues" (April 18, 2000).
7. As well as the successful proceedings arising out of the collapse of Barings, disqualification orders are also currently in force in relation to a former manager of England's international football team and a well-known boxing promoter.
8. See, in particular, *Re Barings (No. 5)* [1999] 1 B.C.L.C. 433 affirmed [2000] 1 B.C.L.C. 523, CA, a CDDA, s. 6 case in which the judge reformulated the duties of care, skill and diligence, laying particular emphasis on the supervisory responsibilities of directors. For amplification of this point, see L.S. Sealy, "Directors' Duties Revisited" (2001) 22 *Company Lawyer* 79; and A. Walters, "Directors' Duties: The Impact of the Company Directors Disqualification Act 1986" (2000) 21 *Company Lawyer* 110.
9. See e.g. *Re Swift 736 Ltd* [1993] B.C.L.C. 896; [1993] B.C.C. 312, CA, *Re Grayan Building Services Ltd* [1995] Ch. 241; [1995] 3 W.L.R. 1; [1995] B.C.C. 554, CA, *Re Westmid Packing Services Ltd* [1998] 2 All E.R. 124 and the general discussion in Walters and Davis-White, n. 4 above.
10. For example, the courts have used the concept of unfitness in the CDDA to fashion minimum standards of financial stewardship based on the statutory obligations relating to the maintenance of accounting records and the preparation of proper accounts: see Walters and

Davis-White, n. 4 above, especially paras 5.02, 5.13-5.19 and 5.52.

11. See the Insolvency Act 2000 (Commencement No. 1 and Transitional Provisions) Order 2001 (S.I. 2001 No. 766). The substantive provisions and other consequential amendments are contained in IA 2000, s. 6 and Sched. 4.
12. Unreported, May 23, 2001, Ch D.
13. CDDA, ss. 2-5 and 10, confer various other powers of disqualification on the courts. Most of these are hangovers from earlier Companies Acts and the types of misconduct with which they are concerned can equally fall within the much broader concept of unfitness that has developed under CDDA, ss. 6-9. As a result, these powers are rarely used and the vast majority of disqualification proceedings are brought under the unfitness provisions. The overlap may raise issues of double jeopardy and/or abuse of process, especially where a criminal court exercises the power of disqualification in s. 2 following the defendant's conviction for an indictable offence in connection with the management of a company and there are separate civil proceedings on foot under the unfitness provisions covering similar ground: see e.g. *Secretary of State for Trade and Industry v. Rayna* [2001] 2 B.C.L.C. 48.
14. Broadly speaking, a court having winding-up jurisdiction: see CDDA, s. 6(3), as substituted by IA 2000, Sched. 4, para. 5.
15. Within the meaning of CDDA, s. 6(2). Broadly speaking, the court only has jurisdiction if the relevant company is or has been the subject of a formal insolvency regime, i.e. insolvent liquidation, administration or administrative receivership. A company which enters a free-standing corporate voluntary arrangement under Part I of the Insolvency Act 1986 does not "become insolvent" and so falls outside the scope of s. 6.
16. See e.g. *Re Bath Glass Ltd* [1988] B.C.L.C. 329 at 332; *Re Samuel Sherman plc* [1991] 1 W.L.R. 1070 at 1073; *Re GSAR Realisations Ltd* [1993] B.C.L.C. 409 at 421; *Secretary of State for Trade and Industry v. Taylor* [1997] 1 W.L.R. 407 at 412; *Re Amaron Ltd* [2001] 1 B.C.L.C. 562 at 568; *Re Sykes (Butchers) Ltd* [1998] 1 B.C.L.C. 110 at 125; *Re Bradcrown Ltd* [2001] 1 B.C.L.C. 547 at 550; and generally Walters and Davis-White, n. 4 above, chapters 4-5.
17. *Re Bradcrown Ltd* [2001] 1 B.C.L.C. 547 at 550.
18. [1995] Ch. 241; [1995] 3 W.L.R. 1; [1995] B.C.C. 554, CA.
19. Deterrence and the raising of standards is emphasised in other cases: see especially *Re Swift 736 Ltd* [1993] B.C.L.C. 896; [1993] B.C.C. 312, CA; and the discussion in Walters and Davis-White, n. 4 above, chapters 2 and 4. Interestingly, a similar view of the nature and purpose of disqualification has been adopted in relation to s. 8, even though disqualification under that provision is discretionary rather than mandatory: see *Re Atlantic Computers plc*, unreported, June 15, 1998, Ch D, Lloyd J.
20. [1998] 1 W.L.R. 422; [1998] 1 B.C.L.C. 676; [1998] B.C.C. 11, CA.
21. As Ferris J. put it in *Re Carecraft Construction Co. Ltd* [1994] 1 W.L.R. 172 at 181: "In disqualification proceedings ... there is no scope for the parties to reach an agreement and then ask the court to embody their agreement in a consent order. The court itself has to be satisfied, after having regard to the prescribed matters and other facts which appear to be material, that the [director] is unfit to be concerned in the management of a company; and the court itself must decide the period of disqualification if it decides to make a disqualification order."
22. See e.g. *Re Homes Assured Corporation plc* [1996] B.C.C. 297, Ch D (on which see further *EDC v. United Kingdom* [1998] B.C.C. 370, ECommHR) and *Re Company X*, unreported, February 1, 1996, Ch D. See also *Secretary of State for Trade and Industry v. Cleland* [1997] 1 B.C.L.C. 437; [1997] B.C.C. 473, Ch D, though this case is difficult to reconcile with *Blackspur-Davies*.
23. [1994] 1 W.L.R. 172; [1993] 4 All E.R. 499; [1993] B.C.L.C. 1259; [1993] B.C.C. 336, Ch D.
24. [1996] 1 W.L.R. 1569; [1996] 4 All E.R. 854; [1996] 2 B.C.L.C. 513; [1997] B.C.C. 155, CA. For a fuller account of the *Carecraft* procedure than that provided here, see Walters and Davis-White, n. 4 above, chapter 8.
25. For an example of what a *Carecraft* statement might look like, see Walters and Davis-White, n. 4 above, Appendix 8.
26. It is also used in CDDA, s. 8 cases: see e.g. *Re Aldermanbury Trust plc* [1993] B.C.C. 598. Moreover, there is no reason in principle why it could not be used in civil disqualification proceedings brought under ss. 2-4.
27. *Practice Note (Chancery Division: Directors Disqualification Applications)* [1996] 1 All E.R. 442.
28. See *Secretary of State for Trade and Industry v. Rogers* [1996] 1 W.L.R. 1569 at 1574; *Official Receiver v. Cooper* [1999] B.C.C. 115 at 119.
- 29.

[1998] 1 W.L.R. 422 at 429.

30. See the report of proceedings in House of Commons Standing Committee B (5th Sitting, November 7, 2000). The figure of £300,000 derives from the government's regulatory impact assessment. The financial memorandum accompanying the Bill stated that there would be no net benefit to the taxpayer. This suggests that any saving will be ploughed back in with a view to achieving efficiency gains, *i.e.* further increases in the numbers of directors being processed on roughly the same budget.
31. See *e.g.* Trade and Industry Select Committee, Second Report, "Draft Insolvency Bill" (December 20, 1999), para. 40.
32. Parliament was told that, on current figures, only 10 per cent of disqualification proceedings in which an order is made are contested and go to a full trial. Of the remainder, 30 per cent are disposed of by agreement (presumably under *Carecraft*) while 60 per cent are simply uncontested: see *Hansard*, H.L., April 4, 2000, col. 1251; *Hansard*, H.C., October 24, 2000, col. 166.
33. The concern for greater efficiency in the management of court resources can be seen as part of the wider attempt to streamline the administration of justice through implementation of the Woolf reforms.
34. See *e.g.* "New Insolvency Act Receives Royal Assent" (DTI Press Release P/2000/808, December 1, 2000).
35. All statutory references in this section of the paper are to the CDDA, as amended by the Insolvency Act 2000, s. 6.
36. As has always been the case with the discretion to commence and/or continue proceedings: see *Blackspur-Davies* (discussed above) and *R. v. Secretary of State for Trade and Industry ex parte Lonhro* [1992] B.C.C. 325, QBD. Given that a statutory undertaking has the same effect as a disqualification order, a decision to press ahead with proceedings where one has been offered is much more vulnerable to challenge than a similar decision made under the old law.
37. In evidence to the Select Committee, Desmond Flynn of the Insolvency Service said: "We propose if this measure is adopted by Parliament that we will pursue our investigations in exactly the same way as we do now and take them up to the point where under our current rubric we would be issuing proceedings. At that point when we have fully worked up a case with fully displayed grounds of what we think is unfit conduct we will then do a smart side step to the right and say 'This is our case. We think this represents a seven-year disqualification, what the court would order if we take proceedings against you. You now have the opportunity to give us an undertaking and unless that undertaking is forthcoming in more or less those terms, related to what we think is the degree of unfitness, we will proceed to court proceedings.'" (Trade and Industry Select Committee, Second Report, "Draft Insolvency Bill", December 20, 1999, Minutes of Evidence, Q172).
38. The IA 2000 makes a series of amendments to the CDDA designed to meet the objections raised in the *Blackspur-Davies* case. See CDDA, ss. 1A(1) and 1(1) as amended by IA 2000, s. 5(1) (nature of prohibition); CDDA, ss. 1A(1)-(2) (period of disqualification); CDDA, ss. 13-15, as amended by IA 2000, Sched. 4, paras 8-10 (sanctions for breach of undertaking); CDDA, ss. 1A(1) and 17(3), as substituted by IA 2000, Sched. 4, para. 12 (leave to act); and CDDA, s. 18, as amended by IA 2000, Sched. 4, para. 13 (registration).
39. See generally Walters and Davis-White, n. 4 above, paras 6.27-6.30.
40. Unreported, May 23, 2001, Ch D. Mr Eastaway is a co-defendant in the disqualification proceedings that gave rise to the *Blackspur-Davies* decision on pre-IA 2000 undertakings discussed above.
41. [2001] 1 B.C.L.C. 653.
42. See Walters and Davis-White, n. 4 above, paras 8.18-8.19, though note also *Official Receiver v. Cooper* [1999] B.C.C. 115, Ch D.
43. The view seemingly (and dubiously) adopted by the court in *Official Receiver v. Cooper* [1999] B.C.C. 115, Ch D.
44. *E.g.* wrongful trading or avoidance proceedings brought by an office holder under the Insolvency Act 1986.
45. Although it may be of little comfort to office holders, the Secretary of State's current practice is to accept undertakings on this basis.
46. See *e.g.* *Re Tech Textiles Ltd* [1998] 1 B.C.L.C. 259, Ch D; *Re TLL Realisations Ltd* [2000] 2 B.C.L.C. 223; [2000] B.C.C. 998, CA; *Re Westminster Property Management Ltd (No. 2)* [2001] B.C.C. 305; and generally Walters and Davis-White, n. 4 above, chapter 13. Moreover, in *Blackspur-Davies*, the Court of Appeal said that, even if an extra-statutory procedure for the granting of leave to act under an undertaking could be devised, it would be difficult for it to operate in the absence of findings or admissions of fact made at the time when the undertaking was given. It seems fair to assume that Parliament did not intend the operation of the statutory undertakings regime to be similarly hampered.
47. *Re Bradcrown Ltd* [2001] 1 B.C.L.C. 547 at 551.
- 48.

In *Re Sevenoaks Stationers (Retail) Ltd* [1991] Ch. 164; [1990] 3 W.L.R. 1165; [1991] 3 All E.R. 578, CA; and *Re Westmid Packing Services Ltd* [1998] 2 All E.R. 124.

[49.](#) See A. Walters, "Directors' Disqualification After the Insolvency Act 2000" (2001) *Insolvency Lawyer* 86 at 92-93.

[50.](#) Trade and Industry Select Committee, Second Report, "Draft Insolvency Bill", December 20, 1999, para. 40. The recommendation appears to stem from a memorandum submitted to the Select Committee by the Law Society. Christopher Chope MP suggested that a statement of facts could also assist professional bodies in dealing with any consequential disciplinary matters: see the report of proceedings in House of Commons Standing Committee B (5th Sitting, November 7, 2000).

[51.](#) *ibid.*

[52.](#) See *Hansard*, H.C., October 24, 2000, cols 186-187, 192 and the report of proceedings in House of Commons Standing Committee B (5th Sitting, November 7, 2000). Patten J. felt able to admit the ministerial statements made in Standing Committee under *Pepper v. Hart* [1993] A.C. 593; [1992] 3 W.L.R. 1032; [1993] 1 All E.R. 42, HL. However, it is clear that he would have reached the same decision without reference to that material.

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