

Directors in the frame

Shareholder dissatisfaction at company performance in the UK often focuses on directors' responsibilities. The Companies Act 2006 codified certain general duties such as the duty to promote the interests of the company and directors' obligations have also been refined over the years by case law. Certain legislative provisions affecting directors extend to "shadow directors", i.e. persons on whose instructions the directors of a company are accustomed to act. Forensic accountants can assist lawyers in actions arising from alleged breaches of directors' responsibilities.

Examples of breaches and their consequences

Directors may breach their responsibilities in numerous ways. Some examples of the areas which may involve forensic accountants and the possible consequences for directors are as follows:

Director may be liable to the company for profits made or to make good losses *if he or she...*

- fails to exercise appropriate level of skill and diligence
- has an interest in a contract with the company which is not authorised
- uses the company's assets, opportunities or information without the informed consent of shareholders
- diverts business from the company
- purchases assets from the company at an undervalue
- borrows unlawfully from the company, i.e. without member approval

Director may be required to contribute to the company's assets in a winding-up *if he or she...*

- is knowingly a party to trading with intent to defraud
- is party to wrongful trading by the company

Director may be liable to disqualification and/or prosecution *if he or she...*

- fails to keep proper accounting records
- approves financial statements which do not show a true and fair view
- commits an indictable offence in connection with the setting up, management or liquidation of the company or with the receivership or management of its property
- is party to fraudulent trading, any other fraud in connection with the company or wrongful trading
- commits an offence under the Enterprise Act 2002 such as price-fixing or bid-rigging
- commits an offence under the Bribery Act 2010 such as the payment of a bribe by a company with the consent and connivance of the director

Forensic accountants' role

Forensic accountants may become involved in showing that specific breaches of duty occurred, in putting forward defences to alleged breaches and in the computation of the financial consequences of a breach.

An example of forensic accountants' involvement in the investigation of alleged breaches of directors' duties is a situation in which wrongful trading is alleged. In such circumstances, the director should be able to show that from the time it became (or should have become) evident that there was no reasonable prospect that the company would avoid insolvent liquidation, he or she took steps to minimise potential losses to creditors. Forensic accountants may be required to advise on the point at which it was or should have been evident that the company would become insolvent and on the extent to which the director took steps to protect the company's creditors. As part of this work they would need to examine financial information in the period preceding the company's insolvency, including bank statements, details of purchases and sales, cash received and paid, creditor balances, including new credit taken on each month, and net assets. A comparable exercise may be necessary if a company's insolvency results in charges of fraudulent trading against one or more of the directors.

In relation to the financial consequences of a breach of duty, a company may seek to recover the profit made by a director following a breach of the duty of good faith owed by the director. Forensic accountants may become involved in the computation of the amount to be recovered or in a review of the company's calculations.

Conclusions

There are many situations in which it may be alleged that a director is in breach of his or her responsibilities, often with potentially serious consequences for the company and the individual. A consideration of the issues relating to alleged breaches of duty and their financial consequences will often be enhanced by independent expert input.

To obtain further details of our activities or to benefit from the firm's experience and expertise, please contact George Sim or Rakesh Kapila.

Please note that this newsletter has been written for the general interest of readers and is intended for guidance only. It is therefore essential to take specific professional advice before taking any action.

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