Company Director Disqualification in the Criminal Courts

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Criminal courts have sweeping powers to disqualify directors arising from prosecutions for regulatory crime, with far-reaching consequences for companies and individuals. This Alerter provides an essential guide for practitioners to approaching director's disqualification orders at a time when the HSE, Environment Agency and other regulators show a growing appetite to prosecute individuals.

Disqualification: an overview

1. The Company Directors Disqualification Act 1986 ("**CDDA**") gives powers to the High Court, Crown Court and Magistrates Court to disqualify individuals from acting, directly or indirectly, as a director of a limited companies. This prohibition extends to acting as a shadow or de facto director. A director's disqualification order can have serious consequences for both the individual – who may lose their livelihood – and also for businesses who will lose strategic insight and management expertise.

2. It is a criminal offence for the director and for the body corporate that employs them, to act in breach of a disqualification order, punishable by up to 2 years imprisonment (on indictment) or a fine. If the disqualified director acts in breach of a disqualification order with the consent, connivance, or neglect of an officer of the body corporate, that officer is also guilty of an offence. The disqualified person is jointly and severally personally liable with the company for any debts incurred acting while disqualified (s.15).

The statutory position: CDDA in the Crown Court and High Court

3. The powers of the criminal courts to disqualify are provided by s.2 CDDA:

> ***2.— Disqualification on conviction of indictable offence.***
>
> *(1) The court may make a disqualification order against a person where he is convicted of an indictable offence (whether on indictment or summarily) in connection with the promotion, formation, management, liquidation or striking off of a company with the receivership of a company's property or with his being an administrative receiver of a company.*

A 'company' includes an overseas company (s.2(1A)).

4. The discretion afforded by s.2 is unfettered and broad in scope. It refers to 'management' in a broad sense and is not restricted to internal or external management of the company's affairs. Carrying on a business through a limited company is a connected with its 'management' within s.2 CDDA (*R v Georgiou* (1988) 4 B.C.C. 322, 325). Note however that the person must have been convicted: the power does not arise when the prosecution is against a company and a company alone.

5. The High Court also has power to disqualify directors under s.6 CDDA. This requires a company to have become insolvent, and the director must be 'unfit'. Per *Secretary of State for Business, Innovation and Skills v Rahman* [2017] EWHC 2468 (Ch), there should be no difference in the principles for determining the length of disqualification as between s.2 (Crown Court) and s.6 (High Court). Although criminal courts do not have to make an explicit finding of 'unfitness', recent cases have drawn on civil cases in criminal appeals and vice versa. The test then for disqualification in the Crown Court and in the High Court is thus very similar.

6. The maximum period of disqualification is 15 years (in the Crown Court) or 5 years (in the magistrates' court) (s.2(3) CDDA). In *Sevenoaks Stationers (Retail) Ltd,*

Re [1991] Ch. 164 the Court of Appeal Civil Division divided disqualification orders into three categories. This also has been adopted by the Criminal Division and divides in this way:

> *(i) The top bracket of disqualification for periods over 10 years. Reserved for particularly serious cases. These may include cases where a director who has already had one period of disqualification imposed on him falls to be disqualified yet again.*
>
> *(ii) The minimum bracket of two to five years' disqualification should be applied where, though disqualification is mandatory, the case is, relatively, not very serious.*
>
> *(iii) The middle bracket of disqualification for from six to 10 years should apply for serious cases which do not merit the top bracket.*

7. Both the Civil and Criminal Divisions of the Court of Appeal emphasise that disqualification is a preventive measure with the object of protecting the public, shareholders, creditors and companies from individuals who use or abuse their role and status as a director of a limited company to the detriment of the public, whether through dishonesty, naivety or incompetence (*R. v Anthony Glen Edwards* [1998] 2 Cr. App. R. (S.) 213, 215).

8. The High Court has been explicit that the threshold for disqualification is high and beyond simple negligence. '*To reach a finding of unfitness the court must be satisfied that the director has been guilty of a serious failure or serious failures, whether deliberately or through incompetence, to perform those duties of directors which are attendant on the privilege of trading through companies with limited liability*' (*Re Bath Glass* (1988) 4 B.C.C. 130, 133).

Disqualification for environmental and health & safety offences

9. The Sentencing Guidelines for environmental and health & safety offences both make a sentencing court consider whether to make ancillary orders, including director's disqualification orders. The growing tendency for regulators to pursue

individuals, as well as organisations, means that this power is going to become increasingly relevant.

10. Most reported cases of disqualification after criminal proceedings involve fraud committed through a company, where dishonesty and misuse of a directorship are elements of the offence. Health & safety or environmental offences typically require a lower degree of *mens rea* for the commission of the offence. This includes, for example, where a body corporate commits an offence with the consent, connivance or attributable to the neglect of the company officer, which is often sufficient for the individual to be found guilty of an offence along with their company. As such, the conviction alone of a health & safety/environmental offence and the facts leading to the conviction alone, may not by themselves provide grounds to make a disqualification order.

11. In *R v Chandler* [2016] B.C.C. 212, the Court of Appeal considered an appeal against sentence following conviction of a strict liability offence under the Consumer Protection from Unfair Trading Regulations 2008. It gave useful guidance on the level of culpability required:

> *Ordinary commercial misjudgement is in itself not sufficient to justify disqualification. In the normal case, the conduct complained of must display a lack of commercial probity, although I have no doubt in an extreme case of gross negligence or total incompetence disqualification could be appropriate.* […] [It must be shown that the director in question] *behaved in a commercially culpable manner in trading through limited companies.*

12. The appeal was allowed. The convictions were for regulatory offences of strict liability incurred as a director, rather than suggesting any personal misconduct by that director. The sentencing judge had not identified the conduct that made him unfit to be a director or heard evidence on which to make the order. No evidence of personal culpability was before the court.

13. On the other hand, if a director is aware of a breach by their company of the environmental permitting regime and this breach for personal financial gain, then this can make their position as director untenable. The leading case is *R. v McIntosh (Edward)* [2019] Env. L.R. 25, where a director of a company was disqualified following guilty pleas to various offences under the Environmental Permitting (England and Wales) Regulations 2010. The Court of Appeal commented that he should have known his company's waste storage was in breach of the Regulations, and his failure to rectify the situation had a financial motivation rather than simple incompetence or inactivity. The Court of Appeal upheld a 5-year disqualification order. It found that the director should have resigned and that he had demonstrated a lack of understanding of his duties that justified disqualification. His financial motivation was a key factor in the order being made and upheld.

14. There is a paucity of Court of Appeal authority concerning disqualification in health & safety matters. Disqualification was considered in the sentencing remarks of Mrs Justice Yip DBE in *R v Harun Rashid, Mohammed Abdul Kuddus, RS Takeaway Limited T/A The Royal Spice* (Crown Court (Manchester), 7 November 2018). The Court declined to make a disqualification order following convictions of the proprietors of a restaurant for corporate manslaughter and health & safety offences following the death of a 15-year-old girl as a result of an anaphylactic reaction to peanuts. The Court noted they were negligent restauranteurs but did not run the risk for the sake of profit. Although not made explicit, it seems that there was no misuse of limited liability, so disqualification was not appropriate.

15. This approach can be contrasted with *R v Crute (Martyn)* [2011] EWCA Crim 3233, where a director was disqualified for 7 years for continuing to offer gas installation services after de-registering his company from the register of the Council of Registered Gas Installers. The individual's management of the company had endangered life, and the disqualification was not subject to appeal. This is an important case which makes it clear that where an individual company officer's

wrongdoing goes beyond what was merely necessary to commit the offence, an HSE prosecution can put directors at risk of disqualification.

Procedure

16. A director's disqualification order is part of the sentence imposed. The criminal standard of proof applies, but in the ordinary way of sentencing hearings hearsay evidence is admissible subject to the judge's assessment of its weight. A court can only make an order when the accused has had an opportunity to consider what order is proposed, why it is proposed, the evidence supporting it, and to make representations at a hearing (see *Chandler*, above).

Resisting disqualification

17. Drawing this together, applications for director's disqualification orders are becoming more common as more individuals are prosecuted and the tariffs for regulatory crime continue to rise. The test for disqualification is similar in the criminal and civil jurisdictions and typically requires more culpability by the individual defendant than simple commission of a regulatory offence arising from management of a company. It is thus important for practitioners to consider the following factors when advising a client on the risk of such an order being made and planning a strategy to meet the application:

    - Any dishonesty, or whether there was merely incompetence or negligence in a very marked degree falling short of dishonesty;
    - Whether conduct was deliberate, dishonest or self-serving;
    - Any breaches of fiduciary or other directors' duties;
    - Personal or financial benefit from the offending;
    - Level of financial damage done/sums involved;

- Previous convictions;
- Time period over which the offence was committed, whether one-off or repeated/prolonged;
- Attempts to deceive the authorities;
- The identity of the victim.

18. Evidence of some or all of these factors must be before the sentencing judge for the prosecution to establish the basis for making the order and notice of this must be provided to Defendants and in good time.

19. In defending a potential disqualification order, remind the court that the purpose of disqualification is to prevent misuse of limited liability. A company can be run with commercial probity but still commit a regulatory offence. Defendants should emphasise any conduct that illustrates the company was not being misused as a shelter to avoid personal liability. Lack of financial gain is an important consideration, and any negligent actions should be distinguished from negligence in management.

Totality

20. A final word concerning the sentencing principle of totality. The Judicial College Compendium (Part II 7-4) makes it clear that a disqualification order is a punishment and will be considered as part of the totality of any sentence. Accordingly, the dissuasive effect of other parts of the sentence should also be considered before the order is made. In *R v Luther* [2016] EWCA Crim 988, a suspended sentence following conviction of a Transfrontier Shipment of Waste Regulations 2007 offence was sufficient to prevent the defendant conducting a business in a harmful way in future. An additional disqualification order was quashed as manifestly excessive.

21. So even if the threshold for a disqualification order is met and the prosecution have approached the procedure correctly, it is still possible to avoid or mitigate a period of disqualification on the grounds of remorse, hardship or good character, as well as any specific factors showing the behaviour will not be repeated and the public therefore do not require the protection of a disqualification order.

22. If a disqualification order is made, it will be inappropriate to combine an order for disqualification with a compensation order if the effect of the disqualification would be to deprive the offender of the means to earn money with which to pay compensation and/or a fine (*Holmes* (1992) 13 Cr. App. R.(S.) 29).

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