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AN APPRAISAL OF THE FRAMEWORK FOR SANCTIONING ERRING DIRECTORS AND OFFICERS FOR WRONGDOING DURING INSOLVENCIES IN NIGERIA AND THE UNITED KINGDOM

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INTRODUCTION

When a company is unable to meet its financial obligations to creditors on time, it is considered insolvent. Insolvency is as a state where a company's financial liabilities surpass its available resources, rendering it incapable of meeting its debts promptly. The repercussions of insolvency extend beyond the devaluation of shareholders' investments. Job losses, negative impacts on local communities, and even repercussions on the national economy are imminent. Shareholders' interests take a backseat, and the focus shifts to safeguarding the rights and interests of creditors.

In this intricate landscape, the role of directors becomes pivotal. Directors bear significant responsibilities during times of financial distress and insolvency. Their decisions can have profound implications for the company and its stakeholders, particularly creditors. The objective of insolvency legislation is to ensure fairness and protect creditors' rights. In the United Kingdom, the Insolvency Act of 1986 outlines detailed provisions, while in Nigeria, the Bankruptcy Act and the Asset Management Corporation of Nigeria (AMCON) Act of 2015 address insolvency matters.[1]

Despite differences, both jurisdictions prioritize the hierarchy of creditors in managing insolvency, reflecting a global commitment to safeguarding stakeholders' interests.

Who is a Director?

Directors are pivotal figures entrusted with the day-to-day management of a company, acting as fiduciaries accountable for the well-being of stakeholders including members, creditors, and employees. Their role is legally mandated and critical for the effective functioning of the organization.

[1] Pereowei Subai, '*Company Law in Nigeria*', (DOK Consults & Research LLP 2023) Page 356

Both in Nigeria and the United Kingdom, the legal framework clearly defines directors and delineates their responsibilities. They are not mere title-holders; rather, their significance lies in their position and the fiduciary duties they uphold towards the company and its stakeholders.

The landmark case, Re Forest Dean Coal Mining Co, emphasizes that the various titles assigned to directors, be it commercial trustees or managing partners, are superficial. What truly matters is their recognition of the responsibility inherent in managing a business for the benefit of the company and its diverse stakeholders.

Duties of a Director during Insolvency

When a company becomes insolvent, meaning it can't pay its debts as they come due, directors must shift their focus from promoting the company's success to minimizing losses for creditors. They must avoid actions that could increase debt or harm creditors further, acting with care, skill, and diligence. Timely decisive action is essential, considering the interests of all creditors, not just those with personal ties.

Directors must proactively manage the company's affairs, monitoring its financial health closely. They must decide promptly whether to continue trading or initiate an orderly wind-up if saving the company isn't feasible, aiming to minimize losses.

Before a receiver is appointed, directors act as fiduciaries for creditors, preparing a comprehensive statement of the company's affairs and being accountable for transactions under their control to the receiver.

Once winding-up proceedings begin, directors have the following additional duties:

a. Prepare a detailed statement outlining the company's financial situation, including its assets, debts, liabilities, and the names and addresses of creditors. This statement should also include information about any securities held by creditors, along with the dates they were obtained.

b. Be available to provide a detailed explanation of all transactions and funds that were under their control to the receiver.

   After the winding-up proceedings has commenced, the directors have the following duties:

   i. To deliver all company property to the liquidator, including any assets that are under their control or in their possession.

ii. Not to leave out any significant information in any statement regarding the company's affairs.

iii. Not to obstruct the production of any documents or records relevant to the company's property or affairs.

OTHER OFFICERS OF A COMPANY

Receivers/Managers

Receivers/Managers, highly skilled professionals specializing in insolvency practices, are appointed to oversee companies facing significant financial challenges. Their role extends far beyond simply liquidating assets; they are entrusted with the crucial task of managing the company's affai
rs until debts are fully settled. This appointment effectively suspends the powers of the company's directors unless formally discharged.

While receivership significantly limits the company's authority over its assets, it's essential to note that it doesn't dissolve the company's legal existence. Ownership of assets remains with the company, underscoring the importance of allowing the receiver to act in the best interests of all parties involved.

Receivers shoulder extensive fiduciary duties akin to those of directors and can face severe legal consequences for breaches. They are held to a high standard of professionalism, expected to exercise skill, care, and act as fiduciaries of the company. In the case of ex curia receivers (Receivers appointed out of Court), they serve as agents for both the appointing party and the company itself, wielding considerable authority in managing the company's affairs.

Despite their authority, the company retains the right to ensure that the receiver fulfills their obligations and safeguards assets from dissipation. Provisions that attempt to absolve receivers from breaching their duties, such as those regarding good faith and care, are rigorously scrutinized and often deemed void to prevent evasion of liability.

Liquidators

A liquidator is an individual typically appointed to supervise the winding-up proceedings of a company. The roles of a Liquidator is similar to that of the Director, however, the Liquidator assumes control upon his appointment, thereby supplanting unless sanctioned by the liquidator at a General Meeting. While the company retains legal existence until its dissolution, the company’s assets remain with the company, not the liquidator. Creditors and contributories retain rights but can't sue on behalf of the company.

The liquidator takes charge of the company's assets, pays creditors, and distributes surplus to the members of the company. Their role encompasses managing the company, settling debts, and distributing remaining surpluses.

In a compulsory winding-up, the court appoints the liquidator; whereas in a voluntary winding-up, the members of the company or its creditors appoint a Liquidator.

Although the Companies and Allied Matters Act (CAMA) doesn't define a liquidator explicitly, their duties and powers indicate their role. They must possess skills, competencies, and integrity, typically as insolvency practitioners. Recent amendments mandate insolvency practitioners as liquidators for Nigerian companies, unlike CAMA 1990.

Administrators

When a company enters administration, an administrator is assigned to oversee its operations. This individual, typically an insolvency practitioner, assumes responsibility for managing the company's affairs and assets on behalf of its creditors. Throughout their tenure, administrators serve as both representatives of the company and officers of the court, thus carrying the obligation to act in utmost good faith. Central to their role is the requirement to maintain independence and impartiality in managing the company and its assets.

Upon appointment, administrators assume control over all of the company's property, effectively supplanting the authority of its directors. Acting as the company's agent, administrators have the authority to engage in contracts with third parties. Payments due under such contracts are prioritized over the administrator's fees, expenses, and distributions to floating charge holders and unsecured creditors.

FRAMEWORK FOR SANCTIONING ERRING DIRECTORS IN NIGERIA

Directors are typically shielded from personal liability for company debts. Yet, in cases of mismanagement leading to insolvency, they may face personal responsibility. In Nigeria, the Companies and Allied Matters Act (CAMA) 2020 dictates penalties for director misconduct in insolvency. Relevant provisions follow.

Fraudulent Trading and Misapplication of Funds

During the winding-up of a company, if it's found that the company's business was conducted recklessly or with intent to defraud creditors, the Court may hold individuals involved personally responsible without limitation of liability[2].

[2] Companies and Allied Matters Act (CAMA), 2020 s 672(1)

Those knowingly participating in such conduct can face fines or imprisonment, as determined by the Court. In the case of *Re Todd Ltd*[3], a director was held liable for contributing over £70,000 to settle the company's debts due to wrongful trading.

Furthermore, during a company's winding-up process, if it's evident that a director knew or should have known before the commencement of the winding-up that the company would likely become insolvent, the Court may hold the director personally liable[4]. However, if the Court finds that the director took all necessary steps to minimize potential losses to the company's creditors, the declaration of personal liability may not be made.

More so, in the course of a company's winding-up proceedings, if it comes to light that any individuals associated with its establishment or administration have mishandled company funds or violated their fiduciary duties, the Court has the authority to investigate their conduct. Should misconduct be confirmed, the Court can mandate the return of misappropriated assets, possibly with accrued interest, or hold those responsible personally liable for their actions.

Disqualification of Directors.

During the winding-up of a company, if it's discovered that an individual is guilty of an offence for which they are liable, or has committed a fraud-related offence, the Court can issue an order disqualifying them from acting as a director for up to 10 years. This disqualification period starts either after the sentence for the offence has been served or when the fine for the offence is paid. The Court can initiate disqualification proceedings on its own or upon application, provided that the person against whom the order is sought is given 10 days' notice. Applications can be made by the official receiver, the company's liquidator, past or present members, or creditors of the company[5]. Both the official receiver and the liquidator are obligated to bring any relevant matters to the attention of the court.

FRAMEWORK FOR SANCTIONING OTHER OFFICERS IN NIGERIA

In Nigeria, officers and contributors of companies facing winding-up proceedings are subject to stringent regulations to uphold integrity and prevent fraudulent activities.

Falsification of Books:

Any officer or contributory found destroying, altering, or falsifying company books with intent to deceive or defraud faces imprisonment for up to two years or a fine determined by the court.

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[3] 1990 (BCLC)

[4] CAMA 2020 s 673

[5] CAMA 2020 s 280

Offences Antecedent to or in the Course of Winding Up:

Officers are prohibited from actions such as failing to disclose company property, withholding company books and papers, concealing assets, or fraudulently disposing of company property. Violators may face prosecution and penalties.

Fraud of Officers in Liquidation:

Officers inducing credit, transferring property, or concealing assets to defraud creditors during liquidation are liable to imprisonment for up to two years upon conviction.

Liability where proper accounts are not kept:

Officers failing to maintain proper accounts during the two years preceding winding-up may be fined as prescribed by regulations unless they can demonstrate honest actions.

Prosecution of Delinquent Officers and Members:

The court may direct the liquidator to refer cases of officer misconduct to the Attorney-General of the Federation for prosecution. All relevant parties are obliged to assist in such proceedings.

FRAMEWORK FOR SANCTIONING ERRING DIRECTORS DURING INSOLVENCY IN THE UK.

In the UK, director sanctions during insolvency are governed primarily by the Insolvency Act 1986 and the Companies Directors Disqualification Act 1986. These laws outline provisions for disqualification and potential personal liability of directors involved in managing insolvent companies. Key aspects of the law include:

Wrongful trading

Under this section, the Courts may impose personal liability on a director at the liquidator's request. Liability arises for wrongful trading if the director knew or should have known there was no reasonable prospect of the company remaining solvent and failed to mitigate potential losses to creditors[6]. In *Re Produce Marketing Consortium Ltd*[7], directors were held liable under Section 214 of the Insolvency Act, contributing £75,000 to the company's debts over a seven-year period.

[6] Insolvency Act 1986 s 214

[7] (No 2) [1989] 5 BCC 569

The Small Business, Enterprise and Employment Act 2015 reinforced wrongful trading provisions in the Insolvency Act 1986. Section 214A holds directors personally liable if they knew or should have known insolvency was inevitable and failed to minimize losses to creditors. Brooks v. Armstrong exemplifies this liability, where Mr. Armstrong, a director of Robin Hood Centre PLC, was not personally liable for wrongful trading as he took reasonable steps to mitigate losses, including seeking professional advice and restructuring. This case underscores that directors who act reasonably to mitigate losses in insolvency may avoid personal liability.

Fraudulent trading

Individuals involved in business dealings with creditors, exhibiting fraudulent intent, shall be personally liable to contribute to the company's assets. Fraudulent intent may be inferred if credit is obtained knowingly without the ability for repayment. However, evidence must substantiate findings of actual dishonesty. Upon proof, directors may face personal liability for company assets and including potential criminal charges.[8]

Recovery for misfeasance

The official receiver, liquidator, creditor, or shareholder may seek recovery of funds or damages from company officers or those involved in its management for misapplication, retention, or mishandling of company assets. This includes breaches of fiduciary duty, such as improper dividend payments, unauthorized use of funds, or illicit loans or payments to directors. This provision complements common law misfeasance rules but offers a quicker recourse for addressing such actions.[9]

Directors Disqualification

The UK has established a comprehensive directors' disqualification framework, primarily governed by the Company Directors Disqualification Act 1986 (CDDA86), regulating directors' conduct. The administrative bodies overseeing this framework are the Companies House and the Insolvency Service, empowered to initiate disqualification proceedings. Three types of disqualification exist under the CDDA86: disqualification orders, disqualification undertakings, and automatic disqualification. Disqualification orders, issued by the court or *suo motu*, prohibit individuals from acting as directors for up to 15 years. Disqualification undertakings, akin to plea bargains, allow directors to agree to refrain from directorial roles for a specified period. Automatic disqualification arises from convictions for certain indictable offenses related to company management. Grounds for disqualification encompass various offenses, including fraudulent conduct, persistent non-compliance with legislation, and unfit management practices.

[8] IA 1986 s 213
[9] Ibid s 212

Report on Directors Conduct

An insolvency practitioner is obligated to report on a director's conduct to the Secretary of State (typically, the Insolvency Service) within three months of the company entering insolvent liquidation if there are suspicions of breaches of duty resulting in creditor loss. Subsequently, the Insolvency Service can conduct investigations and pursue legal action against the directors if deemed necessary.[10]

LEGAL FRAMEWORK FOR SANCTIONING OTHER OFFICERS IN THE UK

In the United Kingdom, robust legal provisions govern the conduct of officers during company winding-up proceedings, aiming to ensure integrity and prevent fraudulent practices.

Fraud in Anticipation of Winding Up:

Officers are deemed to commit an offence if they conceal company property, debts, falsify documents, or make false entries with intent to defraud, facing imprisonment, fines, or both.

Transaction in Fraud of Creditors:

Officers engaging in actions like transferring company property or concealing assets to defraud creditors are liable to imprisonment, fines, or both.

Misconduct in Course of Winding Up:

Officers failing to disclose company property, deliver assets to the liquidator, surrender company books and papers, or report false debts during winding-up proceedings face imprisonment, fines, or both.

Falsification of Company's Books:

Officers or contributors falsifying company books, papers, or securities with fraudulent intent commit an offence, facing imprisonment, fines, or both.

Material Omissions from Statement Relating to Company's Affairs:

Officers making material omissions in statements concerning the company's affairs during winding-up proceedings are subject to imprisonment, fines, or both.

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[10] Ibid s 218(5)

False Representation to Creditors:

Officers making false representations or committing fraud to obtain creditors' consent during winding up or before face imprisonment, fines, or both.

SIMILARITIES BETWEEN THE SANCTIONING REGIME IN UK AND NIGERIA

Statutory Provisions:

Both the UK and Nigeria have legislation governing the sanctioning of erring directors and officers. In the UK, the Companies Act 2006, along with related laws like the Insolvency Act 1986 and the Company Directors Disqualification Act 1986, establish the statutory framework for director sanctions. In Nigeria, the primary legislation for director sanctions is the Companies and Allied Matters Act (CAMA) 2020.

Grounds for Sanction

In both jurisdictions, directors and officers can face sanctions for misconduct, including fraud, negligence, mismanagement, persistent breaches of the law or company's constitution, wrongful trading, and engaging in unfit conduct. The focus is on upholding corporate governance standards, ensuring accountability, and preventing actions detrimental to the company or its stakeholders.

Disqualification of Directors

Director disqualification is a prevalent sanction in both the UK and Nigeria. It entails prohibiting a director from serving in any directorial capacity within a company for a set duration. Disqualification serves to safeguard the public interest and deter unsuitable individuals from participating in company management.

Penalties and Legal Consequences

Both jurisdictions outline a range of penalties and legal repercussions for erring directors and officers. These may encompass fines, imprisonment, restitution orders, compensation claims, and covering legal costs. The severity of the penalties is determined by the nature and seriousness of the misconduct.

DIFFERENCES BETWEEN BOTH REGIMES

Specific Legislative Acts

The UK boasts a more detailed and comprehensive legislative framework for director sanctions, including the Companies Act 2006, Insolvency Act 1986, and the Company Directors Disqualification Act 1986. Conversely, in Nigeria, the primary legislation governing director sanctions is the Companies and Allied Matters Act (CAMA) 2020, lacking a separate act specifically dedicated to director disqualification.

Directors Disqualification

The UK possesses a more intricate director's disqualification framework. Amendments to the CDDA86 by the Small Business, Enterprise and Employment Act 2015 (SBEEA15) bolstered this framework by introducing additional grounds for disqualification, such as convictions outside the UK and instructing unfit directors. SBEEA15 also established provisions for directorial personal liability to creditors in insolvency cases and allowed courts to issue compensation orders against disqualified directors. Additionally, the UK incorporates director undertakings, where erring directors refrain from acting for a designated period. In contrast, Nigeria's director disqualification framework under the Companies and Allied Matters Act 1990 (CAMA90) is less intricate.

Regulatory Authorities:

Enforcement of sanctions on erring directors varies between the UK and Nigeria. In the UK, the Insolvency Service and the Financial Conduct Authority (FCA), alongside the courts, are pivotal in this regard. Conversely, in Nigeria, the Corporate Affairs Commission (CAC) assumes a central role, backed by the courts.

RECOMMENDATIONS FOR NIGERIA

To enhance corporate governance, it is recommended that regulatory bodies, notably the Corporate Affairs Commission (CAC), receive augmented authority and resources to thoroughly investigate director misconduct, enabling them to initiate inquiries, compile evidence, and impose disqualification penalties where warranted. Collaboration among regulatory entities, law enforcement, and the judiciary should be strengthened to ensure effective enforcement.

Moreover, the current disqualification criteria within the Companies and Allied Matters Act (CAMA) should be expanded to encompass a broader spectrum of misconduct, including persistent breaches of laws or company regulations, fraud, mismanagement, and negligence, thereby promoting heightened corporate governance standards and addressing various forms of directorial misconduct.

Conclusively, introducing a centralized disqualification register would provide transparency, allowing companies, creditors, and stakeholders to assess the suitability of directors. Furthermore, streamlining legal processes, facilitated by specialized commercial courts, clear timelines, and alternative dispute resolution mechanisms, would expedite proceedings involving erring directors, mitigating prolonged litigation and ensuring swift resolution of disputes.