

Chapter 12

Vacation of Office and Disqualification

Here, basic guidance to the end-of-chapter questions will be provided.

1. Define the following terms:

- retirement by rotation;
- special notice;
- weighted voting clause;
- succession planning;
- disqualification undertaking.

Term	Definition
retirement by rotation	A system under which directors are periodically required to step down from office and, if they so wish, can then seek re-election
special notice	Certain resolutions require the provision of special notice, namely 28 clear days
weighted voting clause	A clause, usually found in the company's articles, which provides that, in specified circumstances, the voting rights of specified members will be increased
succession planning	A system to identify and put in place replacement directors for those directors who are departing
disqualification undertaking	An undertaking, which is accepted by the Secretary of State, from a person that they will not act as a director for a specified period

2. State whether each of the following statements is true or false and, if false, explain why:

- a company must accept a director's resignation;
- a s 168 resolution can be passed at a meeting or, if the company is private, via a written resolution;
- the CA 2006 requires that a director of a public companies must retire at least every three years, and may then seek re-election;
- a director disqualified under s 6 of the CDDA 1986 must be disqualified for at least two years;
- a director can only be disqualified for committing certain offences, but only if those offences were committed in the UK;
- a director can only be disqualified by court order;
- a disqualified director can be required to pay compensation to a creditor who has suffered loss due to the director's conduct.

- **A company must accept a director's resignation:** This statement is true.
- **A s 168 resolution can be passed at a meeting or, if the company is private, via a written resolution:** This statement is false. A s 168 resolution must be passed at a meeting and the written resolution procedure cannot be used.

- **The CA 2006 requires that a director of a public companies must retire at least every three years, and may then seek re-election:** This statement is false. The CA 206 does not require retirement by rotation.
- **A director disqualified under s 6 of the CDDA 1986 must be disqualified for at least two years:** This statement is true.
- **A director can only be disqualified for committing certain offences, but only if those offences were committed in the UK:** This statement is false. Section 5A of the Company Directors Disqualification Act 1986 provides for disqualification in relation of certain offences committed overseas.
- **A director can only be disqualified by court order:** This statement is false. A director can also be disqualified by a disqualification undertaking.
- **A disqualified director can be required to pay compensation to a creditor who has suffered loss due to the director's conduct:** This statement is false. Whilst a disqualified director can be required to pay compensation, the payment is made to either (i) the Secretary of State for the benefit of the creditors, or; (ii) to the assets of the company.

3. 'The reforms made to the Company Directors Disqualification Act 1986 by the Small Business, Enterprise and Employment Act 2015 are largely superficial, and will do little to substantively improve the effectiveness of the disqualification regime.' Do you agree with this quote? Provide reasons for your answers.

Introduction

- Every essay should begin with a succinct introduction that demonstrates that you understand the essay question. Briefly explain what the essay is about and set out what the essay will discuss and how it will be structured.
- This essay requires you to discuss the reforms made to the disqualification regime by the Small Business, enterprise and Employment Act 2015, of which three are notable.

New grounds for disqualification

- The 2015 Act has added two new grounds for disqualification.

Conviction of certain offences abroad

- It was always incongruous that a person could be disqualified for the commission of certain UK offences, but could not be disqualified in they convicted offences overseas.
- This has now been remedied by a newly-inserted s 5A of the CDDA 1986 which allows for a person to be disqualified if they have been convicted of a relevant foreign offence.
- In addition, misconduct committed overseas is a factor to be taken account when determining whether to disqualify in all disqualification cases.

Persons instructing directors

- It used to be the case that only the director who committed the wrongdoing could be disqualified. Persons whose instructions of influence resulted in the director being disqualified could not be disqualified.
- This has been remedied by the insertion of ss 8ZA-ZE of the CDDA 1986 which allows for the disqualification of a person who directed or instructed a director.

Determination of unfitness

- The 2015 Act amended the matters to be taken into account when determining unfitness. The reforms principally provide that the courts should take into account whether the person's conduct in relation to an overseas company makes him unfair to be involved in management, or whether a person was responsible for an overseas company becoming insolvent.

Compensation orders and undertakings

- Disqualification does not really help those who have suffered loss due to the wrongdoing of the disqualified director.
- Accordingly, the 2015 Act amended the CDDA 1986 to provide for compensation orders and undertakings, which require the disqualified person to pay a specified amount to either (i) the Secretary of State for the benefit of the company's creditors, or; (ii) as a contribution to the assets of the company (ss 15A-15B of the CDDA 1986).
- These new powers have been used sparsely. Indeed, to date only one compensation order has been passed and no compensation undertakings have been accepted.

Conclusion

- Every essay should end with a conclusion. Briefly summarise the main points/arguments and, if possible, come to a conclusion regarding the essay topic (i.e. which of the opposing views has the stronger arguments).

4. You are the company secretary for Dragon Tools Ltd ('DT'). The company has three directors (Walter, Yvonne, and Ahmed), each of whom owns 10% of the company's shares. Upon incorporation, DT adopted the model articles subject to a supplementary article (art 3(2)) which states that each director is entitled to be a director for life and is to receive £20,000 remuneration per year. The directors also have service contracts for five years under which they each receive remuneration of £50,000 per year. These contracts came into effect, without the other knowledge of the shareholders, when the directors were appointed in 2016.

A number of the non-director shareholders have become dissatisfied with the way that the company is being run. They are particularly unhappy with Walter's continued employment with the company and membership of the board of directors, as he rarely attends board meetings and appears to have no interest at all in being involved in the company's management. Six of these shareholders want Walter to be removed from office.

These members seek your advice as to whether they can remove Walter from the board and terminate his service contract. They also wish to know if they can remove art 3(2) from the articles.

- There are a number of issues to consider in this problem question. The removal of a director often overlaps with other company law topics, as seen below.

The validity of art 3(2)

- If you have a problem question with a newly inserted or amended article provision, one issue that is likely to be relevant to the question is whether that provision is valid. The alteration of the articles is discussed at 5.3.3. Note if any statutory restrictions apply or whether the amendment is bona fide for the benefit of the company.
- Here, there are two parts of art 3(2) that require discussion. The first part states that each director is entitled to be director for life. This provision cannot be enforced as it effectively prevents the director from being removed, and the right to remove a director under s 16 of the CA 2006 cannot be taken away from the members.
- The second part provides that each director is to receive £20,000 remuneration per year. It is permissible to state a director's remuneration in the articles, but most directors choose not to as the articles could be amended against their wishes (whereas a service contract cannot).

The directors' service contracts

- The directors have five-year service contracts. Section 188 of the CA 2006 (discussed at 11.4.1) provides that a director cannot have a guaranteed term of employment of more than two years unless it has been approved in advance by a resolution of the members.
- Here, we are told that the other shareholders have not approved the contracts and so s 188 has been breached. The consequences of this will be that the five-year term will be void and the contracts will be deemed to contain a term allowing the company to terminate the contracts by providing reasonable notice (s 189).

The removal of Walter

- The non-director shareholders wish to remove Walter from office. Section 168 of the CA 2006 allows the members to remove a director by passing an ordinary resolution. The issue that arises is that we do not know what percentage of DT's shares these six shareholders control. If they do not have sufficient votes to pass an ordinary resolution, there would be little point in going through the s 168 process.
- In order to effectively remove Walter, the s 168 process must be followed exactly. As a s 169 resolution must be tabled at a meeting (the written resolution process cannot be used), a meeting will need to be called and sufficient notice provided. The directors will be unlikely to call a meeting to have Walter removed, but the members do have the power to make the directors call a meeting (discussed at 14.3.1) as long as certain

conditions can be met. If these conditions cannot be met, the meeting will not be called.

- Alternatively, if a general meeting is upcoming, the members could seek to take a s 168 resolution at that meeting.
- If the members do have the power to call a meeting, they must ensure that adequate notice of the meeting is provided. The normal notice period for a general meeting of a private company is 14 clear days, but a s 168 resolution requires special notice, namely 28 clear days.
- At the meeting, Walter must be given the right to be heard and may also make written representations. If the six non-director shareholders have the votes to pass an ordinary resolution, Walter will be removed. Note, however, that this will not deprive Walter of any compensation he may be entitled to as a result of the termination (s 168(5)(a)).

The removal of art 3(2)

- The articles can be amended by passing a special resolution (s 21(1)). Therefore, art 3(2) can indeed be removed. However, we know that the three directors each hold 10% of the company's shares, meaning that they would likely be able to defeat any resolution that proposed to remove art 3(2).