

## Business law untangled podcast

### Episode 1: How to deal with the end of pandemic-related financial support for businesses

<b>Stephen Downie</b>	<p>Okay, I have just heard “action” so I’m starting. You are listening to the first of a series of podcasts on behalf of Francis Wilks &amp; Jones. You are listening to Stephen Downie. I am a partner at Francis Wilks &amp; Jones. I am sat here with my colleague Maria Koureas-Jones of Francis Wilks &amp; Jones so hopefully you will listen to her in a minute and be enthralled by what she has got to say.</p> <p>Good morning Maria.</p>
<b>Maria Koureas-Jones</b>	<p>Good morning.</p>
<b>Stephen Downie</b>	<p>This podcast and the following podcasts will discuss the issues affecting companies post-Covid-19.</p> <p>We like to be a bit more creative with our podcasts. Hopefully you won’t find this too boring or monotonous - I will try and keep it livened up.</p> <p>We are going to give a general overview of what’s happening with companies and businesses, particularly with regard to directors and their personal risk over a series of podcasts to come.</p> <p>My background is that I became an accountant followed by a lawyer and I have worked with the Insolvency Service, with accountants. I have brought proceedings on behalf of the Secretary of State for a good five-plus years and, for the past 10 years, I have been helping directors. I have a detailed knowledge of all aspects of the type of problems that directors face but the most important thing at the moment of course is our recent pandemic and its effect on business.</p> <p>I will hand over to Maria to discuss some of the statistics and the problem the government faces as a result of this.</p>
<b>Maria Koureas-Jones</b>	<p>We have had unprecedented times haven’t we over the last year and some of the stats that are available are fairly staggering. We are expecting an increase in insolvencies in Q3 and Q4.</p> <p>Why is that? Well, some of the stats will help us in terms of context. We know that, as of June 2021, we had nearly two million still on furlough so the government was still massively supporting businesses financially. We had unprecedented financial support which has obviously been paid for from the government purse.</p> <p>We also know that there has been a huge amount of fraud during this period. The application process, for example, for bounce back loans and CIBLs was very streamlined but very quickly produced and contained flaws and it is estimated that the cost to the taxpayer is some £29 billion.</p> <p>So the government at the moment is having to look at how is that money going to</p>

	be recouped, particularly in circumstances where we think (and the government has estimated that) 35-60% of all the CIBLs and the bounce back loans won't be repaid.
<b>Stephen Downie</b>	So that's a good £15 million-plus of the £27-£29 million lent out that is unlikely to come back, isn't it?
<b>Maria Koureas-Jones</b>	The £27 billion is just the cost from fraud and I don't know the overall figure that has been loaned, but of the overall figure that has been loaned 35-60% of that is estimated to be lost.
<b>Stephen Downie</b>	Oh wow.
<b>Maria Koureas-Jones</b>	So huge sums that HMRC, liquidators, administrators and the Insolvency Service are all going to be looking to take action in relation to and certainly we have seen an increase across the very experienced team here who are regularly assisting directors, companies and insolvency practitioners, an increase in claims flowing from the likes of CIBLs, bounce-back loans, fraud and various other issues.
<b>Stephen Downie</b>	And we are seeking quite a few of these coming in in terms of the sort of work we deal with advising directors. There is certainly a noticeable change, it hasn't been faded it's been a complete change to Covid-19 based actions threatened or brought against directors.
<b>Maria Koureas-Jones</b>	<p>Absolutely.</p> <p>One of the things we are regularly seeing at the moment - and this podcast is going out to accountants so they will be feeling the regular contact in relation to this - as well is director loan accounts and directors who have quite comfortably taken payment through director loan accounts over the last few years in an unproblematic fashion have been faced with the issue where a company has gone into an insolvency process - through no fault of their own, whether it is because of Covid or supply chain issues or staffing issues whatever it might be - and they are faced with a rather large debt owed by them personally and their families of course because it affects their family home to an administrator or liquidator in having to repay that. That is a stressful situation for directors and we are regularly helping those directors navigate that stressful scenario and try to figure out the best approach to adopt.</p>
<b>Stephen Downie</b>	A typical scenario we are seeing is that the bounce back loan has come into a company and then directors have used it to pay their personal financial needs, paid it out. That all seemed sensible at the time, the business has to survive but the directors also and their families have to survive, but the problem is now of course is that they are having to account for such losses arising.
<b>Maria Koureas-Jones</b>	<p>And of course a liquidator or administrator who is looking at that conduct a year to two years ago is thinking with the benefit of hindsight, so he wasn't aware of the fact that the director couldn't pay their mortgage and wasn't aware of the stresses that the business was under. And, of course, when we are all faced with a stressful situation, we generally don't record keep.</p> <p>We all know that those records are fundamental when you are faced with a claim by a liquidator or administrator because you need to be able to point to something which justifies the commercial decision that was taken at the time.</p> <p>So we have seen and continue to see an increase in claims against directors which allege that the directors have breached their duties to the company, that they have failed to act in the best interest of the company, either, for example, because</p>

	they have taken money out of the company and paid for their mortgage or they have taken large director loan accounts without the ability to repay.
<b>Stephen Downie</b>	<p>So, what are the risks to directors?</p> <p>The problem with somebody pursuing you as a director they always pursue you on the basis of a perfect world scenario. Courts will look at any decisions made by directors with a retrospective very clean academic view whereas in reality directors are in the middle of this quagmire with suppliers and creditors demanding payment, staff demanding their wages, people complaining at x, y and z. Not all businesses are making millions and millions, particularly during the pandemic and the problem happens to be that directors exacerbate these issues by sticking their head in the sand.</p> <p>The characteristic of a failed company is where a director has not sought advice earlier and just tried to deal with things themselves and this happens after the company has failed and when they are trying to defend their home and their family from a threat of taking away the matrimonial home or all assets that they have where liquidators come after them, the Insolvency Service comes after them and HMRC chases them down. So, you know, the one thing (and I would say this as a lawyer!) I would say is take advice early. But obviously the reason for that is because you may think that a lawyer or an accountant is expensive but it's nothing like as expensive as it is going to be for your life if you try and deal with it yourself without knowledge of the processes and protocols and without having an understanding - even a basic understanding - of your options.</p> <p>Ultimately, a lot of companies have been relying on grants and loans for the past 18 months. Some companies have done well - the online companies have done well and the bigger entities. But, for the usual SME who relies on footfall or relies on a standard sort of commercial marketing approach which obviously has changed as a result of recent times, then they have been very dependent on grants and loans.</p>
<b>Maria Koureas-Jones</b>	Steve, is it fair to say that you have had recently some directors come to you or to the team who have left things particularly late and in a state where actually it makes it very difficult both to reduce the number that is going to be payable as a result of whatever circumstances have caused the claim, but also makes it really difficult for us to reduce the stress levels.
<b>Stephen Downie</b>	<p>Yes, absolutely.</p> <p>A typical scenario we see links to director loan accounts they are being pursued for repayment of the loan. We had a director come to us who had been running the claim brought against him by a liquidator for the last couple of years, trying to deal with it himself and we were a week away from trial, so we had to go running around trying to get the trial dealt with and trying to damage limit his situation. It cost a huge amount of money which would have been avoided if he had actually sought advice a couple of years ago.</p>
<b>Maria Koureas-Jones</b>	<p>I think often admissions are made during that two-year period which then massively reduce the ability to drive down the settlement cost.</p> <p>So, I think the importance, as you said earlier, although a director need to pay a few thousand on taking advice actually, had they done, they would have materially reduced the settlement sum by far more than that money.</p>
<b>Stephen Downie</b>	Or they might have avoided it at all. In our team we are quite creative with our

	<p>defences, there are a lot of defences for directors available that people really don't know about.</p> <p>I have had claims where they have brought the claim against the director not realising that they had the wrong company.</p> <p>It is about eye for detail and I think taking advice early filters out anything which could save you and, if you still are in trouble, then you know you could look at damage limitation. As you said Maria, settlement is a damage limitation process but sometimes you have a full defence.</p> <p>I would always encourage people to go and seek advice first.</p> <p>What else is going to happen in the new economy or the post-Covid economy? What is HMRC's attitude going to be? Are they going to start presenting winding up petitions against every company? There have been 18 months where practically no winding up petitions have been presented. Has it built up? Would it lead to a huge avalanche through the courts. The courts are struggling as it is notwithstanding the Covid-19 restrictions and government's policy on still limiting the amount of employees that go to offices.</p> <p>There is also the issue that if you have a huge amount of petition, how does a court possibly deal with it? There is a balance that HMRC has between the public interest in prosecuting people and trying to run down companies when Rishi Sunak has of course spent the last 18 months trying to protect them.</p>
<b>Maria Koureas-Jones</b>	<p>So we know that, from 1 October, the stay that existed through the Covid pandemic on winding up petitions and has given companies some breathing space during the Covid pandemic was lifted and so, from 1 October, winding up petitions could commence again, albeit there is a £10,000 limit. We are expecting that some winding up petitions will be presented on the back of aged debt.</p> <p>Steve, we have discussed it and we think it is unlikely that there will be a tsunami, particularly given that HMRC were predominantly the main petitioning creditor pre-Covid and we think that it unlikely that the government is going to want to have supported businesses for the last year and then, in the next breath, wind up those same entities. But, as a result of that change and that stay in petitions being lifted, what do you think the risks are to directors and their businesses?</p>
<b>Stephen Downie</b>	<p>The problem with directors, unlike us guys who are involved in this all the time, the directors often don't really know they are involved until it happens. The 'head in the sand approach' can sometimes lead to the insolvency of a company - not dealing with things straightaway, not seeking advice. This problem resurrects itself because the directors either try and deal with claims that may be brought against them by themselves or they just don't respond and leave it until they are on the eve of a trial.</p> <p>You know directors have various duties, fiduciary and non-fiduciary, within a company and if they don't comply with those duties, sometimes which can expand to the public interest and mis-selling then they are pretty much at risk.</p> <p>So, what's been happening during the last 18 months is that we have had this temporary welfare state for businesses where lots of businesses have been relying on grants and loans.</p> <p>Has there been fraud in applying for a grant? Have loans been mis-applied in the wrong way?</p>

	<p>I know from the bounce back loan application form there is no prescribed reason or purpose you should use it for but unfortunately with director misconduct you can be pursued for not using the bounce back loan in the correct manner. You have to be careful when you are taking these loans out.</p> <p>The most important thing I think Maria is what is HMRC's view is going to be. Ultimately, they present most winding up petitions and you can't stop unsecured conventional creditors presenting winding up petitions. But is HMRC going to similarly pursue directors and companies on the basis that they have been funding their continued existence for the last 18 months? We have discussed we think it is probably unlikely, isn't it?</p>
<b>Maria Koureas-Jones</b>	<p>So we think that HMRC is probably going to be more prepared to enter into extended time-to-pay arrangements and you have seen that on some of the cases that you have been working on, that HMRC is more prepared to agree a longer duration of time for a business to repay aged debt.</p>
<b>Stephen Downie</b>	<p>Yes A few years ago, you were lucky to get more than 12 months but we are seeing 5/6 years on time-to-pay arrangements so there is an out there and HMRC is prepared to be flexible. They have got to balance the public interest risk of government between recovering businesses and damaging businesses.</p> <p>Obviously, the fraudsters and the wrongdoers do need to be captured, they do need to be held accountable for misusing these schemes during Covid-19 but where we find the most problems is that grey area in between and, as I said earlier, directors often try and deal with things themselves or stick their heads in the sand and they are what we call the 'low hanging fruit' that the government likes to target because they are able to get what they want with relatively low use of resources.</p>
<b>Maria Koureas-Jones</b>	<p>And often they can't remember why they made a decision it is just they haven't produced the records to justify the decision at the time and I know we have seen in the last month the Insolvency Service actually looking to disqualify, purely on the grounds of failing to complete company records.</p>
<b>Stephen Downie</b>	<p>Yeah, I mean we are getting into a whole plethora of different types of director misconduct that we will deal with in future podcasts.</p>
<b>Maria Koureas-Jones</b>	<p>So the possible outcome for companies then. We thought and discussed HMRC creditors taking winding up action. The other options available are of course looking at an insolvency process, so a restructuring of some sort and we have seen an increase in CVAs haven't we over the last year, big names like Wasabi, Pizza Express, Itsu, Café Nero, lots of well-known brands that have entered into an insolvency process.</p> <p>Do you think that we are likely to see that continue into other sectors over the next year or two?</p>
<b>Stephen Downie</b>	<p>Well a CVA or a company voluntary arrangement is a really good theoretical insolvency model. It enables companies to come to an agreement with creditors, agree to pay them back a specific amount over a period of time and enables a business to survive and that's what all those high street names you just referred to have done. But whether a business can coming out of Covid, continue to maintain its trading liabilities, continue to generate sales - we know that the high street and erm sales are not up to the pre-Covid levels yet - whilst also trying to service this debt, that is the question whether that's possible. There may be finance</p>

	opportunities out there or new types of funding which enables this to happen. Certainly the recovery loan does that.
<b>Maria Koureas-Jones</b>	<p>You mentioned earlier that there had been a suspension of wrongful trading. You are absolutely right when you say that directors are faced with the circumstances where they are trading businesses where they don't know that they are going to be able to fund the wage bill or the expenses. Directors do of course, in those circumstances, need to be very alive to the risks of a claim for breach of fiduciary duty a claim against them personally in their own homes for not acting in the company's best interest.</p> <p>I think taking advice at an early stage, particularly where the company is facing tight cashflow, is going to be really important, as is documenting why those decisions are made.</p>
<b>Stephen Downie</b>	Yes, absolutely and ultimately, although Rishi Sunak protected directors to a certain degree by suspending any claims for wrongful trading during the last 18 months, have you seen many wrongful trading claims pre-Covid?
<b>Maria Koureas-Jones</b>	Very few.
<b>Stephen Downie</b>	Yeah it just doesn't happen that often a breach of fiduciary duty claim is almost always the most common type of claim brought against directors together with various other claims under either the Insolvency Act or under the Companies Act or generally.
<b>Maria Koureas-Jones</b>	<p>Absolutely. The other potential exposure for companies at the moment of course as they are coming out of these protections is just general debt recovery claims so creditors pursuing action.</p> <p>Creditors have been relatively relaxed in agreeing time to pay and I am not talking about HMRC now but other secured creditors. I suspect that patience will wear thin over the coming year and that we might see an increase in County Court judgments and enforcement through high court bailiffs or third party debt orders or charge orders or whatever it might be.</p>
<b>Stephen Downie</b>	<p>Yes, we do a lot of debt recovery for businesses and the issue now is that petitions can only be presented for debts above £10,000 whereas before Covid the debt had to be over £750. A popular way of dealing with a claim for a debt was to petition for the company to be wound up and then leave it in the hands of a liquidator to get your money back.</p> <p>What are the options?</p>
<b>Maria Koureas-Jones</b>	In terms of the debt recovery options?
<b>Stephen Downie</b>	Yes.
<b>Maria Koureas-Jones</b>	Well bankruptcy petitions are obviously still fine against a sole trader for example but otherwise it is going to be a case of pushing Part 7 claims through the courts and looking to enforce those.
<b>Stephen Downie</b>	Yeah and I think getting county court judgments against individuals and businesses is not really that desirable. Really, what you want to do rather than just getting a judgment, you want to get paid so the ideal scenario is you need to know if the person has got assets.

	<p>The same thing happens with directors who are subject to a claim for misfeasance or anything they have done wrong. If you are a director sitting at home thinking I haven't got any money, well look around at the bricks and mortar surrounding you - they will take your family home from you.</p>
<b>Maria Koureas-Jones</b>	<p>The old adage 'don't throw good money after bad' is apt - if you are going to pursue litigation let someone know that they have got the ability to pay back any judgment awarded.</p>
<b>Stephen Downie</b>	<p>Yeas, absolutely.</p>
<b>Maria Koureas-Jones</b>	<p>What do you expect to be the outcome for directors over the next year? What do you forecast we are going to see in terms of claims?</p>
<b>Stephen Downie</b>	<p>Well we are already starting to see them come through.</p> <p>The Insolvency Service has, over the last six months, become remarkably active and one of the main grounds of misconduct – just for listeners, the Insolvency Service is an executive agency of the Secretary of State for business. They bring director disqualification claims against directors of companies that have traditionally fallen in to insolvency - and what I have seen happen quite a lot lately is that they are seeking or investigating director disqualification claims on the basis of the wrongful use of loans made over the Covid-19 pandemic.</p> <p>These loans were freely handed out and directors were protected by Rishi Sunak from wrongful trading allegations but now they are turning round saying, what did you use the loan for and was that appropriate?</p>
<b>Maria Koureas-Jones</b>	<p>Legislation is currently before parliament with a view to actually extending the insolvency service's options in terms of director disqualification to pursue a director of a dissolved company, which hasn't been an option for them before.</p> <p>We should see that legislation pass within the next few weeks so you're expecting obviously to see an increase in those as well I suspect.</p>
<b>Stephen Downie</b>	<p>Yes, it is at the third reading at the moment so in the next few weeks or maybe the couple of months.</p> <p>On 29 December 2020 the <i>FT</i> made this grand announcement about how Covid-19 had not affected the UK's business because of the incredible growth in the number of company registrations. That happened to occur at the same time as all the loans coming out.</p> <p>The bounce back loan followed the CBILs because it was an easier loan to apply for and the outcome of that is that the loan was drawn down, pocketed by the director, used potentially to pay their family needs and living expenses.</p> <p>I am not saying that these were criminal proceeds - they were using it maybe for very reasonable reasons but you can't loan money to pay your living expenses through a company and then what has happened subsequently is that they have then dissolved the company. There are no other creditors chasing them down, nobody has noticed it and they have just had it struck off the Companies Register and thought well, that was a nice £30,000, £40,000 or £50,000 for free.</p>
<b>Maria Koureas-Jones</b>	<p>And if the Insolvency Service doesn't pursue these claims against directors of either trading companies or dissolved companies, the other of course potential</p>

	<p>claims are liquidator administrators who are taking office maybe 1, 2, 3, 4 years after Covid and they are looking at money that exited a company bank account into a director's personal account or mortgage account and likewise they are going to be analysing whether that was the right thing to do at the time or whether there was a personal claim as a result of that.</p>
<b>Stephen Downie</b>	<p>Absolutely. The interesting thing with the new legislation coming out is that it's not always going to be the case that somebody appoints a liquidator to a company, particularly if the only asset in the company is a potential claim on an unknown basis because they won't have the knowledge then.</p> <p>A potential claim against a director for repayment of the bounce back loan, I think probably there won't be so many of those claims around. So what the government has done is they have brought these disqualification claims to encompass, not just the insolvent companies, but also the dissolved companies. They have enabled, under this new legislation, directors of dissolved companies to be disqualified.</p> <p>A little-known power out there is the compensation order which came out in 2015. Vince Cable was seeking with the small business enterprise and regulatory format, to make business more transparent, show who owned businesses etc. etc. One of the provisions of that was that if you were disqualified then there is almost a mandatory strict liability for the losses suffered.</p> <p>There are three grounds for those losses and one of them is a loss to a specific creditor which, in this case is HMRC.</p> <p>If they come after you and you are a director of a dissolved company and they offer to disqualify you, you can voluntarily agree to that. If you take that undertaking to be disqualified, you avoid legal costs at that point but, as we said earlier, this doesn't solve the problem because they will then later seek a compensation order against you and by then it's too late. We will discuss that in future podcasts.</p>
<b>Maria Koureas-Jones</b>	<p>One of the other things we will be discussing in future podcasts is, where you do give a director's undertaking, actually an application that can be made to court promptly - it does need to be made promptly - for permission to act as a director of another company and the team are regularly helping directors with that.</p>
<b>Stephen Downie</b>	<p>Yeah we have got to date a 100% record at these applications for leave. You sign a disqualification undertaking and, since the company was insolvent or dissolved etc, you have grown a maturing or potentially successful business then what you can do is apply to the court for leave because the last thing the justice system wants is disqualifying a director which may lead to another business or a current active live business failing as well because of the loss of that director and the effect on suppliers, staff etc. So there are options out there, absolutely Maria.</p>
<b>Maria Koureas-Jones</b>	<p>We have covered off a huge amount in terms of the potential claims that we are expecting but we don't think it is all doom and gloom for the economy.</p> <p>We think that directors can be optimistic. There are certainly lots of growth areas in the economy that we are seeing – safety equipment, IT - we have obviously seen a massive growth for IT over the last year as a result of necessity really.</p> <p>Insolvency brings opportunity, the option to restructure and utilise previous business knowledge and lessons learned with a view to then perhaps restructuring and using that for a new business. So we don't think it is all doom and gloom.</p>



<b>Stephen Downie</b>	<p>No. There was an all parliamentary group report recently about businesses being enabled by the insolvency process to survive but one thing that's very important is that pre-packaging a sale of your business out of administration is a key way to enable a business to.</p> <p>It is certainly the case that you will protect the suppliers, maybe not in respect of outstanding debts, but you could protect the employees, you will enable the business to continue going. This is all of what we want for the economy so, you know, insolvency is not the death knell it may sound. It is just a restructuring process.</p>
<b>Maria Koureas-Jones</b>	<p>It is just about taking advice early to understand whether that's the best option, best process for all involved and that might be both the directors but also for creditors.</p> <p>So, Steve what are we going to talk about in our next podcast?</p>
<b>Stephen Downie</b>	<p>Well in the next podcast we are going to address directors loan accounts.</p> <p>We will have a series of podcasts and I think we will cover a few other topics, such as the director disqualification and compensation order issue with regard to dissolved companies. We may also have a podcast dealing with HMRC enforcement powers against directors which is an important one. I deal with a few clients facing these and they can be quite difficult. HMRC have direct enforcement powers against directors of companies that go into insolvency and certainly we will be looking at those as well.</p>
<b>Maria Koureas-Jones</b>	<p>Well thanks for listening and we look forward to speaking to you again on the next podcast.</p>
<b>Stephen Downie</b>	<p>And it is goodbye from me.</p>
<b>Maria Koureas-Jones</b>	<p>And goodbye from him.</p>