Something Old, Something New, Something Borrowed, Something Blue?—a consideration of the proposed additions to the Companies Act 1993 to restrain the use of phoenix companies.

The Insolvency Law Reform Bill 2005 recently passed by the New Zealand House of Representatives significantly reforms the insolvency provisions of the Companies Act 1993. Although the new voluntary administration regime has dominated the corporate insolvency law reform debate both outside and within the legislative chamber, the Bill also includes certain provisions targeted at reducing the on-going abuse by directors of the corporate form through the use of phoenix companies. Phoenix companies or phoenix syndrome is the *old* practice of recycling a company's assets through the incorporation of a new company with an identical or almost identical name to the existing (often insolvent or almost insolvent) company in order to capitalise on any goodwill in the existing company's name.

The *new* New Zealand provisions are effectively *borrowed* from sections 216 and 217 of the UK Insolvency Act 1986 and associated regulations. The paper reviews the developing UK jurisprudence on these sections and suggests the likely approach that New Zealand courts will adopt. It also suggests that based on the UK experience, these reforms are unlikely to achieve the intended objectives.

Trish Keeper
School of Accounting and Commercial Law
Victoria University of Wellington
Wellington
New Zealand

Working Paper
Please Do Not Quote Without The Permission of the Author

I BACKGROUND

Among the raft of insolvency law reforms passed in November 2006 by the New Zealand House of Representatives[1] were a number of provisions to supplement and amend the corporate insolvency provisions of the *Companies Act 1993*[2] ("the Act"). This paper focuses principally on new sections 386A – 386F[3] and new section 380(2)[4] of the Act that were introduced to prevent inappropriate use of phoenix companies. Abuse of the corporate form through the mechanism of phoenix companies is not unique to the New Zealand situation. Indeed in 1982, in an often quoted description of the practice in the United Kingdom, the Cork Committee Report on Insolvency Law and Practice[5] commented that the attention of the Committee had been:

> drawn the widespread dissatisfaction at the ease with a person trading through the medium of one or more companies with limited liability can allow such a company to become insolvent, form a new company, and then carry on trading much as before, leaving behind him a trail of unpaid creditors, and it was pointed out that the dissatisfaction was greatest where the director of an insolvent company had set up business again using a similar name for the new company, and trades with assets purchased at a discount from the liquidator of the old company.[6]

The directors of the new company (known as a phoenix company) use to their advantage that "in law the phoenix company will be treated as an independent entity and as such will be devoid of any responsibility or accountability in respect of the debts of the liquidating company from which it is spawned."[7]

In 1999, the Ministry of Economic Development ('MED') signalled that as part of Tier One of a MED review of both personal and corporate insolvency, the issue of phoenix companies would be targeted. Although prior to this date, there had been anecdotal evidence of phoenix company abuse, the 1998 high profile corporate failure of New Zealand Stevedoring Ltd, had focused attention on the practice. To initiate discussion on the prevalence of, and reform options for, phoenix arrangement abuse, the MED published a Discussion Document in January 2001 asking for submissions from relevant stakeholders.[8]

A Cabinet Paper released by the Minister of Commerce in December 2003 summarised submissions received in response to the Discussion Document and highighted that phoenix company arrangements may also prejudicially affect the creditors of the phoenix company. When a phoenix company adopts a similar name to a failed company in an attempt to benefit from any remaining goodwill in the name of the failed company, creditors may extend credit to the new company without being fully informed of the risk. For those responsible for the failure of the old company, are now

---

[1] Although the Companies Amendment Act 2006(NZ) received Royal Assent in 7 November 2006, it is not yet in force.

[2] The Insolvency Law Reform Bill 2005 (14-2) was by Supplementary Order Paper 2006, No 61,divided into the Companies Amendment Act 2006(NZ) and the Insolvency Act 2006 (NZ).

[3] Companies Amendment Act 2006, s 35 (NZ).

[4] Companies Amendment Act 2006, s 33 (NZ).

[5] United Kingdom, *Report of the Insolvency Law Review Committee*, Cmnd 8558 (1982).

[6] Ibid para 1813.

[7] Stephen Griffin,'Extinguishing the Flames of the Phoenix Company' (2002) 55 *Current Legal Problems* 377, 378.

[8] Ministry of Economic Development, 'Insolvency Law Review: Tier One Discussion Documents—Phoenix Companies' (January 2001) 99-111.

controlling the phoenix company. This practice of company recycling, if it is without restriction, was identified in the Cabinet Paper as acting "to the detriment of the new company and other businesses that deal with that company".[9] For the phoenix company itself may fail due to a director re-enacting his or her own form of groundhog day by repeating the same, ultimately fatal, business mistakes or by deliberately structuring the new company to use a phoenix arrangement to escape from its creditors, thereby perpetuating the cycle.

The Cabinet Paper noted that after consultation with stakeholders, the MED was unable to provide data that indicated the extent of abuse in New Zealand, and therefore it was not possible to "quantify the magnitude of abuse of phoenix company arrangements".[10] Most submitters had however suggested that this failure could be explained by the small probability of detection and subsequently enforcement action under the existing legislative restrictions, rather than that phoenix company abuse was minimal.

Both the Discussion Document and the Minister of Commerce's Cabinet Paper recognised that the use of phoenix arrangements "is counter to stakeholder interests in only a subset of cases".[11] Many phoenix situations actually are legitimate and in fact operate to promote the interests of creditors of the insolvent entity through lower transaction costs and higher sale price as the business is sold as a going concern.

In the Cabinet Paper, the Minister of Commerce recommended the introduction of restrictions on the "re-use by a director of a company in insolvent liquidation of the name of that company".[12] Further it recommended that such provisions be based on sections 216 and 217 of the United Kingdom *Insolvency Act 1986* (UK), referring to a then recently published Final Report of the United Kingdom Company Law Review that had concluded that abuse of phoenix companies had been reduced by the changes introduced in 1986.[13] Of interest is that the Cabinet Paper made no reference to the statement in that the Final Report of the Company Law Steering Group that had in fact acknowledged that the provisions had failed significantly to disturb the phoenix syndrome's potential to prejudice the public interest.[14]

Accordingly the decision was made to go ahead with to enact new sections to supplement the existing provisions in the Act, although as acknowledged in the Cabinet Paper, the proposed provisions would neither create a widespread restriction on the re-use of the name of the insolvent company,[15] nor would they eliminate the abuse of phoenix companies,[16] thus echoing the comments in the United Kingdom of the Company Law Steering Group. Sections 368A to F are therefore inherently incapable of dealing with phoenix company abuse and will, in common with the United Kingdom counterparts on which they are based, attract significant criticism.[17]

---

[9] Office of the Minister of Commerce, 'Cabinet Paper to the Chair of the Cabinet Economic Development Committee' (December 2003), *BL 3/28/3/4* para 3.
[10] Ibid para 15.
[11] Discussion Document, above n 8, p 102.
[12] Cabinet Paper, above n 9, para 44.
[13] Cabinet Paper, above n 9, para 49.
[14] United Kingdom, Department of Trade and Industry, *Modern Company Law for a Competitive Economy: Final Report* (June 2001) paras 15.55 -15.77.
[15] Cabinet Paper, above n 9, para 52.
[16] Cabinet Paper, above n 9, para 48.
[17] For a thorough criticism of sections 216 and 217 and the asociated rules contained in The Insolvency Rules 1986 see Stephen Griffin, above n 7, David Milman, 'Curbing the Phoenix Syndrome' (1997) *J.B.L.* 224 and Gary Wilson, 'Deliquent Directors and Company Names: The role of Judicial Policy-Making in the Business Environment' (1996) 47 *N Ir Legal Q* 345.

Regardless, the amendment of the Act was “seen as the best way to change the perception within business community that the laws dealing with phoenix companies are not adequate”.[18] Clearly this decision was motivated, at least in part, by a political desire to be seen to be responding to business concerns. However, this paper suggests that the new provisions, specifically sections 368A – F, may cause a number of unanticipated and undesirable consequences.

II PHOENIX COMPANIES: NEW SECTIONS 386A – 386F

For the purposes of this paper the new sections, which are attached in Appendix One, are discussed under three headings. Firstly the new offence restricting phoenix company activity and the definitions of key terms as set out in sections 386A and 386B are reviewed. Secondly, the paper considers the extent of the concurrent civil liability established by section 386C. Finally, the paper addresses sections 386D to 386F which contain the three exceptions to the section 368A offence and issues relating to applications for leave under s368A.

A *The New Offence and Definitions (sections 368A and 368B)*

An analysis of section 368A reveals that the offence contains five distinct elements. These are:

1. The accused is a director of the failed company and is either a director or has demonstrated the requisite degree of control over the new (phoenix) company.
2. The time limits specified in the section are satisfied.
3. That the old company was placed in insolvent liquidation
4. The names of both companies, if not identical, are sufficiently similar as to suggest an association.
5. That none of the exceptions apply and that the court had not given leave for the director to be involved with the new (phoenix) company.

Each of these elements is discussed separately below, however first the paper outlines the nature of the offence in terms of intention or mens rea. It also discusses what factors New Zealand courts are likely to take into account when required to consider the issue.

1 *Role of intention?*

Section 368A prescribes that a director ‘must not’ be a director of a phoenix company within a certain period of being a director of a failed company, unless that director has been granted leave. The mischief that the section precludes relates to a person being involved with two companies with the same or similar name within certain time frames of one company being liquidated. As outlined above, the prohibition is narrower in its focus than all ‘bad’ phoenix company arrangements. It is also not designed to prevent the re-use of a company or business name per se, only the recycling of a company name by a director of the failed company. It does not attempt to restrict transactions by delinquent directors with new companies which have no relationship with the failed company, although any asset sale by a director at undervalue to another company, with which that director is associated, if done in bad faith will contravene new section 380(2).

[18] Office of the Minister of Commerce , ‘Regulatory Impact Statement’ (attached to the Cabinet Paper to the Chair of the Cabinet Economic Development Committee, BL 3/28/3/4), (December 2003).

Section 368A does however have the potential to catch bona fide directors of a phoenix company, who were also directors of the failed company. For the culpability of a director in the collapse of the failed company is irrelevant to the offence. Also the section does not require that the assets of the failed company were transferred at less than market value or at all. In fact, on a natural and ordinary construction of the section there is no requirement to prove to a Court any intention by a defendant to abuse the corporate form.

The necessity of intention and the extent of any complementary judicial discretion under section 216 of the *Insolvency Act 1986* (UK) have been considered on a number of occasions by the English courts. Section 216 (is set out in Appendix Two) applies to any director (or shadow director) of a company at any time within a 12 month period prior to that company being placed into insolvent liquidation. If that director becomes within a 5 year period, a director of another company which has a prohibited name, this is an offence.[19] A prohibited name is defined in similar terms to the New Zealand provision as one that is either the same name as that by which the liquidated company was known or is so similar as to suggest an association with the liquidated company.

In one of the first cases to consider the issue, Ralph Gibson LJ[20] in *Thorne v Silverleaf* commented that "it is clear that the sections as enacted apply to a wider set of circumstances that the case of a person attempting to exploit the goodwill of a previous insolvent company".[21] This case involved a director of two earlier failed companies, each of which had the name "Mike Smith" as part of its name. A creditor, who had had previous dealings with the director, and knew of the previous corporate failures, agreed to invest money in a new company also using the "Mike Smith" name. Subsequently, after a falling out between the two men, and the failure of the latest company, the creditor was successful in bringing proceedings under sections 216 and 217. On appeal, Ralph Gibson LJ, in upholding the decision of the lower court, held that in the absence of an application under section 216(3) for leave, the court is left with no discretion on the application of the sections.[22]

In a later case of *Ricketts v Ad Valorem Ltd*,[23] comment was also made to "the surprisingly long reach of this legislation."[24] Mr Ricketts, had only been a director for 6 weeks of Air Component Company Ltd when that company went into insolvent liquidation and, in the view of the court, was not responsible for its demise. However, subsequently and within 12 months of its liquidation, he became a director of another company, Air Equipment Company Ltd, which also subsequently went into liquidation. This second company had formerly been called Air Equipment Ltd, but had changed its name following a complaint from a third party, highlighting that Mr Ricketts had not intentionally traded on the goodwill in the name of the earlier company. A creditor of Air Equipment Company Ltd claimed payment from Mr Ricketts for the debts of this company by virtue of sections 216 and 217 of the Insolvency Act 1986. On appeal, it was argued on behalf of Mr Ricketts that the decision of the District Court went against the purpose of the provisions, which is to curb the abuse of phoenix arrangements. However, although it was found as a matter of fact that the:

---

[19] The penalties for breach are contained in s.430 and Sched 10 of the Insolvency Act 1986 (UK).
[20] *Thorne v Silverleaf* [1994] 1 BCLC 637.
[21] *Thorne v Silverleaf* [1994] 1 BCLC 637, 642 (Ralph Gibson LJ).
[22] *Thorne v Silverleaf* [1994] 1 BCLC 637, 642 (Ralph Gibson LJ).
[23] *Ricketts v Ad Valorem Factors Ltd* [2004] 1 All ER 894.
[24] *Ricketts v Ad Valorem Factors Ltd* [2004] 1 All ER 894; para 24 (Simon Brown LJ).

> [t]his was not a phoenix syndrome case; there was no transfer of assets by Air Component to Air Equipment at an undervalue; there was no evidence that the companies were used to run up debts and to avoid their payment….there no evidence that creditors of Air Equipment or anyone else had been misled by the similarity of the names of the two companies or the fact that Mr Ricketts was a director of both of them[25]

the argument was rejected. Mummery LJ stated, "the legal position is that, if the name of Air Equipment is a prohibited name within the natural and ordinary meaning of the language of s216(2), this case is caught by the restrictions, even if this is not a 'Phoenix Syndrome' case and even if the sanctions of criminal liability seem to be harsh.[26]

However, when the issue does come before a New Zealand court for determination, the court may not have to take such a harsh line. Under New Zealand criminal law, while many regulatory or public welfare offences have been classified as strict liability, liability is subject to a defence of the absence of fault. In contrast, this defence is not available to defendants in the United Kingdom when charged with strict liability offences. In New Zealand, it is only those offences that have been categorised as absolute liability offences, where this defence is unavailable. And only a small number of offences fall within this category. Adams on Criminal Law[27] comments New Zealand courts have been reluctant to conclude that offences are absolute liability[28] and will only be so categorised if it is imposed "in clear terms or by necessary implication".[29]

Therefore what approach are courts in New Zealand likely to take? As stated, the courts have been disinclined to categorise an offence as absolute liability, especially when conviction gives rise to serious and substantial consequences[30] for a defendant, as is the situation with section 368A, especially as civil liability is consequential on conviction for the offence rather than as a separate head of liability. If the section is construed as a strict liability offence, to which the defence of absence of fault will be available to a defendant, this may avoid some of the harsher consequences of the UK cases, Although, the extent this may aid a defendant is unclear. Adams on Criminal law describes the no fault defence is one of:

> due diligence or absence of negligence. It includes cases where the accused reasonably, but mistakenly, believed in facts which, if true, would have made the conduct innocent, and also cases where the accused may have known the facts but had done what a reasonable person would have done to prevent the offence.[31]

The question arises in respect of which of the five elements of the offence would the no fault defence be potentially applicable. The first four elements arguably are all questions of fact that will need to be proven to the court, although the exact nature of the test for each element is not yet clear. With respect to the fifth element, it is

---

[25] *Ricketts v Ad Valorem Factors Ltd* [2004] 1 All ER 894, para 16, (Mummery LJ).
[26] *Ricketts v Ad Valorem Factors Ltd* [2004] 1 All ER 894, para 18, (Mummery LJ).
[27] Bruce Robertson (ed), *Adams on Criminal Law* (2005).
[28] Ibid, 66.
[29] *Millar v MOT* [1986] 1 NZLR 660, 668. (CA).
[30] Companies Act 1993 (NZ) s 368A(2) provides that contravention of section 368A(1) is an offence that is liable to a penalty as set out in section 373(4). This section specifies that a person is liable for imprisonment for a term not exceeding 5 years or to a fine not exceeding $200,000.
[31] Adams on Criminal Law, above n 27, 63.

possible that a defence of absence of fault may be available. For example, where it shown that a defendant had taken reasonable steps to comply with the exceptions or taken some action which the director mistakenly believed complied with the exceptions. However, this would not aid a director who acted in ignorance of the restriction.

2 *Extended Definition of Director*

Sections 368A and B expand the ambit of the restriction beyond appointed directors of the failed company or the phoenix company. In terms of the failed company, the offence extends to any director of that company who was a director at any time in the 12 months before commencement of the liquidation.

However, a wider circle of persons involved in the phoenix company are targeted. Section 386A(1) restricts prohibited directors from not only being a director of the phoenix company, but also from being directly or indirectly involved in the formation, promotion or management of a phoenix company. This will discourage former directors from using dummy directors to run the phoenix company.

The offence cannot be avoided by adopting a non-corporate form for the new business, as section 386(1)(c) extends the prohibition to any involvement in a business that has same or similar name to a failed company. Clearly the mischief of section 368A is the deterrence from exploitation of any goodwill of the failed company that is attached to its name, rather than to ensure that anyone who has been responsible for the failure of one company should initially, at least, be required to do so without the benefits of limited liability.[32]

3. *Liquidation of Failed Company*

A failed company is defined as one that was placed in liquidation when it was unable to pay its debts,[33]rather than some other form of insolvent administration. Accordingly if a director of a failing company becomes involved in a phoenix company, when a failing company is in receivership or voluntary administration, this would not on the face of the section breach the provision. However, a director contemplating such a course of action would need to ensure either that the failing company was not ultimately liquidated or that his or her involvement with the new company fell within one of the exemptions. Otherwise the director may contravene the prohibition as soon as the old company is placed in liquidation, even if the director had resigned prior to that date, provided the liquidation was within 12 months of the resignation.

4 *Time Limits*

The restriction against involvement in a phoenix company extends to any time both before and for a period of five years after the commencement of the liquidation, providing the phoenix company has the same or similar name to the pre-liquidation name of a failed company. In terms of an existing company, or companies within a corporate group with a similar name and common directors, the exception contained in section 368F should be noted.[34] The restriction also applies to any time within the five

---

[32] See the Report of the Insolvency Law Review Committee, above n 5, para 1826. The Committee was of the view that a person who was responsible for the failure of one company, and who wishes to commence trading, should initially at least be required to do without the benefit of limited liability.

[33] This term is defined at section 287 of the *Companies Act 1993 (NZ)*.

[34] See discussion on page 12 for discussion of this exception.

year period after the commencement of liquidation and the restriction would include a company incorporated after the commencement of liquidation or an existing company which changed its name to a name similar to the pre-liquidation name of the failed company, providing there is a common director.

5 *Identical or Similar Names and the requirement of Association*

Section 386B(1) defines a pre-liquidation name as any name (including trading names) of the failed company in the 12 months prior to the commencement of liquidation. The inclusion of any former names is to prevent the directors of a struggling company transferring the goodwill and assets to a new company with the same or similar name and then changing the name of the failing company immediately before it is placed in liquidation.

For a company to be phoenix company, in relation to a failed company, it must be known by a name that is the same or a similar name. In an attempt to clarify what is meant by the phrase 'known by a name', section 386B(2) specifies that a company is known by a name, if that is its registered name or if it carries on business or part of its business under that name. Therefore, the cumulative affect of these extended definitions, is that there is potential for contravention when the phoenix company uses a name in any way similar or associated with that of the failed company, even as a trading name or logo.

In an attempt to provide clarification as to the required degree of similarity, section 386B states that the name must be so similar as to suggest an association with the pre-liquidation name of the failed company. Whether 'association' will require evidence of actual confusion between the two entities or whether a judge will imply a requirement of objective reasonableness into this assessment will need to be determined by the courts. Clearly, association will require something less than the "identical or almost identical"[35]grounds for refusing an application for a company name under section 22 of the Act. It is the writer's view that when a New Zealand court is required to construe what degree of similarity is required for names to suggest an association, that court will be highly influenced by the developing English jurisprudence on this issue For an identical statutory test for similar names as one that suggests an association can be found in section 216 (2)(b) of the *Insolvency Act.*

Mummery LJ in *Ricketts v Ad Valorem Factors Ltd*[36]*,* the leading decision of the English Court of Appeal, upheld a decision of the District Court that an alleged phoenix company called 'Air Equipment Company Ltd' was a prohibited name as it related to an earlier failed company called 'Air Component Company Ltd'. He stated that in determining association:

> "[i]t is necessary, of course, to make a comparison of the names of the two companies in the context of all the circumstances in which they were actually used or likely to be used: the type of product dealt in, the location of the business, the types of customers dealing with the companies and those involved in the operation of two companies.[37]

As discussed above, counsel for the defendant argued that the court should take a purposive approach in its interpretation, which would have allowed the court to take

[35] *Companies Act 1933* (NZ) s22(2)(b).
[36] *Ricketts v Ad Valorem Factors Ltd* [2004] 1 All ER 894.
[37] *Ricketts v Ad Valorem Factors Ltd* [2004] 1 All ER 894, para 22 (Mummery LJ).

into account that Mr Ricketts had not been involved in any wrongdoing, nor was there any question of creditor confusion. Defence counsel also argued that for the District Court to find that the name 'Air Equipment' was a prohibited name was an "unreasonable restriction on the right to the lawful use of ordinary words in specialised fields,[38] and that the facts of the case should be distinguished from earlier decisions in which a unique identifier, such as personal name was used. Both of these arguments were rejected by Mummery LJ, who held that it was open to the District Court to reach the conclusion that it did "even in the absence of proof that there has been any express misrepresentation or that anyone has actually been deceived or confused into thinking that there was an association."[39]

In a number of cases the use of identifier such as the personal name of the director has been sufficient to suggest an association.[40] In another case, a company with the name 'MPJ Construction Ltd' was seen to suggest an association with a company named MPJ Contractors Ltd' and the adoption of a different style of stationery was not sufficient in the circumstances to avoid the effects of sections 216 and 217.[41]

B *The Parasite of Civil Liability*

Contravention of s368A may also result in personal liability for certain debts of the phoenix company under s368C. Liability under this subsection is not a separate head of liability with a separate burden of proof, but is consequential or parasitic[42] on the contravention of section 368A and, of course, the failure of the phoenix company. Civil liability accrues on the contravention of section 368A, which would occur on the elements of the offence being proven, rather than on conviction for the offence. However, only those persons who contravene s368A by virtue of being a director of the phoenix company under section 368A(1)(a) or are directly or indirectly concerned in or take part in the promotion, formation or management of such company under s368A(1)(b) are potentially liable. Those persons who involvement in a successor business (which is not a company) but which has the same or similar name to the failed company are excluded under section 368C(1). However, as the principals of such a successor business would not have the advantage of the corporate form, they run the risk of personal liability for the debts of the business through the operation of the general law.

Personal liability for certain debts of the phoenix company also may extend to persons who, under a sort of 'guilt by association' provision, knowingly follow the instructions of someone who is in breach of section 368A in the management of the phoenix company. For section 368C(2) provides that a person (A) who is involved in the management of the phoenix company may become liable for certain debts of the phoenix company, if in the management of that company, A is willing to act on the

---

[38] *Ricketts v Ad Valorem Factors Ltd* [2004] 1 All ER 894, para 21 (Mummery LJ).
[39] *Ricketts v Ad Valorem Factors Ltd* [2004] 1 All ER 894, para 22 (Mummery LJ).
[40] See *Thorne v Silverleaf* [1994] 1 BCLC 637with regard to common identified in companies name of 'Mike Smith'; *Commissioners of HM Revenue & Customs v Benton-Diggins* [2006] EWHC 793(Ch) with regard to name 'William' as a common name in a number of hairdressing businesses; *Commissioners for HM Revenue & Customs v Walsh* [2005] EWHC 1304(Ch)with regard to surname 'Walsh' and *Penrose v Official Receiver* [1996] 2 All ER 96 with regard to the identified 'Hudson' with respect to cafes.
[41] *Archer Structures Ltd v Griffith* [2003] EWHC 957 (ch), [2004] 1 BCLC 201, [2003] BPIR 1071.
[42] See Gary Wilson, 'Deliquent Directors and Company Names: The role of Judicial Policy-Making in the Business Environment' (1996) 47 *N Ir Legal Q* 345, 347 where he described section 217 of the Insolvency Act 1986 (UK) in this regard.

instructions given by another person (B), who A knows at that time is contravening s386(1)(a) or (b).

Personal liability covers those debts and liabilities incurred during the period when the director or person involved in management etc of the phoenix company and that company was known by the same name or a similar name to the pre-liquidation name of the failed company.[43] Liability is stated to be joint and several, thus leaving it open for creditors to include within any proceedings actual directors of the failed phoenix company as well as managers or persons acting under instruction.

In the United Kingdom since 1986 the overall effect of section 217 has been to create a route for creditors to seek a private remedy against a director for a debt on the liquidation of the debtor (phoenix) company. Directors may be liable irrespective that they have not personally guaranteed the debts of the company and regardless of whether a director has acted bona fide or whether there has been any confusion among creditors. In *Thorne v Silverleaf,* a creditor of the phoenix company was able to recover even when the creditor was involved in the affairs of that company, to the extent that he was described as aiding and abetting the commission of the section 216 offence.

C *Exceptions*

The exceptions to sections 216 and 217 of the *Insolvency Act 1986 (UK)* are located in the *Insolvency Rules,*[44] and while this has created problems in terms of interpretation, these exceptions carve out certain business practices from the operation of the provisions. The exceptions contained in sections 368D to F substantially emulate the UK exceptions.

1 Exception One: Section 386D (Successor company)

The most important of the exceptions provides a mechanism for directors to be able to capitalise on any goodwill in the failed company name, by excluding the application of section 386A when the new company qualifies as a successor company as that term is defined in s386D(2) and is named in a successor company notice. A successor company is a company that acquires the whole or substantially the whole of the business of the failed company, provided that the acquisition is arranged by a liquidator or receiver or under a deed of company arrangement under Part 15A of the Act. The exemption requires that the successor company notice must be sent to all creditors of the failed company within 20 working days after arrangements for the acquisition of the business are made. It must specify certain details which identify the failed company, the circumstances in which the business is acquired by the successor company, the name of the successor company and any proposed trading names. The notice must also state in respect of a person named in the notice (although the section does not specify which persons must be named in the notice) those persons' full name, the duration of his or her directorship of the failed company and the extent of his or her involvement in the management of the failed company. Providing these requirements are complied with, someone, who otherwise would be prohibited director,

[43] Liability for a person (A) who have acted on the instructions of another person (B), when B is known by A to have contravened section 386A, covers those debts accrued in the period when A was acting or was willing to act on the instructions of B under section 368C(3)(b). Section 368C(5) creates the presumption that if A has acted on the instructions of B in the past, that A will be presumed, unless the contrary is shown, to have been willing at any later point to be willing to act on the instructions of B.

[44] *Insolvency Rules 1986* (UK), 4.226 to 4.230.

can act in any of the prohibited ways with regards the successor company, regardless of the fact that leave has not been obtained from the court.

The rationale behind this exception is that the involvement of a liquidator or receiver in the sale process is deemed sufficient to ensure that the transaction is at arms length and that the best price possible is obtained for the benefit of the creditors of the failed company. It also recognises that often the only persons interested in the assets of the failed company are the former directors and shareholders. This provision was not included in the original Bill and clearly would have unnecessarily restricted the ability of a liquidator or receiver to hive off profitable parts of the company to a known buyer, thus forcing a liquidator to find other buyers for the business or to break up the business and sell off its assets in parts. This may reduce the value of any goodwill in the failed business and its name and would have, in many cases, act to the detriment of creditors.

However, as shown in the United Kingdom, as the only control on the exemption is that the transfer to the successor company must be done under the supervision of a liquidator or receiver, that it is imperative that any such insolvency administrator is independent of both companies. For all that is required is that the creditors of the failed company receive a compliant successor company notice. Under the exemption, there is no mechanism for creditors to object to the transfer of the business to the successor company or to question the details of the transfer. The notice is only required to set out the circumstances in which the business has been acquired by the successor business" which is an imprecise standard and therefore open to the possibility of abuse. On a narrow construction, the obligation could be satisfied by simply detailing the circumstances giving rise to the failure of the earlier company rather than details specific to the transfer of the assets of the business such as the transfer price. As stated above, the drafters of section 386D appear to have overlooked specifying which persons must be detailed in the successor company notice, although at a minimum it must include those persons who were or are directors of both the failed company and the successor company. Although providing full details of the composition of the successor company board, including any new directors, may be advantageous to convincing creditors and suppliers to continue to do business with the new company.

2 Exception Two: Section 386E: (Temporary Leave of the Court))

The second exception is more technical in nature and permits a period of grace for a director to apply for leave of the court. The leave application to act as a director of a phoenix company must be filed within 5 working days after the commencement of liquidation of the failed company and can not be filed retrospectively. The period of grace allows the person to act as director while the application for exemption is processed. The time limit for this period of grace, starting from the commencement of liquidation, is the earlier of the close of six weeks from that date and the 'date of which the Court makes an order of exemption'.

Specifying the 'date of the order of exemption' as the alternative date is likely an oversight by the legislative drafters. For if the provision is construed literally, in the event that a court refused to make an order of exemption, this would mean that period of grace must always expire at the end of the six week period. The illogical result would be that although the court has refused to grant leave to a person to permanently become a director, that person could remain as a director until the expiration of the six week period without contravening s368A. The equivalent United Kingdom Insolvency rule provides that the temporary period expires in six weeks or on the day that the court disposes of the application for leave, whichever of those days occurs first. A New

Zealand court may be required to construe s368E(2)(b) in such a manner to avoid what otherwise would be an absurd outcome.

3 *Exception Three: Section 386F (Existing non-dormant phoenix company)*

The prohibitions in sections 386A(1)(a) and (b) do not apply in respect of what otherwise would be a phoenix company, due to the fact that has been known by a name (or names) that is the same or similar to the name to a failed company, if it has been known by that name or names for not less than 12 months before the commencement of liquidation and it has not been dormant during that period. The provision recognises that a director of one company within a group of associated companies is commonly a director of other companies within that group and that the names of group companies are often deliberately so similar to suggest an association with each other. Clearly, it would be unworkable if all other companies within a group had either to change their names or remove any common director when one company within a group was placed in liquidation. However the exception only applies providing that the existing company has not at any time during the 12 months prior to the liquidation been a dormant company.[45] This requirement is designed to ensure that the existing company is not capitalising on the good will of the failed company, nor is it likely that customers will be confused between the two companies. It prevents the practice of having an incorporated company kept 'on the shelf' waiting to be used once it is clear that a failing company is about to be placed in liquidation.

In *Penrose v Official Receiver*[46] Chadwick J commented with regard to the third excepted case[47]that it "shows that the mischief is not thought to exist in a case where the company having a prohibited name has been established and trading under that name for a period of not less than 12 months before the liquidating company went into liquidation. The former director of the liquidation company can join, or can remain a member of, the board of such company without restriction. That must be because the mischief is not perceived to exist when the company having a prohibited name is not a phoenix."

The relationship between section 216 and the third exception was also recently examined by the English Court of Appeal in *ESS Production Ltd (in administration) v Sully*[48] although the key issue in the case was that Insolvency Rule 4.230 rule only expressly refers to a name in the singular sense, although in the offence contained in section 216, there is an express reference to the name or names by which the prohibited company had been known. As section 368F specifically refers to 'name or names', it is clearly intended that the exception should include both the actual name as well as any name by which that company was known. This may be something less than the trading name of the company.

D *Leave of the Court*

[45] Section 368 F(2) specifies that a company has not been dormant during the 12-month period if transactions that are required by section 194(2) to be recorded in its accounting records have occurred throughout that period. Section 2194(2) provides that accounting records must contain (a) entrieds of moneys received and spent each day and the matters to which it relates; (b) a record of the assets and liabilities of the company; (c) if the company's business involves dealing in goods, then a record of goods bought and sold and record of stock held at the end of the financial year; and (d) if the company's business involves providing services, a record of services provided and relevant invoices.

[46] *Penrose v Official Receiver* [1996] 2 All ER, 96.

[47] *Insolvency Rules 1986* (UK) rr 4.230.

[48] *ESS Production Ltd (in adminstration) v Sully* [2005] EWCA Civ, 554.

If a director does not fall within any of the excepted circumstances outlined above, then in order to avoid the double jeopardy of a criminal offence and personal liability for relevant debts of the successor company, he or she must first obtain the leave from the court under section 386(A)(1). As currently worded, the section does not provide a court with any guidance as to the factors that it should consider when disposing of an order of exemption, although this may be detailed in the regulations that are yet to be promulgated.

However, the writer suggests that some guidance as to the likely approach may be gleaned from the English cases which have had to consider the issue. The New Zealand provision diverges in a limited respect from the equivalent provision in the *Insolvency Act 1986* (UK). For section 216(5) of the *Insolvency Act 1986* (UK) supplies some additional guidance to a judge in that it states that the Secretary of State or the Official Receiver may appear (at the leave application hearing) and call attention to any relevant matters. Also *Insolvency Rule* 4.227 specifies that a Court is authorised to require the liquidator to report on the circumstances of the failed company's insolvency and the applicant director's role in its downfall. However, how far a judge can consider factors such the degree of risk faced by the creditors of the new company continues to be one of the more controversial aspects of the UK provisions.

In the first case to consider the discretion, *Re Bonus Breaks Ltd,*[49] Morritt J took a broad public interest approach in deciding to grant leave to the applicant and did not limit his considerations to whether the applicant could be involved with a new company with a similar name to an insolvent company. Instead he considered not only the applicant's conduct and nature, but also the proposed capital and management structure of the new entity, including the experience and skills of the other directors. The later point was viewed as essential to rectify the perceived flaws of the applicant in certain areas. Further in granting leave, Morritt J, who was concerned at the level of redeemable capital, did so on the basis of an undertaking offered by the applicant agreeing to restrict the redemption of capital for a two year period.

One commentator viewed this Morritt J's approach as a "radical reading of section 216",[50] as in his view it created an illogical situation whereby a former director of an insolvent company is free (subject to the *Disqualification Act 1986* (UK)) to set up a new company to conduct any business without scrutiny, whereas as soon as that director wants to use a prohibited name for that company, the director's performance, skills and attributes are subject to evaluation. Subsequent courts have however preferred to take a more limited approach or to treat the case as one appropriately decided on the information presented to Morritt J.[51]

In the arguably leading case on this point in the United Kingdom, *Penrose v Official Receiver,*[52] Chadwick J took the opportunity to set down what principles he believed should guide a court in the exercise of its discretion in these circumstances. In this case, it was argued before the court that its discretion in this instance was similar to when it was asked to reconsider an order disqualifying a director;[53] however Chadwick J rejected this argument. His Honour was of the view that the disqualification imposed by section 216 was not because the director had committed any wrongdoing, but simply to "because the applicant wishes to continue trading through a limited company

---

[49] *Re Bonus Breaks Ltd* [1991] BCC 546.
[50] Wilson, above n 42, 352.
[51] *Penrose v Official Receiver* [1996] 2 All ER 96, 104, and *Re Lightning Electrical Contractors Ltd* [1996] 2 BCLC, 302 306, [1996] BCC, 950 at 940 per EW Hamilton QC.
[52] *Penrose v Official Receiver* [1996] 2 All ER 96.
[53] *Company Directors Disqualification Act 1986, s 17 (UK).*

with a prohibited name"[54] and it was "wrong to treat him, without evidence of misconduct as it he were unfit to be a company director." He then stated:

> "[u]nless the court is satisfied on the material which is before it on the application under s 216 of the Insolvency Act that the applicant is a person whose conduct in relation to that liquidating company makes him unfit to be concerned in the management of a company, it should exercise its discretion under s 216(3) with regard only to the purposes for which s 216 was enacted and not on the more general basis that the public requires some protection from this applicant's activities as a company director.[55]

These purposes he derived from an analysis of the three heads of exceptions, which in his opinion, in each of the excepted cases allowed the director to trade under the new name "notwithstanding that the new company might be as undercapitalised as the old and notwithstanding that his lack of management skills might persist."[56] The purposes of the Act he identified were to prevent directors being involved with a new company that had, in some manner, received the benefit of the failed company assets at undervalue, including the goodwill attached to the name by operating with a similar name to the failed company in such a manner as to create confusion for creditors. As long as the court was convinced that a director was not acting contrary to these principles, that director could be involved in a new company, regardless that it may be likely that the director will make the same mistakes in the structure and financial management of the company. The approach of Chadwick J was subsequently affirmed in the decision of E.W. Hamilton QC (sitting as a deputy judge of the Chancery Division) in *Re Lightning Electrical Contractors Ltd.*[57] This more restricted approach has also been the subject of criticism, both at the policy level and also in terms of difficulties in the practical implementation of the test proposed by Chadwick J.[58] The writer suggests a modified *Penrose* approach, which does require some consideration of the level of skill of the applicant may be more consistent with the rehabilitation measures introduced in the voluntary administration regime that was adopted at the same time as the phoenix company sections.

III *OTHER SOLUTIONS?*

The United Kingdom provisions may have reduced the incident of phoenix company abuse, but clearly have not been a panacea. This may be an acceptable outcome for the government given that it was clearly concerned to be seen to be taking action.[59] However a legislative solution was not supported by all submitters on the Discussion

---

[54] *Penrose v Official Receiver* [1996] 2 All ER 96.

[55] *Penrose v Official Receiver* [1996] 2 All ER 96.

[56] *Penrose v Official Receiver* [1996] 2 All ER 96. Chadwick J preferred on the facts of the case not to follow the decision of the previous leading authority on this point *In Re Bonus Breaks* [1991] BCC 546, per Merritt J who had held that in determining leave it was necessary to consider the alleged phoenix company's ability to avoid the pitfalls which had resulted in the earlier companies failure. The approach of Chadwick J in *Penrose*has been subsequently affirmed by the decision in *Re Lightning Electrical Contractors Ltd* [1996] BCC 950 per E.W.Hamilton QC (sitting as a deputy judge of the Chancery Division)

[57] *Re Lightning Electrical Contractors* [1996] BCC 950.

[58] See Wilson , above n 42, 356-362, but he does conclude on balance that the approach in *Penrose* is to be preferred as "it presents an interpretation of the ambit of the section which is coherent with the other pertinent legislation dealing with both directors of insolvent companies and with the general availability of the limited company as a medium for the conduct of business." 365. and Griffin, above n 7, 387.

[59] Cabinet paper, above n9, para

Document as many viewed the issue as one of insufficient enforcement incentives, rather than inappropriate legislation.[60]

A legislative solution was not followed in Australia, following the recommendations of the Cole Royal Commission. The Royal Commission in 2002 investigated incidences of phoenix company abuse within the building and construction industry. In its Report, the Royal Commission supported a multi-organisational approach using existing laws and emphasising the need for concerted efforts using existing legislation. This recommendation was based on the effectiveness of existing legislation and the practices of relevant governmental regulatory and non-government bodies such as unions. It concluded that detection of phoenix company activity cannot be the responsibility of one agency. An example of one of these agencies using existing laws to deal with the problem was demonstrated recently by the ATO. It used the Australian Corporations Act equivalent of section 241 of the Act, as a creditor of a company, to successfully apply to wind up a company while it was still a going concern.

IV *CRIMINAL OFFENCE FOR INTENTIONAL ACTIONS AGAINST CREDITORS INTERESTS*

The second string to the deterrence of abusive phoenix company arrangements is a targeted at intentional acts by directors to defraud creditors and as such should only capture directors involved in 'bad' phoenix company arrangements. This is achieved by an amendment to section 380 of the Act to make it an offence for any director who with intent to defraud creditors does anything that causes material loss to any creditor. The proposal to create a new criminal provision was generally supported by those stakeholders who made submissions to the MED, although concern was expressed at the potential for a low level of successful prosecutions given the requisite standard of proof and the need to prove intent. However, a criminal provision was recognised as being seen as a greater deterrent, especially given the maximum penalty is imprisonment for a term not exceeding 5 years or a fine not exceeding $200,000. In addition, as primary responsibility for investigation falls on the government (through the National Enforcement Unit of the MED), it avoids the pitfalls of primary reliance on creditor enforcement.

The downside of a criminal sanction for such behaviour is that creditors who have suffered the material loss at the hand of the directors have no direct rights to compensation from those directors, if the company is not eventually placed in liquidation. Once a company is in liquidation, directors may face civil liability for the debts of the company in the event it is proven that they breached their duties as directors and liability under section 301 operates to benefit creditors generally.[61] Existing provisions permitting a liquidator to deal with transactions for inadequate consideration with directors and certain other persons may also be available.

V *CONCLUSION*

Having identified the '*mischief*' generated by abuse of phoenix company arrangements, the Government decided to introduce new provisions to bolster perceived weaknesses in the current laws. One of the government's key goals in reforming insolvency law was to promote the public interest by maximising the business community's contribution to the New Zealand economy through increasing

[60] Cabinet Paper, above n9, para 17.

[61] *Mitchell v Hesketh* (1998) 8 NZCLC 261, 559 funds recovered from director are paid to to the liquidator for distribution to the creditors and not directly to specific creditor who initiated action under s301.

job opportunities and incomes. Stephen Griffin in 2002 wrote with regard to section 216 and 217, that they provide a governance of phoenix companies that falls short of offering an adequate means of protection to the public interest and if the objective of section 216 was to “curb the prejudicial effect of the phoenix syndrome, the provision must be regarded as an unmitigated failure.”[62] His main concern is that the section does not protect the public interest with respect to phoenix companies that adopt a name unrelated to that of the failed company. This criticism can be equally levelled at new sections 368A- F and together with the potential for directors in good faith being caught under the provisions, may operate to counter any overall benefit to the public interest.

[62] Griffin, above n 7, 377.

APPENDIX ONE

New sections 386A to 386F Companies Act 1993

Phoenix Companies

"386A Director of failed company must not be director, etc, of phoenix company with same or substantially similar name

"(1) Except with the permission of the Court, or unless 1 of the exceptions in sections 386D to 386F applies, a director of a failed company must not, for a period of 5 years after the date of commencement of the liquidation of the failed company,---

"(a) be a director of a phoenix company; or

"(b) directly or indirectly be concerned in or take part in the promotion, formation, or management of a phoenix company; or

"(c) directly or indirectly be concerned in or take part in the carrying on of a business that has the same name as the failed company's pre-liquidation name or a similar name.

"(2) A person who contravenes subsection (1) commits an offence and is liable on conviction on indictment to the penalty set out in section 373(4).
Compare: Insolvency Act 1986 (UK) s 216

"386B Definitions for purpose of phoenix company provisions

"(1) In sections 386A to 386F,---

"**director of a failed company** means a person who was a director of a failed company at any time in the period of 12 months before the commencement of its liquidation, and **director of the failed company** has a corresponding meaning

"failed company means a company that was placed in liquidation at a time when it was unable to pay its due debts

"phoenix company means, in relation to a failed company, a company that, at any time before, or within 5 years after, the commencement of the liquidation of the failed company, is known by a name that is also---

"(a) a pre-liquidation name of the failed company; or

"(b) a similar name

"pre-liquidation name means any name (including any trading name) of a failed company in the 12 months before the commencement of that company's liquidation

"**similar name** means a name that is so similar to a pre-liquidation name of a failed company as to suggest an association with that company.

"(2) For the purposes of sections 386A to 386F, a company is known by a name if that name is its registered name or if it carries on business, or carries on a part of its business, under that name.
Compare: Insolvency Act 1986 (UK) s 216(6)

“386C Liability for debts of phoenix company

"(1) A person who contravenes section 386A(1)(a) or (b) is personally liable for all of the relevant debts of the phoenix company.

"(2) A person (A) who is involved in the management of a phoenix company is personally liable for all of the relevant debts of the company if---

"(a) in the management of the company A acts or is willing to act on instructions given by another person (B); and

"(b) at that time A knows that B is contravening section 386A(1)(a) or (b) in relation to the company.

“(3) In this section, relevant debts---

"(a) in subsection (1), means the debts and liabilities incurred by the phoenix company during the period when the person liable was involved in the management of the company and the phoenix company was known by a pre-liquidation name of the failed company or a similar name:

"(b) in subsection (2), means the debts and liabilities incurred by the phoenix company during the period when A was acting or was willing to act on the instructions of B and the phoenix company was known by a pre-liquidation name of the failed company or a similar name.

"(4) Liability under this section is joint and several.

"(5) For the purposes of this section, a person who, as a person involved in the management of a company, has at any time acted on instructions given by a person who he or she knew at the time to be in contravention of section 386A is presumed, unless the contrary is shown, to have been willing at any later time to act on any instructions given by that person.
Compare: Insolvency Act 1986 (UK) s 217

"386D Exception for person named in successor company notice

"(1) Section 386A does not apply to a person named in a successor company notice.

"(2) A successor company is a company that acquires the whole or substantially the whole of the business of a failed company under arrangements made by a liquidator or receiver or made under a deed of company arrangement under Part 15A.

"(3) A successor company notice is a notice by a successor company that---

"(a) is sent by the successor company to all creditors of the failed company for whom the successor company has an address; and

"(b) is sent to those creditors within 20 working days after the arrangements for the acquisition of the business are made under subsection (2); and

"(c) specifies---

"(i) the name and registered number of the failed company; and

“(ii) the circumstances in which the business has been acquired by the successor business; and

“(iii) the name that the successor company has assumed, or proposes to assume, for the purpose of carrying on that business; and

"(iv) any change of name that the successor company has made, or proposes to make, for the purpose of carrying on that business; and

"(d) states, in respect of a person named in the notice,---

"(i) his or her full name; and

"(ii) the duration of his or her directorship of the failed company; and

"(iii) the extent of his or her involvement in the management of the failed company.
Compare: Insolvency Rules 1986 (UK) rule 4.228

"386E Exception for temporary period while application for exemption is made

"(1) A person does not contravene a prohibition in section 386A for the temporary period set out in subsection (2) if that person applies to the Court within 5 working days after the commencement of the liquidation of the failed company for an order exempting that person from the prohibition in question.

"(2) The temporary period in subsection (1) is the period beginning on the date of the commencement of the liquidation of the failed company and ending on the earlier of---

"(a) the close of 6 weeks after the commencement of liquidation; and

"(b) the date on which the Court makes an order of exemption.
Compare: Insolvency Rules 1986 (UK) rule 4.229

"386F Exception in relation to non-dormant phoenix company known by pre-liquidation name of failed company for at least 12 months before liquidation

"(1) The prohibitions in section 386A(1)(a) and (b) do not apply in respect of a phoenix company that has been known by a name or names that are the same as the failed company's pre-liquidation name or are similar names if---

"(a) it has been known by that name or those names for not less than the period of 12 months before liquidation commences; and

"(b) it has not been dormant during those 12 months.

"(2) For the purposes of subsection (1), a company has not been dormant during the 12-month period if transactions that are required by section 194(2) to be recorded in its accounting records have occurred throughout that period.
Compare: Insolvency Rules 1986 (UK) rule 4.230".

APPENDIX TWO

Insolvency Act 1986, Ch. 45, s. 216 (England)

216 Restriction on re-use of company names

(1) This section applies to a person where a company ("the liquidation company") has gone into insolvent liquidation on or after the appointed day and he was a director or shadow director of the company at any time in the period of 12 months ending with the day before it went into liquidation.

(2) For the purpose of this section, a name is a prohibited name in relation to such a person if --

(a) it is a name by which the liquidation company was known at any time in that period of 12 months, or

(b) it is a name which is so similar to a name falling within paragraph (a) as to suggest an association with that company.

(3) Except with leave of the court or in such circumstances as may be prescribed, a person to whom this section applies shall not at any time in the period of 5 years beginning with the day on which the liquidation company went into liquidation --

(a) be a director or any other company that is known by a prohibited name, or

(b) in any way, whether directly or indirectly, be concerned or take in the promotion, formation or management of any such company, or

(c) in any way, whether direclty or indirectly, be concerned or take part in the carrying on of a business carried on (otherwise than by a company) under a prohibited name.

(4) If a person acts in contravention of this section, he is liable to imprisonment or a fine, or both.

(5) In subsection (3) "the court" means any court having jurisdiction to wind up companies; and on an application for leave under that subsection, the Secretary of State or the official receiver may appear and call the attention of the court to anymatters which seem to him to be relevant.

(6) References in this section , in relation to any time, to a name by which a company is known are to the name of the company at that time or to any name under which the campany carries on business at that time.

(7) For the purposes of thi section a company goes into insolvent liquidation if it goes into liquidation at a time when its assets are insufficient for the payment of its debts and other liabilities and the expenses of the winding up.

(8) In this section 'company" includes a company which may be wound up under Part V of this Act.

217 Personal liability for debts, following contravention of s 216

(1) A person is personally responsible for all the relevant debts of a company of at any time –

(a) in contravention of section 216, he is involved in the management of the company, or

(b) as a person who is involved in the management of the company, he acts or is willing to act on instructions given (without the leave of the court) by a person whom he knows at that time to be in contravention in relation to the company of section 216.

(2) Where a person is personally responsible under this section for the relevant debts of a company, he is jointly and severally liable in respect of those debts with the company and any other person who, whether under this section or otherwise, is so liable.

(3) For the purpose of this section the relevant debts of a company are –

(a) in relation to a person who is personally responsible under paragraph (a) of subsection (1), such debts and other liabilities of the company as are incurred at a time when that person was involved in the management of the company, and

(b) in relation to a person who is personally responsible under paragraph (b) of that subsection, such debts and other liabilities of the company as are incurred at a time when that person was acting or was willing to act on instructions given as mentioned in that paragraph.

(4) For the purposes of this section, a person is involved in the management of a company if he is a director of the company or if he is concerned, whether directly or indirectly, or takes part, in the management of the company.

(5) For the purposes of this section a person who, as a person involved in the management of a company, has at any time acted on instructions given (without the leave of the court) by a person whom he knew at that time to be in contravention in relation to the company of section 216 is presumed, unless the contrary is shown, to have been willing at any time thereafter to act on any instructions given by that person.

(6) In this section "company" includes a company which may be wound up under Part V.

Insolvency Rules 1986, SI 1925, s. 4.226

4.226 Preliminary

The Rules in this Chapter –

(a) relate to the leave required under section 216 (restriction on re-use of name of company in insolvent liquidation) for a person to act as mentioned in section 216(3) in relation to a company with a prohibited name,…

(b) prescribe the cases excepted from that provision, that is to say, those in which a person to whom the section applies may so act without that leave , and

(c) apply to all windings up to which section 216 applies, whether or not the winding up commenced before the coming into force of the Rules.

4.227 Application for leave under s 216(3)

When considering an application for leave under section 216, the court may call on the liquidator, or any former liquidator, of the liquidation company for a report of the circumstances in which that company became insolvent, and the extent (if any) of the applicant's apparent responsibility for its doing so.

4.228 First excepted case

(1) where a company ("the successor company") acquires the whole, or substantially the whole, of the business of an insolvent company, under arrangements made by an in insolvency practitioner acting as its liquidator, administrator or administrative receiver, or as supervisor of a voluntary arrangement under Part 1 of the Act, the successor company may for the purpose of section 216 give notice under this Rule to the insolvent company's creditors.

(2) To be effective, the notice must be given within 28 days from the completion of the arrangements, to all creditors of the insolvent company of whose addresses the successor company Is aware in that period; and it must specify –

(a) the name and registered number of the insolvent company and the circumstances in which its business has been acquired by the successor company,

(b) the name which the successor company has assumed, or proposes to assume for the purpose of carrying on the business, if that name is or will be a prohibited name under section 216, and

(c) any change of name which it has made, or proposes to make, for that purpose under section 28 of the Companies Act.

(3) The notice may name a person to whom section 216 may apply as having been a director or shadow director of the insolvent company, and give particulars as to the nature and duration og that directorship, with a view to his being a director of the successor company or being ptherwise associated with its management.

(4) If the successor company has effectively given notice under this Rule to the insolvent company's creditors, a person who is so named in the notice may act in relation to the successor company in any of the ways mentioned in section 216(3), notwithstanding that he has not the leave of the court under that section.

4.229 Second excepted case

(1) Where a person to whom section 216 applies as having been a director or shadow director of the liquidating company applies for leave of the court under

that section not later than 7 days from the date on which the company went into liquidation, he may, during the period specified in paragraph (2) below, act in any of the ways mentioned in section 216 (3), notwithstanding that he has not the leave of the court under that section.

(2) The period referred to in paragraph (1) begins with the day on which the company goes into liquidation and ends either on the day falling six weeks after that date or on the day on which the court disposes of the application for leave under section 216, whichever or those days occurs first.]

4.230 Third excepted case

The court's leave under section 216(3) is not required where the company there referred to, though known by a prohibited name within the meaning of the section –

(a) has been known by that name for the whole of the period of 12 months ending with the day before the liquidating company went into liquidation, and

(b) has not at any time in those 12 months been dormant within the meaning of section 252(5) of the Companies Act.