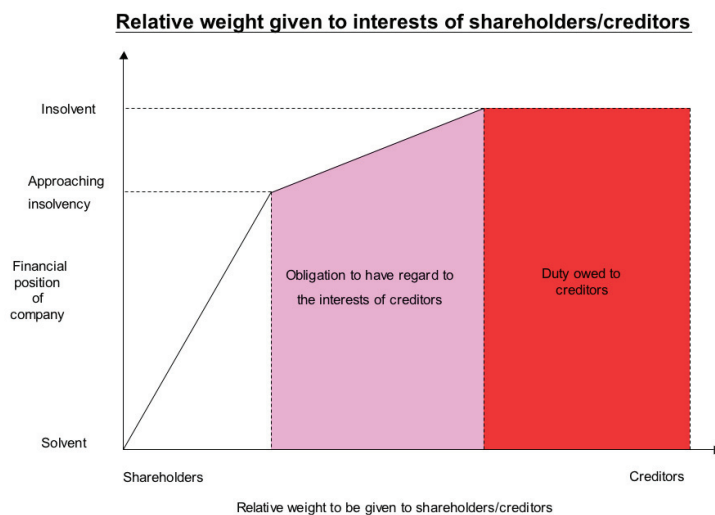


## The New Companies Act 2006

The new Companies Act incorporates a developing theme of the common law in recent years, namely that the law should impose on directors a higher standard of skill, care and diligence that has traditionally been expected of them by the UK courts.

In a solvent company this duty is owed to the shareholders. However, the Act also makes it clear that the duty to members is subject to certain obligations of directors to act in the interests of creditors. Weighing up the risk to creditors against the profit to shareholders is a necessary part of any director's duty, and directors should always have regard to the interests of creditors. But when a company is in insolvency - or approaching insolvency - the risk to creditors becomes particularly acute. Failure to meet the required standards at this point could lead to personal liability.



A director trading a company on the brink of insolvency may be liable to an action for breach of duty. He may be required to compensate the company for losses arising from his breach of duty. He may also be liable for wrongful trading, in other words trading where he knows or ought to know that there is no reasonable prospect that the company will avoid going into insolvent liquidation. Such a director may be required to contribute to the company's assets. Where the director is aware of this, he should carefully consider how to deal with the company's assets, or which of his creditors to pay, because he could be liable for fraudulent trading and any transaction could be set aside as a transaction at an undervalue, or as a preference to a particular creditor.

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All this means that - in the current climate - directors must, in their own interests as well as in the interests of any creditors, carefully monitor the financial situation of their company to enable them to make reasonable judgements about its solvency and prospects. Importantly for small companies, directors will not be excused the obligation to have regard to the likely consequences of a decision simply because the company cannot afford to investigate those consequences in any depth. The director must make the best assessment of the consequences as is possible in the circumstances. It is therefore important that directors take quality professional advice, and absolutely crucial if their company is approaching insolvency.

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