

HOOK A DIRECTOR FOR HIS COMPANY'S DEBTS JAMES HUTCHINSON, MARCH 2009

Summary

A recent case, drawing on an archaic nineteenth century statute, opens up another route for creditors to make directors personally liable for their company's debts. The Court of Appeal held that a director, who signs a contract on behalf of his company, might be making an implied representation about the company's ability to perform that contract and be liable in deceit if he knows that representation to be false.

The problem with claims for wrongful trading and fraudulent trading

Wrongful trading is a statutory offence under the Insolvency Act 1986 (S.214). Where a director concludes that there is no reasonable prospect of the company avoiding an insolvent liquidation, that director has to take every step, which a reasonably diligent person would take, to minimise potential loss to the company's creditors. If, after the company has gone into insolvent liquidation, a director is shown to have failed to comply with this duty in operating the Company before liquidation occurred, a court can order the director to make such contribution to the company's assets as it thinks fit.

Very few wrongful trading cases are brought to court, as they have to be brought by a liquidator who often has limited funds to pursue the director. Even if a creditor was to fund the liquidator, any recovery would go into the general pot for creditors and the court has no power to pass the award to the funding creditor.

In the same way, claims for fraudulent trading under S213 of the Insolvency Act 1986 are rare and the proceeds of such a claim benefit all creditors generally.

However, where fraud is involved, creditors can make claims against directors which provide a remedy to them and not the general group of the company's creditors.

Fraudulent deceit

Fraudulent deceit is a claim made directly against a director for damages. A recent case in the Court of Appeal has recognised the possibility of a creditor in very specific circumstances suing a director and recovering for its own benefit. In [Contex Drouzhba Limited v Wiseman](#) [2007] EWCA Civ1021, a director signed on behalf of his company a document which contained a promise that the company would pay for goods to be ordered in the future. The Court found as a matter of fact that the company did not have the capacity to pay, nor had it any chance of gaining that capacity. The Court said that, by signing the order, the director had impliedly represented that the Company did have the capacity to pay but he had known this to be not true and had known that the Company had no chance of being able to pay. Accordingly, he was found personally liable for fraudulent deceit. There are however certain requirements that the promise given by the director, on behalf of his company, but for which he is personally responsible, needs to fulfil. These are set out in Lord Tenterden's Act of 1828.

Under Lord Tenterden's Act (or the Statute of Frauds (Amendment) Act 1828), a representation as to credit or solvency needs to be in writing and signed by the person who is to be made liable. Note that in this case the Court found that the representation was "implied". In other words, there were no words written or to which the director put his signature that represented expressly an ability to pay. The Court said that that was not necessary – the contract had payment terms in it and by signing up to them, the director was representing that the Company would be able to meet them. In this case, the director knew the Company did not have that capacity and so the representation was fraudulent. The fact that the fraud was comprised in a written document which was signed was sufficient to satisfy the requirements of the Act. Neither was the Court impressed by the argument that the director was

acting on behalf of his Company when doing so. As Lord Justice Waller explained, the Court was not concerned with excusing fraudulent behaviour or with differentiating between capacities in which persons put their names to documents.

Section 6 of the Act states:

“Action not maintainable on representations of character etc, unless they be in writing signed by the Party chargeable.

No action shall be brought whereby to charge any person upon or by reason of any representation or assurance made or given concerning or relating to the character, conduct, credit, ability, trade, or dealings of any other person to the intent or purpose that such other person may obtain credit, money, or goods upon, unless such representation or assurance be made in writing, signed by the Party to be charged therewith.”

As a claimant against a director in these circumstances, you will need to prove that these requirements are satisfied, even if the very deceit on which you rely is only implied by the director signing the order.

Comment

A successful claim for fraudulent deceit will always be difficult to bring and will depend on the particular facts of the case. However, the decision in [Contex v Wiseman](#) is another weapon in a creditor’s armoury. Note that the Court found that there had been an implied representation (i.e. simply by ordering the goods the director was taken to have represented that his Company could pay for them). This follows the principle first explained in the case of John Hudson v Oaten (unreported 1980). Even if the success of a claim might be in doubt, the threat of personal proceedings against a director might be enough to ensure payment.

When entering into new contracts with companies where there might be a question in the future over their ability to pay, we suggest getting a director of the purchaser company to confirm in writing that the company (a) is capable of paying for the goods or services ordered and (b) will pay. If it later transpires that the company is insolvent, the creditor would have a legitimate right to pursue the director, even if the director was sending the communication on behalf of the Company. The creditor receiving payment from a Company shortly before its liquidation however may need to be wary of it being treated as a preference under S239 of the Insolvency Act 1986.

An email exchange might suffice following the case of *Metha v J Pereira Fernandes SA* [2006] EWHC 813. This case held that an email satisfied the requirement of “writing” under the Statute of Frauds 1677. Whether it was signed would depend on whether the sender typed in his name or initials. An automated signature on an email would not authenticate the intention of the sender.

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