A CRITICAL ANALYSIS ON THE REGULATION AND SANCTIONING OF WRONGFUL AND FRAUDULENT TRADING; WHETHER THE SYSTEM IS SUFFICIENT TO DETER DIRECTORIAL MISCONDUCT IN TRADING

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A. INTRODUCTORY CHAPTER
B. THE DUTY TO PROMOTE THE SUCCESS OF THE COMPANY AND THE EFFECTS OF LIMITED LIABILITY
- **(1) Introduction**
- **(2) Section 172; Duty to Promote the Success of the Company**
- **(3) Director's Duty to Creditors (Section 172(3))**
- **(4) The Doctrine of Limited Liability**

C. THE REGULATION AND SANCTIONING OF WRONGFUL TRADING
- **(1) Introduction**
- **(2) Insolvency**
- **(3) Establishing wrongful trading**
- **(4) Section 214(3) Defence**
- **(5) Conclusion**

D. THE REGULATION AND SANCTIONING OF FRAUDULENT TRADING; THE CIVIL AND CRIMINAL OFFENCE
- **(1) Introduction**
- **(2) Dishonesty**
- **(3) Intent to defraud**
- **(4) The Civil Offence vs The Criminal Offence**
- **(5) Liability for Fraudulent Trading; Contribution to the Company's Assets**
- **(6) Conclusion**

E. DIRECTOR DISQUALIFICATION; SUFFICIENT TO DETER?
- **(1) Introduction**
- **(2) Effect of Disqualification**
- **(3) Protection of the public**
- **(4) Conclusion**

F. CONCLUDING CHAPTER

A. INTRODUCTORY CHAPTER

While shareholders own the company, it is directors who deal with the company's day-to-day affairs and management.[1] A company and their director(s) have a fiduciary relationship of trust for the directors to act on their behalf.[2] Where there is a large corporation with numerous directors, the management powers are given to the board as a whole, not just one individual. As directors have such authority in the management of the company, there are various fiduciary duties imposed on them to ensure they do not act *ultra vires*.[3] The Companies Act 2006 provides seven fiduciary duties

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[1] Eugenio Vaccari and Emilie Ghio, *English Corporate Insolvency Law: A Primer* (1st edn, EE) 211.

[2] Derek French, *Mayson, French & Ryan on Company* Law (37th edn, OUP 2021) 456.

[3] ibid at 457.

originating from common law. Although these duties are owed to the company as a whole, it is debatable whether they offer much protection to creditors.

Section 172(3) of the Companies Act 2006 provides for a duty to creditors, however, it was not until the recent landmark case of *BTI 2014 LLC V Sequana SA and others* [2022] that confirmed directors should indeed consider the interests of creditors.[4] Following this judgement, directors must aim to minimise losses to creditors when the company is insolvent or bordering insolvency.[5] Here, section 172(3) of the Companies Act 2006 is engaged and directors should cease trading as this may cause further loss to creditors. Thus, if the director continues to trade when they are no longer permitted to, they may not only be found liable for wrongful or fraudulent trading but also be in breach of section 172(3).

However, the protection offered by limited liability creates an incentive for directors to commit misconduct and take on risky ventures. As companies have their own separate legal personality, the debts of the company are not the debts of its shareholders.[6] This safeguards shareholders as they will not be found personally liable for the company's debts, however, places creditors at a greater risk for loss. Furthermore, limited liability has led to issues concerning the corporate veil.[7] As the veil protects the company's members and directors, it is difficult to hold them accountable for misconduct. This prompts directors to take risky ventures which they otherwise would not. Therefore, limited liability and the corporate veil provides an incentive for directors to continue trading even when there is a risk that this will cause greater loss for creditors.

When directors continue trading even though the company is insolvent or facing imminent insolvency, they may be liable for wrongful trading. This civil offence was first introduced as the burden of proof in fraudulent trading was too high and is nowadays much more common than fraudulent trading. However, questions remain on whether this is sufficient to deter director misconduct in relation to trading. The punishments, or lack thereof, for directors liable of wrongful trading have been criticised for being ineffective deterrence.[8]

A court may order directors to contribute to the company's assets to make up for the loss caused to the company as a result their wrongful trading.[9] However, this is only ordered when the wrongful trading results in a loss and the amount is limited to the loss caused.[10] Thus, this is more compensatory rather than punitive for the directors.[11] Furthermore, directors may also face disqualification. While disqualified, they will not be permitted to be a director for any company in the UK or with connections to the UK. However, similarly, this does not aim to punish the director themselves but rather to protect the public. This does not make the contribution order or disqualification insufficient deterrence as they do effectively raise standards of director practise.[12] Whilst the current schemes for the regulation and sanctioning of

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[4] [2022] UKSC 25.
[5] ibid.
[6] Geoffrey Morse and Thomas Braithwaite, *Partnership and LLP Law* (9th edn, OUP 2020) 318.
[7] David Milton, 'Piercing the Corporate Veil, Financial Responsibility, and the Limits of Limited Liability' (2007) 56 ELJ 1305.
[8] Richard Williams 'What Can We Expect to Gain from Reforming the Insolvent Trading Remedy?' (2015) MLR 78 (1) 55-84.
[9] s 214 Insolvency Act 1986.
[10] *Re Produce Marketing Consortium Ltd (No 2)* [1989] BCLC 520.
[11] *Re Lo-Line Electric Motors Ltd* [1988] Ch 477.
[12] ibid (n1) 269.

wrongful trading are not necessarily inadequate, there is a notably low number of claims which suggest some reform may be beneficial.[13]

The continuation of trading in an insolvent (or impending insolvency) company with the intent to defraud is fraudulent trading.[14] Unlike wrongful trading, this is a civil offence under section 213 of the Insolvency Act 1986 as well as a criminal offence under section 993 of the Companies Act 2006. For both the civil and criminal offence, it must be proved that the director in question had the intention to defraud creditors of the company or trade for any fraudulent purposes.[15] However, the phrasing of "intent to defraud" has led to many complications and uncertainties.[16] Whilst some interpretations have been given by English courts, no conclusive definition is provided by statute. Furthermore, the high burden of proof has made claims difficult to succeed in, thus, discouraging claims from being made. Similar to wrongful trading, directors may be ordered to contribute to the company's assets or face disqualification if found liable. Moreover, section 993(3) provides for criminal sanctioning of up to ten years imprisonment. The criminal penalty is an effective deterrence, however, similar with wrongful trading, the effectiveness of the civil offence is questionable. Furthermore, the lack of certainty caused by the phrase "intent to defraud" and the high burden of proof suggest that reform may be beneficial to ensure the current systems are adequate in the prevention of fraudulent trading.

Thus, this essay will analyse the aforementioned statues and their applications and interpretations in the English courts to determine whether they are adequate to deter director misconduct in relation to wrongful and fraudulent trading.

This chapter introduces topics of director misconduct in relation to wrongful and fraudulent trading which is the focus of this dissertation. Chapter two will discuss director duties and the effects of the doctrine of limited liability. Following this, chapter three will focus on the regulation and sanctioning of wrongful trading. Then, chapter four addresses the issue of fraudulent trading and whether the current schemes of regulation and sanctioning are sufficient. The penultimate chapter five will consider director disqualification and whether this sanctioning is sufficient to deter directors from committing such offences. Finally, chapter six is the concluding chapter.

B. THE DUTY TO PROMOTE THE SUCCESS OF THE COMPANY AND THE EFFECTS OF LIMITED LIABILITY

(1) Introduction

A director's relationship with their company is a fiduciary one and so they are subject to a number of fiduciary obligations.[17] This refers to a relationship of trust and confidence and is based on the notion of loyalty;[18] a fiduciary is trusted to act on behalf of another.[19] Thus, the director as a fiduciary, acts on behalf of the company taking into consideration their best interests. Unlike the traditional duties, such as contractual, these obligations are not stated in the contracts but are found in statute. Originating in common law, the enactment of the Companies Act 2006 later consolidated these

[13] A Herzberg 'Why Are There So Few Insolvent Trading Cases?' (1998) 6 ILJ 77.
[14] s 213 Insolvency Act 1986, s 993 Company Act 2006.
[15] ibid.
[16] Andrew Keay 'Fraudulent Trading: The Intent to Defraud Element' (2006) CLWR 35 (2).
[17] [1967] 2 AC 134, 159.
[18] Millett LJ in *Bristol and West Building Society v Mothew* [1998] Ch 1, 18.
[19] Derek French, *Mayson, French & Ryan on Company Law* (38th edn, OUP 2023) 457.

duties giving them statutory footing; sections 171 to 177 now sets out seven general directors' duties.[20]

However, when a company becomes insolvent or is on the brink of insolvency, the directors' duties shift to also consider the interest of creditors as per section 172(3).[21] The recent case of *BTI 2014 LLC V Sequana SA and others* [2022] clarified this.[22] This chapter shows that though directors have various fiduciary duties which regulate their conduct, the effectiveness of such duties are diminished because limited liability protects the company and thus creates an incentive for misconduct especially in relation to trading when the company is insolvent.

(2) Section 172; Duty to Promote the Success of the Company

The Companies Act 2006 consolidated the pre-existing law on the regulation of director duties.[23] Here, the focus is on section 172 specifically because, as Woods argues, this is one of the duties most commonly "disputed in post insolvency cases", concerning what the directors should have done prior to the company is declared insolvent.[24]

Under section 172, directors must act in a way, which they consider in good faith, would be most likely to promote the success of the company. They must "have regard to" to a non-exhaustive list of factors provided by section 172(1). These factors range from likely long-term consequences of decisions[25] to the need to act fairly between members of the company[26]. However, section 172(1) has faced criticism for its ambiguity in relation to the phrase "have regard to". Though some guidance has been provided by Secretary of State, Margaret Hodge who stated that "have regard to" means to "think about" and to "give proper consideration to",[27] ambiguity remains. Keay argues that many components of section 172(1) "remain somewhat of a mystery".[28] He criticised that this phrase has caused uncertainty surrounding what directors "actually need to do to fulfil their obligations under the section".[29]

This has undoubtably been the most controversial director duty under the Companies Act 2006. Keay provides that section 172 is more educational rather than practical and thus does little in practice. [30] Moreover, he criticises section 172 for being "vague" and providing "little direction or guidance".[31] Nonetheless, this duty remains relevant in insolvency. When a company is placed into insolvency (or when the director ought to know this), directors must cease trading as this may place the company into

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[20] Eugenio Vaccari and Emilie Ghio, *English Corporate Insolvency Law: A Primer* (1st edn, EE) 216.
[21] Companies Act 2006.
[22] [2022] UKSC 25.
[23] Sarah Worthington and Sinead Agnew, *Sealy & Worthington's Text, Cases, and Materials in Company Law* (12th edn, OUP 2022)
[24] John Wood 'Directors' duties post insolvency' (2021) IC&CLR 32 (7) 371-386, 5.
[25] s 172(a) CA 2006.
[26] s 172(f) CA 2006.
[27] Web archive, 'Duties of company directors' (*The National Archives*, 28 June 2007)<https://webarchive.nationalarchives.gov.uk/ukgwa/20070628230000/http:/www.dti.gov.uk/files/file40139.pdf>accessed 14 January 2023.
[28] Andrew Keay, 'Having regard for stakeholders in practising enlightened shareholder value' (2019) OUCLJ 19 (1) 118, 120.
[29] Ibid at 137.
[30] Andrew Keay, 'The Duty to Promote the Success of the Company: Is it Fit for Purpose?' (2010) University of Leeds School of Law, Centre for Business Law and Practice Working Paper.
[31] ibid at [36].

more debt.[32] Directors must consider the interest of creditors and minimise their losses.[33] Thus, when a company is insolvent or on the brink of insolvency, the section 172 duty to promote the success of the company is superseded by the creditor's duty (section 172(3) will be discussed later in chapter 2.3).

(3) Director's Duty to Creditors (Section 172(3))

Directors owe their fiduciary duties to the company itself.[34] However, there has been some ambiguity as to whether such duties are also owed to creditors.[35] The list of non-exhaustive factors under section 172(1) provides for stakeholder interests, however the interest of creditors is not generally mentioned here.[36] Section 172(3) does briefly mention creditors which provides that "the duty imposed by this section has effect subject to any enactment or rule of law requiring directors, in certain circumstances, to consider or act in the interests of creditors of the company".[37] However, it was not until the recent decision of the Supreme Court in *BTI 2014 LLC V Sequana SA and others* [2022] that the true extent of a duty to consider creditor's interests was clarified.[38] The following section will explore directors' duties towards creditors prior to and following this landmark case.

West Mercia Safetywear Ltd (in liquidation) v Dodd [1988] confirmed that directors have a duty to consider creditors' interest when they know or ought to know that the company is insolvent or on the brink of insolvency.[39] Nonetheless, there was uncertainty of whether the interests of creditors are to be prioritised at this point, or if this is merely to be considered alongside the interests of shareholders. The later enactment of section 172(3) preserved the duty and gave this statutory recognition.[40] However, *Yukong Line Ltd of Korea v Rendsburg Investment Corpn of Liberia (No 2)* [1998] later ruled against the idea of directors owing a duty to creditors.[41] Here, a director of an insolvent company, breached his duty to the company and transferred assets. Toulson J held that directors had no fiduciary duty towards creditors.[42] Nonetheless, the landmark decision in *BTI 2014 LLC V Sequana SA and others* [2022] clarified that directors do indeed have a duty towards creditors when the company is on the brink of or already insolvent.[43]

This was the first time the Court discussed the circumstances and extent to which directors must consider the interest of creditors with regard to their duties.[44] Here, the directors of *AWA* paid dividends of €135 million to *Sequana SA* which was compliant with the statutory requirements under the Companies Act 2006. However, *AWA* had long-term liabilities concerning pollution (needed to clean up a polluted river) which held the risk *AWA* may become insolvent in the future. This materialised a few months later and *AWA* became insolvent. *BTI* brought a claim on the basis that the

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[32] French (n 19) 697.
[33] *BTI 2014 LLC V Sequana SA and others* [2022] UKSC 25.
[34] Vaccari and Ghio (n 20) 233.
[35] ibid.
[36] CA 2006.
[37] ibid.
[38] [2022] UKSC 25.
[39] [1988] BCLC 250.
[40] CA 2006.
[41] [1998] 2 BCLC 485.
[42] ibid.
[43] Uksc, 'New Judgment: BTI 2014 LLC v Sequana SA and others [2022] UKSC 25' (UKSC Blog, 5 October 2022)<http://ukscblog.com/new-judgment-bti-2014-llc-v-sequana-sa-and-others-2022-uksc-25/> accessed 11 April 2023.
[44] [2022] UKSC 25.

director's decision to distribute dividends breached their duty to consider the interest of creditors, as there was a real risk of the company becoming insolvent in the future.

The Court here held that directors must consider the interest of creditors under section 172 and applied section 172(3). This concluded that there is no standalone creditors duty *per se*; such a creditors duty exists but as an extension of section 172.[45] Lord Reed rejected the existence of a "creditor duty" distinct from the general duty to promote the success of the company. However, he acknowledges that "there are circumstances in which the interests of the company … should be understood as including the interests of its creditors as a whole".[46] The interest of creditors is only to be considered alongside the interest of members. In addressing *West Mercia Safetywear Ltd (in liquidation) v Dodd* [1988], Lord Reed states that the "duty remains the director's duty to act in good faith in the interests of the company … effect of the rule is to require the directors to consider the interests of creditors along with those of members".[47] Lord Reed's view is supported by Lord Hodge who provides that the risk of insolvency "gives rise to the fiduciary duty to the company to give separate and proper consideration to the interests of a company's creditors".[48]

However, though a duty to consider creditors' interest was found to exist, the Court held that the mere real risk of insolvency was not sufficient to trigger this duty. There must be an "sense of imminence" such as when the company is insolvent or borderline insolvent or when insolvent liquidation or administration is to be expected.[49] As per Lord Briggs, "real risk of insolvency is not a sufficient trigger for the engagement of the creditor duty".[50] He states that the "real risk" argument is based on an "unsound principle" which assumes that "creditors of a limited company are always among its stakeholders".[51] This argument is supported by Lord Hodge.[52] Thus, when the dividend was paid, directors were not under duty to consider the creditor's interest as *AWA* was neither actually nor imminently insolvent at this time.

Therefore, following this decision, directors do have a duty to consider the interest of creditors. This duty arises when they know or ought to know that the company is insolvent, bordering insolvency, or when the possibility of insolvency is probable. This deters directors from continuing to trade when the company is insolvent or on the brink of insolvency and thus preventing wrongful and fraudulent trading.

(4) The Doctrine of Limited Liability

Though there are duties imposed on directors to ensure they do not act unlawfully, the doctrine of limited liability offers some protection to both directors themselves and shareholders. The cornerstone case which established the principle of limited liability is *Salomon v Salomon*.[53] Lord Macnaghten provides; "the company is at law a different person altogether from the subscribers to the memorandum … the company is not in law the agent of the subscribers or trustee for them".[54] Thus, the company has a

[45] Pedro Schilling de Carvalho and Bobby Reddy, 'Credit Where Credit's Due: The Supreme Court Take On Director's Duties And Creditors' Interests' (2023) CLJ 82(1), 18.
[46] [2022] UKSC 25 at [11].
[47] ibid.
[48] ibid at [246].
[49] ibid at [88].
[50] ibid at [199].
[51] ibid at [191].
[52] ibid at [247].
[53] [1897] AC 22.
[54] ibid at 51.

separate legal personality.[55] All business conducted and contracted signed are done so in the name of the company, not the individual(s) representing it.[56] Hence, liability of a company's member is limited to the amount they invested in the company. Furthermore, money owed to the company is not owed to its shareholders and debts of the company are not debts of the shareholders.[57]

This creates an incentive for directors to take risky ventures which may lead to wrongful or fraudulent trading as their personal assets are protected if the company faces financial difficulties. As identified by Hirt, the issue of limited liability becomes particularly "apparent when the company is insolvent because it has insufficient assets to meet the claims of all creditors". [58] The abuse of limited liability places creditors at a greater risk during insolvency. If the company is insolvent and has no assets, creditors will struggle to obtain their owed capital. There are only certain circumstances, where wrongful or fraudulent trading is present, that a director who caused the loss may be held responsible to pay back some of the company's debts.[59] Therefore, the creditors bear a greater burden.

Thus, whilst directors do have duties imposed on them to prevent misconduct, the doctrine of limited liability offers protection which can be abused causing directors to take risky ventures. This may lead to wrongful or fraudulent trading as limited liability creates an incentive to continue trading even when the company is insolvent or bordering insolvency as personal assets are not at risk, only the company's is.

(5) Conclusion

Directors owe various fiduciary duties to both the company and also its creditors once the company becomes insolvent. The landmark case of *BTI 2014 LLC V Sequana SA and others* [2022] clarified that directors do indeed have a duty to consider the interest of creditors once the company is insolvent or on the brink of insolvency.[60] At this stage, section 172(3) can be engaged, and directors must aim to minimise loss caused to creditors. However, the principle of limited liability has caused greater risk for creditors. As companies have their own legal personality and are known as a separate entity, stakeholders will not be held personally liable if the company goes into insolvency. This offers greater protection to directors and shareholders; however, creditors are at greater risk of not receiving their owed capital.

C. THE REGULATION AND SANCTIONING OF WRONGFUL TRADING

(1) Introduction

This chapter will explore the civil offence of wrongful trading covered by section 214 of the Insolvency Act 1986. When there is no reasonable prospects of the company avoiding insolvency or is already insolvent, directors should cease trading.[61] At this

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[55] Geoffrey Morse and Thomas Braithwaite, *Partnership and LLP Law* (9th edn, OUP 2020) 319.
[56] Alan Dignam and John Lowry, *Company Law* (12th edn, OUP 2022) 15.
[57] Paul Davies, *Introduction to Company Law* (3rd edn, OUP 2020) 7.
[58] Hans Hirt, 'The Wrongful Trading Remedy in UK Law: Classification, Application and Practical Significance" (2004) 1 ECFR 71, 74.
[59] s 213 Insolvency Act 1986, s 214 Insolvency Act 1986.
[60] [2022] UKSC 25.
[61] Eugenio Vaccari and Emilie Ghio, *English Corporate Insolvency Law: A Primer* (1st edn, EE) 242.

stage, the financial welfare of their creditors must be prioritised; thus, should directors continue to trade, they may be found liable for wrongful trading. This was introduced following the recommendations from the Cork Report as the burden of proof required to establish fraudulent trading was too difficult.[62]

If found liable, the director will be held personally liable for the company's debts resulting from the wrongful trading starting from the point where they knew the company was insolvent.[63] In some cases, they may be disqualified from being a director for up to fifteen years.[64] However, section 214(3) of the Insolvency Act 1986 provides a defence arising when the director has done everything within their power to minimise loss caused to the company's creditors.

Though first introduced as an extension of fraudulent trading, nowadays wrongful trading is much more common. Nonetheless, the regulation and sanctioning of wrongful trading has faced criticism due to its lack of effectiveness.[65] This chapter will critically analyse the civil offence under section 214 and whether this is sufficient to deter director misconduct.

(2) Insolvency

Once a company becomes insolvent, it may be wound up or liquidated and when this is finalised the company ceases to exist.[66] This may be ordered by the court in compulsory liquidation, or by shareholders through special resolutions in voluntary liquidation. The money raised from this will be used to pay back the company's debts because in a limited liability company, the members are not liable for such debts, only the company's assets can be claimed by liquidators and distributed to its creditors. Thus, directors even when the company is nearing insolvency, may in an attempt to save the business, continue trading which could cause further debts and loss to creditors if unsuccessful. To prevent the abuse of limited liability, the conduct of the company's directors during insolvency will be investigated for any wrongdoing which may have occurred leading up to insolvency.[67]

Continuing to trade post insolvency is not in itself an offence. [68] However, where a loss has occurred as a result of this, the directors responsible may be held liable for wrongful trading.[69] Thus, where wrongful or fraudulent trading has occurred, directors may be ordered to contribute to the company's assets.[70]

(3) Establishing Wrongful Trading

For a claim of wrongful trading to succeed, the director must have known or ought to know that the company was impending insolvency and there were no reasonable prospects of avoiding this.[71] This is judged by the objective and subjective test provided by section 214(4) of the Insolvency Act 1986. Firstly, the court will consider the standard expectation of a reasonably diligent director with the knowledge, skill and

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[62] Insolvency Law and Practice: Report of the Review Committee (Chairman, Sir Kenneth Cork) Cmnd 8558 (1982) (Cork Report).
[63] Brenda Hannigan, *Company Law* (6th edn, OUP 2021) 311.
[64] s 10 Company Directors Disqualification Act 1986.
[65] Andrew Keay 'Wrongful trading: problems and proposals' (2014) 65 (1). 63 - 79 (17).
[66] Vaccari and Ghio (n 77).
[67] Richard Williams 'What Can We Expect to Gain from Reforming the Insolvent Trading Remedy?' (2015) MLR 78 (1) 55-84, 58.
[68] *Secretary of State for Trade and Industry v Taylor* [1997] 1 WLR 407, 414.
[69] s 213 Insolvency Act 1986, 214 Insolvency Act 1986, s 993 Companies Act 2006.
[70] Hannigan (n 79).
[71] Vaccari and Ghio (n 77) 242.

diligence that can be reasonably expected of a person carrying out the same functions as the director.[72] Secondly, the subjective element will examine the specific director themselves and what "general knowledge, skill and experience that the director has".[73] Thus, where a director has specialist knowledge, skill or experiences, he will be judged against those higher standards. This is a strict test and failure to satisfy either of these elements will lead to an unsuccessful wrongful trading claim as seen in *Jackson v Casey* [2019].[74] Here, the petition failed because the applicant could not prove the objective test.

When applying section 214, courts must identify the relevant time which the directors knew or ought to have known that the company was insolvent or impending insolvency. As this is also a subjective test, courts are cautious with taking a strict approach. Hannigan argues that this is because they do not wish to encourage directors to put their companies into administration or liquidation too soon out of fear they may be found liable for wrongful trading.[75] *Re Hawkes Hill Publishing Ltd* [2007] held that while directors ought to have known that the company was insolvent, this did not necessarily mean that the company could not avoid insolvent liquidation.[76] However, often directors do not act until it is too late and creditors have to bear the consequences of this.[77] This is evidenced in *Roberts v Frohlich* [2011].[78] The court found that the company's accounts showed the company was balance sheet and cash flow insolvent, however, the directors continued trading for another year despite this. Mr Justice Norris here provides "hope that "something might turn up" was on any objective view groundless and forlorn".[79] This was because "insolvent liquidation was all but inevitable".[80]

These cases shows that while courts are rightly cautious to embrace a strict approach, directors do not act until it is too late. Thus, overall, a stricter approach may be more beneficial to deter wrongful trading and protect the interest of creditors.

However, such stricter approach has not materialised yet in all areas (though a strict approach is taken in relation to the defence under section 214(3) discussed in chapter 3.4). During the Covid-19 pandemic, the UK government introduced a temporary relief measure for wrongful trading. The Corporate Insolvency and Governance Act 2020 provides that courts should assume the director's conduct was not the cause for the worsening of the company's or its creditors' financial circumstances.[81] Scholars have argued that introduction of this provision as a result of the Covid-19 pandemic was not necessary.[82] One argument made by Vaccari and Ghio is that due to the current economic and financial climate during the pandemic, it was difficult for applicants to establish whether the company had reasonable prospects of avoiding insolvency. As per "directors may not have been able to assess if their companies had a reasonable chance of avoiding insolvent liquidation or administration

[72] s 214(4)(a).
[73] s 214(4)(b).
[74] [2019] EWHC 1657 (Ch).
[75] Hannigan (n 79) 307.
[76] [2007] BCC 937.
[77] Hannigan (n 79) 307.
[78] [2011] 2 BCLC 625.
[79] ibid at [112].
[80] ibid.
[81] Corporate Insolvency and Governance Act 2020 (Coronavirus) (Suspension of Liability for Wrongful Trading and Extension of the Relevant Period) Regulations 2020.
[82] Vaccari and Ghio (n 77) 246.

because of the constantly changing governmental restrictions".[83] Nevertheless, this shows how the government is cautious when taking a strict approach as this may cause directors to put the company into insolvency proceedings when there may be a chance of saving it. They are mindful of the economic state especially during the pandemic when large numbers of businesses were shutting down as a result of global lockdowns.[84]

(4) Section 214(3) Defence

A defence to wrongful trading is offered by section 214(3) of the Insolvency Act 1986. Even when a director has been found guilty of wrongful trading, they may avoid liability to contribute to the company's assets if the court is satisfied that the director "took every step with a view to minimising the potential loss to the company's creditors" even if they knew or ought to know that the company was insolvent.[85]

The burden of proof lies on the director to demonstrate that they took every step to minimise loss to creditors. This was emphasised by *Brooks v Armstrong* [2015] which held that this is judged against what a reasonably diligent person with the knowledge of the director would do.[86] Here, the court provided some factors to consider which range from "keeping creditors informed and reaching agreements to deal with debt and supply where possible" to "obtaining professional advice (legal and financial)".[87] Thus, whilst section 214(3) does offer a defence, the burden of proof lies on the directors themselves.

Re Ralls Builders Ltd [2016] considered the scope of this defence.[88] While the directors tried to rely on section 214(3), their argument was not successful. Snowden J held that "if a director can show that he took 'every step ... as he ought to have taken' after the relevant time 'with a view' to minimising the potential loss to creditors, he avoids liability under s.214(1), even if he does not actually succeed in his objective".[89] However, he goes on to apply a strict approach; "s.214(3) is intended to be a high hurdle for directors to surmount … it is right to construe s.214(3) strictly and to require a director who wishes to take advantage of the defence offered by that subsection to demonstrate not only that continued trading was intended to reduce the net deficiency of the company, but also that it was designed appropriately so as to minimise the risk of loss to individual creditors".[90] Thus, the interests and positions of creditors as a whole rather than individuals must be examined. This strict approach ensures that directors do not take advantage and protects the interests of all creditors. Therefore, though a defence can be raised, this is strictly applied.

(5) Liability for Wrongful Trading; Contribution to the Company's Assets

For a successful claim of wrongful trading, the applicant must also show that the wrongful trading caused an increase to the company's debts. Knox J in *Re Produce Marketing Consortium Ltd (No 2)* [1989] provides that the appropriate amount for the director to contribute is the loss caused by the director as a result of their wrongful

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[83] ibid.
[84] 'The economic impact of Covid-19 lockdowns' Debate Pack 25 November 2022 Number CDP 2022-0215 By Philip Brien, Daniel Harari, Matthew Keep, Matthew Ward.
[85] s 214(3).
[86] [2015] EWHC 2289 (Ch).
[87] ibid at [259].
[88] [2016] BCC 293.
[89] ibid at [244].
[90] ibid at [245].

trading.[91] Thus, the amount as per Hannigan, is "primarily compensatory rather than penal to ensure that any depletion of the assets attributable to the period of wrongful trading is made good".[92] Furthermore, Vinelott J in *Re Purpoint Ltd* [1991] rejected a claim for a director, liable for wrongful trading, to pay all the company's creditors for debts incurred after he should have known that the company was impending insolvent liquidation.[93] French provides that "in effect, the jurisdiction under s 214 is primarily compensatory rather than penal".[94] As the amount for contribution is limited and less is at stake for directors; this may be inadequate in the prevention of wrongful trading.

Where there are multiple directors, they will be jointly liable to contribute to the company's assets unless one of them can rely on the section 214(3) defence.[95] This money goes to the company's general assets to be distributed amongst the company's creditors as per section 214(1) of the Insolvency Act 1986. Courts have discretion as to the order they can make so long as it goes to the company's assets.[96] However, orders cannot be made to specific creditors.[97] Vaccari and Ghio argue that since the contribution to the company's assets is not available for distribution to secured creditors except for the unsecured part of their claim, administrators and liquidators may be reluctant to commence expensive litigation procedures.[98] Thus, this may be a potential cause for the low number of claims.

(6) Conclusion

In conclusion, the regulation of wrongful trading under section 214 of the Insolvency Act 1986 could benefit from some reform. Whilst the government makes efforts to keep this provision up to date, as evidenced by the Covid-19 pandemic provisions which were somewhat unnecessary, the low number of proceedings suggests this is far from a perfect law. One criticism of section 214 is the lack of punishment for director misconduct. Unlike the criminal offence of fraudulent trading, wrongful trading is a purely civil offence and thus has no criminal sanctioning. Whilst directors may be ordered to contribute to the company's assets, this is limited to cases where a loss has resulted. Therefore, this is more compensatory rather than punitive. A better deterrence can be found in director disqualification which will be discussed in chapter five.

Nonetheless, section 214 has some merits which must not go unnoticed. The introduction of wrongful trading has been effective in the deterrence of improper trading as the standards of proof in fraudulent trading was perceived to be too high. Thus, where there is no fraud element, but the director has caused loss due to their continued trading when they knew the company was insolvent or impending insolvency, a claim can be brought under section 214. This allows creditors to receive some compensation for the amount of loss caused as a result of this trading. Furthermore, whilst there is a defence under section 214(3), this is strictly applied and places the burden of proof on the director to show they have taken every step possible to minimise loss.

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[91] [1989] BCLC 520.
[92] Hannigan (n 79) 311.
[93] [1991] BCLC 491.
[94] Derek French, *Mayson, French & Ryan on Company* Law (37th edn, OUP 2021), 724.
[95] Vaccari and Ghio (n 77) 245.
[96] ibid.
[97] ibid.
[98] ibid.

D. THE REGULATION AND SANCTIONING OF FRAUDULENT TRADING; THE CIVIL AND CRIMINAL OFFENCE

(1) Introduction

This chapter will discuss the two aspects of fraudulent trading: the civil and criminal offence. Section 213 of the Insolvency Act 1986 provides for the civil offence of wrongful trading. However, unlike wrongful trading, fraudulent trading, is also a criminal offence under section 993 of the Companies Act 2006. Liability under section 993 may result in up to ten years imprisonment and fines.

The main difference between wrongful and fraudulent trading is intent. In fraudulent trading, the appellant must prove that the directors carried out business with the intention of purposefully defrauding the company's creditors. Section 213 and section 993 both provide that fraudulent trading refers to "any business of the company has been carried on with intent to defraud creditors of the company or creditors of any other person, or for any fraudulent purpose". Likewise with wrongful trading, directors liable for fraudulent trading may be ordered to contribute to the company's assets and face disqualification. This chapter will consider whether the regulation and sanctioning of fraudulent trading under both section 213 and section 993 is effective to prevent directors (and others) from committing such offences.

(2) Dishonesty

Dishonesty is a key element in the offence of fraudulent trading.[99] Justice Laddie in *Bernasconi v Nicholas Bennett and Co* [2000] provides that "references to "intent to defraud", "for any fraudulent purpose" and "knowingly" all emphasise that the provision is only effective against those who have acted dishonestly".[100] Here, he referred to Maughham J's definition in *Re Patrick and Lyon Limited* [1933]; "the words "defraud " and "fraudulent purpose," where they appear in the section in question, are words which connote actual dishonesty".[101] Though dishonesty is not explicitly stated in the provisions, intention to defraud and common law implies that this is a key element which must be proved for a claim of fraudulent trading to suffice. Thus, raising the burden of proof on the applicant.

Furthermore, in *Pantiles Investments Ltd v Winckler* [2019], the court accepted that knowledge requires dishonesty.[102] Judge Mullen here refers to the test from *Ivey v Genting Casinos (UK) Ltd* [2017].[103] For the criminal offence of fraudulent trading, both the subjective and objective standard must be proven. Firstly, the defendant's state of mind will be considered with regards to their knowledge and belief. This does not concern whether it was reasonable but if it was honestly held. Secondly, the court must consider whether the defendant's conduct was honest by the objective standard of an ordinary person. However, as per *Welham v DPP* [1961], this test has proven problematic as actual dishonesty must be provided.[104] The high burden of proof in establishing dishonesty and intent to defraud has led to a lack of claims which will be discussed in chapter 4.3.

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[99] Lucy Jones, *Introduction to Business Law* (5th edn, OUP 2019) 526.
[100] [2000] BCC 921 [13].
[101] [1933] Ch 786, 790.
[102] [2019] EWHC 1298 (Ch).
[103] [2017] UKSC 67.
[104] [1961] AC 103.

(3) Intent to Defraud

Trading with an insolvent company is not in itself sufficient for a claim of fraudulent trading, there must be an "intent to defraud". Fraudulent trading occurs when the business continues with an intention of defrauding the company's creditors or for some other fraudulent purpose. This is the main difference between the fraudulent and wrongful trading. However, "intent to defraud" has proven controversial by case law and academics due to its interpretation. Keay criticised that what is necessary to prove the directors had intention is problematic.[105] He directs this at how "intent to defraud" has never been statutorily defined which has led to inconsistency in the application and interpretation of the test.[106]

The interpretation of "intent to defraud" was firstly considered by Maugham J in *Re William C. Leitch Brothers Ltd* [1932], at the time, in relation to s 275 of the Companies Act 1929.[107] Nonetheless, its interpretation is still relevant for fraudulent trading in relation to its legislative successors. Maugham J here highlighted the difficulty of interpreting "intent to defraud" and sets out a test based on whether the director incurred debts when they knew there was no reasonable chance for the company to pay back its creditors. However, this was later narrowed in *Re Patrick and Lyon Ltd* [1933], again by Maugham J stating that intent to defraud is concerned with actual dishonesty involving real moral blame.[108] Nonetheless, both definitions of "intent to defraud" are vague and has caused further uncertainty. As per Williams, Maugham J's attempt to define "intent to defraud" has caused more difficulty in its interpretation.[109] Similarly, Keay also provides that these two definitions have "been suggested on occasions, inconsistent". [110]

Whether the intent to defraud is present is dependent on the specific case itself.[111] This is for the court to decide based on the person's actions and conduct.[112] In *Re Augustus Barnett and Son Ltd* [1986], a subsidiary supported by its parent company continued trading even whilst making a loss.[113] The parent company continuously issued statements that it would support the subsidiary, some in letters known as 'comfort letters' published in the subsidiary's annual accounts. This continued for three consecutive years before the parent stopped its support and the subsidiary went into liquidation. Here, no fraudulent trading was found. Lord Hoffman J held that based on the facts of the case, the parent company had not intended to defraud the subsidiary's creditors. At the time the statements were made, the parent had an honest intention to support the subsidiary. Even though the parent company eventually stopped its support, this does not mean that its original statements were fraudulent. This case demonstrates the difficulties in establishing fraud which may potentially deter claims from being made.

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[105] Andrew Keay 'Fraudulent Trading: The Intent to Defraud Element' (2006) CLWR 35 (2), 122.
[106] ibid at 122.
[107] [1932] 2 Ch 71.
[108] [1933] Ch 786, 790.
[109] R.C Williams, 'Fraudulent Trading' (1986) 4 C&SLJ 14, 26.
[110] ibid (n Keay) 125.
[111] Lee Roach, *Card & James' Business Law* (4th edn, OUP 2016), 642.
[112] Derek French, *Mayson, French & Ryan on Company* Law (37th edn, OUP 2021), 718.
[113] [1986] BCLC 170.

The Company Law Committee report of 1962 considered the effects of the fraudulent trading provisions.[114] The Jenkins Committee criticised its inadequacy in dealing with the offence of fraudulent trading along with other directorial incompetence.[115] However, the report directed this criticism at the Board of Trade for its failure in bringing the cases to court, not the courts or legal draughtsman. Beekman and Ross suggest that the uncertainty of the standard of proof may have potentially contributed to this.[116] Even though the law has settled the issue of standard of proof, inconsistencies in its application has led to some uncertainty.[117] Both the Jenkin Committee and the Cork Committee have recognised the difficulties in its interpretation, however neither did much to resolve this issue. Thus, reform may be necessary to ensure certainty, as this will encourage claims to hold directors (and others) liable for fraudulent trading.

(4) The Civil Offence vs The Criminal Offence

Lord Steyn in *R v Hinks* [2001] provides that the purposes of civil law and the criminal law are in ways different.[118] Whilst the civil and criminal offence of fraudulent trading share many of the same characteristics, there are some distinct differences between the two. Fraudulent trading carries more serious sanctioning than wrongful trading due to criminal liability. As per section 993 “every person who is knowingly a party to the carrying on of the business in that manner commits an offence”.[119] If found guilty, directors may face up to ten years imprisonment, thus, section 993 is a more effective deterrence than section 213. Furthermore, the criminal prosecution can be initiated even if the company is not yet insolvent.[120] This allows pre-emptive action to be brought against the director before the company is at an unsavable state preventing the company from entering insolvency.

Nonetheless, section 993 and section 213 share many of the same characteristics and conditions. The element of intention to defraud is present in both the civil and criminal offence, and similarly dishonesty. However, section 993 carries a higher standard of proof “beyond reasonable doubt”. As a criminal law regulation, the claimant must prove beyond reasonable doubt that the defendant had the intention to defraud or act fraudulently. Nevertheless, there are not many differences between section 213 and section 993. This is highlighted by Keay who provides that there are not many apparent differences other than the procedural and burden of proof requirements.[121]

As per Hannigan, the civil offence of fraudulent trading is “less important now in the light of the provisions on wrongful trading in IA 1986, ss 214 and 246ZB”.[122] He based this on how the burden of proof in fraudulent trading is much higher than the civil offence of wrongful trading and provides that liquidators or administrators are more likely to consider the civil offences as there is no need to establish intent to defraud.[123]

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[114] Board of Trade, Report of the Company Law Committee (Cmnd 6659, 1962).
[115] ibid, 193.
[116] M. Beekman and S. Ross, ‘Fraudulent or Wrongful Trading’ (1991) 141 NLJ 1744.
[117] ibid.
[118] [2001] 2 AC 241.
[119] Companies Act 2006.
[120] Eugenio Vaccari and Emilie Ghio, *English Corporate Insolvency Law: A Primer* (1st edn, EE), 239.
[121] Andrew Keay, *Company Directors’ Responsibilities to Creditors* (1st edn, Routledge 2007), 39.
[122] Brenda Hannigan, *Company Law* (6th edn, OUP 2021) 303.
[123] ibid.

Nevertheless, fraudulent trading is still relevant as this can be used against a wider category of respondents whereas wrongful trading is only applicable to directors. A policy argument was made in *Bank of India v Christopher Morris & 6 Ors* [2005] that as the purpose of section 213 is to compensate those who have suffered loss because of fraudulent trading, it would defeat the purpose of this if liability was limited only to directors.[124] As per, it "would in practice defeat the effectiveness of the section if liability were limited to those cases in which the board of directors was actually a direct privy to the fraud of the company with whom the transactions were entered into".[125]

(5) Liability for Fraudulent Trading; Contribution to the Company's Assets

Likewise with wrongful trading, the same principles apply that directors could be made to make up for the loss that incurred while fraudulently trading. A liquidator or administrator can apply to the court for an order for the directors to contribute to the company's assets if liability has been found for either the civil or the criminal offence. As per section 213(2) of the Insolvency Act 1986 "the court … may declare that any persons who were knowingly parties to the carrying on of the business in the manner above-mentioned are to be liable to make such contributions (if any) to the company's assets as the court thinks proper". This is not only applicable to directors but also to any persons involved in the fraudulent activity. The funds from these orders will be shared amongst the company's creditors to compensate for the loss caused by the fraudulent trading.

However, similarly with wrongful trading, the aim of this is to compensate creditors for loss suffered due to the fraudulent trading rather than punish the guilty parties who conducted the offence. Courts do not have discretion to induce a punitive element to the orders.[126] As the aim is to compensate, this order can only be made where the fraudulent trading has caused a loss to the company or a 3rd party (likely creditor). *Instant Access Properties Ltd (in liq) v Rosser* [2018] held that even though the defendant fabricated false documents, they were not necessarily liable to contribute to the company unless a petitioner could prove that this fraudulent trading caused a loss for the company or another party.[127] Here, Morgan J entirely dismissed the claim for fraudulent trading (along with the breach of fiduciary duty claim) despite the defendant's misconduct as no dishonesty was found.

Whether the court order to contribute to the company's assets is sufficient to deter directors and others from committing fraudulent trading is questionable. Under this provision, there is potential for the guilty party to avoid liability and punishment. Where section 993 applies, the guilty party may face criminal liability and imprisonment as a consequence of their actions. Furthermore, directors liable under section 213 may face disqualification.[128] However, where the guilty party liable under section 213 is not a director, the consequences they face are limited. They remain unaffected by director disqualification (though nonetheless may be disqualified from their role within the company) and where no loss has occurred, the court cannot make an order for the contribution of company assets. Though an argument could be made that there is no victim where no loss has occurred, this should not excuse the misconduct of the guilty party. By allowing these individuals to avoid repercussions sets a potentially

[124] [2005] EWCA Civ 693.
[125] ibid [112].
[126] Vaccari and Ghio (n 136) 241.
[127] [2018] EWHC 756 (Ch).
[128] s 10 Company Directors Disqualification Act 1986.

dangerous precedent; of validating their misconduct and insubordination. Therefore, due to its limits, this may be insufficient to deter fraudulent trading.

(6) Conclusion

Overall, findings of liability for fraudulent trading have reduced since the introduction of wrongful trading. As the burden of proof in claims for fraudulent trading is high, this deters claims from being made and makes it more difficult to have a successful claim. The issue of fraudulent trading concerns its interpretation. Whilst not explicitly stated under section 213 nor section 993, dishonesty must be present and proven using the Ivey test.[129] There are also various issues concerning the phrase "intent to defraud" which has been subject to much interpretation by both courts and academics. Nonetheless, it remains that there is no official definition of this.

Unlike wrongful trading, liability for fraudulent trading holds the risk of criminal sanctioning. Those found guilty of fraudulent trading may face up to ten years imprisonment along with potentially additional fines, thus more is at stake for directors if found liable. Another consequence is the court may order the guilty director to contribute to the company's assets where their fraudulent trading has caused a loss. This also aims to compensate losses for the company and its creditors rather than punish the guilty director themselves like wrongful trading. however, where their trading is fraudulent, but they have not caused any losses to the company or any other third party, this order cannot be made and is thus limited. Therefore, whether this order is effective in the prevention of fraudulent trading is questionable. Though a director found guilty of fraudulent trading under section 993 may face criminal sanctioning, the civil offence under section 213 does not offer much to punish the director for their misconduct.

E. DIRECTOR DISQUALIFICATION; SUFFICIENT TO DETER?

(1) Introduction

Directors found guilty of wrongful or fraudulent trading may face disqualification for up to 15 years under the Company Directors Disqualification Act 1986 (CDDA 1986). Director disqualification proceedings are usually brought when the company is placed into insolvency proceedings.[130] When a company becomes insolvent or where there has been a complaint against a director, the company or the directors themselves will be investigated by the Insolvency Service. If the Service deems that a director has not followed their legal responsibility, they may face disqualification.[131] The Service will first inform the director in writing of their misconduct which deems them unfit and the intention to start the disqualification process.[132] In response, the director may wait for the Service to take them to court for a disqualification order or give a disqualification undertaking (though this is not available in wrongful and fraudulent trading).[133] Once

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[129] *Ivey v Genting Casinos (UK)* Ltd [2017] UKSC 67.

[130] Gareth Allen, 'Investigating company director misconduct' (*Insolvency Service Blog*, 2 October 2019) <https://insolvencyservice.blog.gov.uk/2019/10/02/investigating-company-director-misconduct/> accessed 9 March 2023.

[131] ibid.

[132] Gov.uk, 'Company director disqualification' (*GOV.UK*) <https://www.gov.uk/company-director-disqualification> accessed 9 March 2023.

[133] ibid.

disqualified, one will no longer be permitted to act as a director of a company registered in the UK or overseas companies with connections to the UK.[134]

Disqualification for participating in wrongful trading or the civil offence of fraudulent trading is covered by section 10 of the CDDA 1986. This provides that where a person liable under section 214 or section 213 of the Insolvency Act 1986 has been ordered to make a contribution to the company's assets, the court may if it deems fit, also make a disqualification order against them. Furthermore, disqualification for fraudulent trading under section 993 of the Companies Act 2006 is regulated by section 4 of the CDDA 1986. However, disqualification may also be ordered for a variety of other reasons, most commonly unfitness.[135] Therefore, even where the director is not liable for wrongful or fraudulent trading, they may still face disqualification if their conduct deems them unfit.[136] This aims to protect the public interest from limited liability abuse and unfit directors.[137] Whilst the primary purpose of disqualification is not to punish directors for misconduct, this does raise the standards of directors' practice and thus is an effective method in the deterrence of wrongful and fraudulent trading.[138]

(2) Effect of Disqualification

As per section 1(1)(a) of the CDDA 1986, one "shall not be a director of a company, act as receiver of a company's property or in any way, whether directly or indirectly, be concerned or take part in the promotion, formation or management of a company unless (in each case) he has the leave of the court". Section 1(1)(b) also provides that disqualified directors will not be permitted to act as insolvency practitioners. Furthermore, there are additional restrictions placed on disqualified directors.[139] If the disqualified director operated in a particular profession, for instance as an accountant or a solicitor, then their respective professional body may prevent them from operating during the disqualification period.[140] This limits the roles and job opportunities which a person can have within the company and thus deters directors from acting *ultra vires.*

Once the disqualification order is in effect, the disqualified director's details will be published on the Companies House database of disqualified directors[141] and the Insolvency Service's register of disqualified directors.[142] All of this information is public allowing anyone to search through these databases. This can be embarrassing and damaging to one's reputation and thus, deter directors from misconduct.

Section 10 of the CDDA 1986 provides for director disqualification for liability under section 213 or 214 of the Insolvency Act 1986. This is considered in *Secretary of State for Trade and Industry v Gill* [2004], which concerned two furniture companies that continued trading in an attempt to save the business even though it was in severe financial difficulties.[143] *Uno* accepted deposits from customers for orders which could later not be fulfilled. Though advised to, directors did not safeguard deposits by placing it into a trust account for the customers, and instead used this money to keep the business running. When the company eventually went into liquidation, an application

[134] s 1(1)(a) CDDA 1986.
[135] Eugenio Vaccari and Emilie Ghio, *English Corporate Insolvency Law: A Primer* (1st edn, EE), 270.
[136] ibid.
[137] ibid at 269.
[138] ibid.
[139] Gov.uk (n 148).
[140] ibid.
[141] https://www.gov.uk/search-the-register-of-disqualified-company-directors.
[142] https://www.insolvencydirect.bis.gov.uk/IESdatabase/viewdirectorsummary-new.asp.
[143] [2004] EWHC 933 (Ch).

was made for a directors' disqualification order. However, this was dismissed because the behaviour was realistic and reasonable as an attempt to save the business. Thus, whilst directors may face disqualification for wrongful or fraudulent trading, this can be avoided so long as the director's conduct was a reasonable attempt to save the business.

(3) Protection of the Public

The CDDA 1986 was introduced with the aim to protect the public interest from directors who may otherwise take advantage of the benefits of limited liability.[144] This ensures that directors give regard to all factors and do not prejudice stakeholders as well as the public. Most commonly, directors are not disqualified for criminal activity but for unfit conduct.[145] Director disqualification aims to protect the public rather than punish the guilty director.[146] Thus, questions arise of whether director qualification is sufficient to deter directors from committing such offence of wrongful or fraudulent trading. Scholars such as Williams critiques director disqualification as an ineffective form of regulation.[147] However, whilst its main aim is for the protection of the public, this does not diminish its effectiveness in deterring director misconduct in relation to wrongful and fraudulent trading.

In *Re Lo-Line Electric Motors Ltd* [1988], the director continued trading when he knew the companies were insolvent using unpaid Crown debts.[148] For this, the period of disqualification ordered was only three years because the respondent was not consciously dishonest. When considering what misconduct amount to disqualification, Sir Nicolas Browne-Wilkinson VC provides that "ordinary commercial misjudgment is in itself not sufficient to justify disqualification … the conduct complained of must display a lack of commercial probity".[149] Here, the court held that the primary purpose of disqualification was to protect the public from directors whose past records present them to be dangers to creditors. Hicks criticised that rather than considering the past, courts should examine evidence and likelihood of the director becoming a future danger to the public.[150] However, this will place a greater burden on courts and new issues will arise regarding the test for this. Nevertheless, as explained by Sir Nicolas Browne-Wilkinson VC, the "the power is not fundamentally penal".[151] The same principle is applied by Lord Woolf MR in *Re Westmid Packing Services Ltd (No 3), Secretary of State v Griffiths* [1998].[152] However, whilst its primary purpose is to protect the public from unfit directors, this does not reduce its effectiveness as a deterrence for director misconduct in relation to wrongful and fraudulent trading as this promotes better director practice.

(4) Conclusion

[144] *Re Lo-Line Electric Motors Ltd* [1988] Ch 477.
[145] Vaccari and Ghio (n 151) 270.
[146] *Re Lo-Line Electric Motors Ltd* [1988] Ch 477.
[147] Richard Williams, 'Disqualifying Directors: A Remedy Worse than the Disease?' (2007) JCLS 213.
[148] [1988] Ch 477.
[149] ibid at 486.
[150] Andrew Hicks, 'Director Disqualification: Can it Deliver?' (2001) JBL 433, 447.
[151] ibid at 486.
[152] [1998] BCC 836, 843.

Thus, director disqualification is an adequate deterrence for director misconduct in relation to wrongful and fraudulent trading. Though its main aim is to protect the public rather than punish the directors themselves, disqualification does effectively raise the standards of director practice. Whilst disqualification is ordered more commonly for unfit conduct rather than malpractice in relation to trading, this ensures operating directors are competent. Moreover, the lengthy period of disqualification of up to fifteen years is sufficient to deter as this is limiting on one's career options and growths. Furthermore, disqualified directors are published online for anyone to see, the negative publication can have detrimental effects on one's reputation. Therefore, by encouraging high standards of practice and placing restrictions on disqualified directors, this ensures they do not act ultra vires and commit offence such as wrongful and fraudulent trading.

F. CONCLUDING CHAPTER

Although directors do have fiduciary duties imposed on them to prevent misconduct, the doctrine of limited liability has caused issues.[153] The company operating as a separate legal entity entitles them to their own legal personality, property, and debts.[154] Therefore, when the company faces insolvency, the assets of its members and directors are protected. This however is more burdensome on the company's creditors who may suffer loss as a result. Thus, regulation on wrongful and fraudulent trading ensures that directors who continue trading when they knew or ought to have known that the company was in financial difficulties are held accountable preventing the abuse of limited liability.

Under the provisions on wrongful trading, liable directors may be ordered to contribute to the company's assets for the loss caused as a result of such trading. This more compensatory rather than penal approach may fail to dissuade directors from engaging in these activities. The liable directors may also face disqualification which is a much more effective deterrence as this is more consequential for the directors themselves. However, other than this, there is little punitive measures. Furthermore, courts are cautious when taking a strict approach as they do not wish for directors to place companies into insolvency procedures too soon where there is a possibility the business could be saved.[155] Thus, wrongful trading is rather underused, and the low number of claims suggests some reform may be beneficial to encourage more proceedings.

Fraudulent trading has a higher standard of proof than wrongful trading. This is potentially the reason for the low number of proceedings under this section.[156] However, unlike the civil offence of wrongful trading, fraudulent trading is also a criminal offence under section 993 of the Company Act 2006. As guilty directors may face up to ten years imprisonment, more is at stake, and this is therefore a better deterrence than the civil offences. Moreover, liability for fraudulent trading may also result in a court order for the contribution of the company's assets. However, unlike wrongful trading, this is not limited to directors but applies to all parties involved in the loss caused by the fraudulent trading.

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[153] Hans Hirt, 'The Wrongful Trading Remedy in UK Law: Classification, Application and Practical Significance" (2004) 1 ECFR 71.
[154] Geoffrey Morse and Thomas Braithwaite, *Partnership and LLP Law* (9th edn, OUP 2020), 318.
[155] Brenda Hannigan, *Company Law* (6th edn, OUP 2021), 307.
[156] A Herzberg 'Why Are There So Few Insolvent Trading Cases?' (1998) 6 ILJ 77.

Furthermore, directors found liable for wrongful or fraudulent trading may face disqualification for up to 15 years. Disqualification is arguably an equally or even more compelling remedy than personal liability, as directors would lose career and job opportunities. Thus, this paper found that disqualification is an adequate deterrence for director misconduct in relation to wrongful and fraudulent trading.

Overall, this dissertation proves that while the regulation and sanctioning of wrongful and fraudulent trading has its merits, the low number of claims suggest that some reform may be beneficial to make better use of the provisions. The high burden of proof (in fraudulent trading) and strict application of the tests to establish wrongful and fraudulent trading may be a cause of this. Furthermore, there are some flaws in the system such as ambiguity of “intent to defraud” in fraudulent trading where further clarification by the courts may be necessary. Finally, the lack of punitive measures for director misconduct is potentially why some liquidators and administrators are reluctant to bring claims. Therefore, due to the aforementioned reasons in this paper, the current systems are underused and may benefit from reform.