

Directors Beware Do You Know The Risks Surrounding Your Personal Liability?

Background

In the case of *Contex Drouzhba Ltd v Wiseman* [2007] the English Court of Appeal held that a director who signed an agreement on behalf of a company which contained an implied representation that the company would be able to pay in accordance with the terms of the agreement was personally liable for deceit, as he knew that the representation was false.

Facts

Mr Wiseman ("W") was the director responsible for the operations of Scott Daniel Limited ("SDL"). W signed on behalf of SDL a framework agreement with Contex Drouzhba Ltd ("CDL") which contained a clause requiring payment by SDL 30 days after shipping of the goods supplied by CDL. At the time of signing the agreement, W knew that SDL could not meet the obligations under the agreement as SDL was insolvent. CDL sued W in deceit. At first instance, the trial judge found that W was liable in damages for deceit on the basis that on signing the agreement, W had impliedly represented that SDL had the capacity to meet its obligations to pay for the goods supplied and that this representation was made fraudulently by W. W appealed the trial judge's decision.

Decision

The English Court of Appeal dismissed the appeal holding, inter alia, that where a director is effectively the "mind of the company" and where the document he signs makes a fraudulent misrepresentation to his knowledge then, even if the company would be liable for the deceit carried out by its director, the director has a personal liability for his own fraud. Where fraud is committed by a director, his status as director of the company can not be used as a shield from the liability for his own fraud.

The Implications for a Company Director

In light of this case, directors should ensure that all representations, expressed or implied, in an agreement are accurate before signing any document on behalf of the company to avoid personal liability. The judgment is not limited to representations in relation to a company's ability to pay but has implications for any representation made in a document, for instance, the quality of the goods supplied or the ability to deliver the goods on time.

Although the English Court of Appeal emphasised the fraudulent nature of W's conduct, the principle of personal liability could be extended to a negligent misrepresentation. Directors should consider including a disclaimer of personal liability in any document signed on behalf of the company. Although such a disclaimer will have no effect where a misrepresentation has been made fraudulently, it may protect a director against the risk of an action for negligent misrepresentation.

A Victory for Creditors

The judgment represents a more favourable alternative to wrongful trading and fraudulent trading actions under the Insolvency (Northern Ireland) Order 1989.

If a liquidator is satisfied that there is sufficient evidence to bring a fraudulent trading or wrongful trading action, he will make an application to Court to declare that the director or past director of the company make a contribution to the company's assets. Fraudulent trading and wrongful trading actions are rare as they are brought by the liquidator as opposed to the creditor aggrieved by the wrongful or fraudulent trading. The more insolvent the company is, the less money the liquidator has available to commence such proceedings.

In addition, any recovery made by the liquidator pursuant to a fraudulent trading or wrongful trading action is paid into the general pool of assets which are available for distribution amongst all creditors.

By contrast the right for a supplier to sue a director personally for deceit can be utilised for the benefit of the individual creditor to whom the representation was made with no obligation to share any judgment made on foot of that action.

If a supplier believes a company buying its goods or services is in financial difficulty, it may consider asking the director ordering the goods on behalf of the company to write a letter confirming the ability of the company to pay for whatever has been ordered. If such a representation proves false, the supplier may claim against the director personally for deceit based on the case of *Contex Drouzhba Ltd v Wiseman*.

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