now. However, unless something happens to reverse the European process, a true single market will eventually emerge.

I believe that the sooner we have a single market for financial services, the better. Europe's insurance companies need the wider opportunities that the single market will bring in order to match the resources that our global competitors enjoy. If we fail to meet the challenge, we may wake up one morning to find that the leaders of the European insurance industry are indeed talking in a common language - [pause] Japanese. Thank you.

WRONGFUL TRADING - NO LONGER JUST A CONCEPT
by N.H. Stanbury, F.C.A., Director, Directors and Officers Ltd.

Prior to the passing of the Companies Act 1985 and the Insolvency Act 1985, a director's primary duty was only to his company, as was well-established in common law and confirmed in *Multinational Gas Petrochemical Co. - v -Multinational Gas & Petrochemical Services Ltd. and Others* [1983] Ch. 258. However, S.309, Companies Act 1985 extended the duty to consider the interests of employees and S.15 Insolvency Act 1985 required the director to minimise the potential loss to his company's creditors by refraining from "wrongful trading".

The wrongful trading provisions are now contained in S.214, Insolvency Act 1986 and permit the liquidator of an insolvent company to seek (on behalf of the creditors) a personal contribution from any director who".... knew or ought to have concluded that there was no reasonable prospect that the company would avoid going into insolvent liquidation ...."and who failed to take".... every step with a view to minimising the potential loss to the company's creditors as .... he ought to have taken ...." having regard to ".... the general knowledge, skill and experience ...."that he had or should reasonably be expected to have had. It should be noted that: (a) any director, including a shadow director (who may be e.g. a parent company) who participated in the alleged wrongful trading is vulnerable, even if this occurred several years before the liquidation (provided that it was after 28th April 1986); (b) the contribution sought is towards the deficiency of assets in the liquidation and the amount (if any) declared by the court as the liability of each individual director is a matter for the court's discretion.

The wrongful trading provisions should be distinguished from those that can be applied (under S.213) if fraudulent trading has occurred, although the sanctions and procedures are very similar. Fraudulent trading has always been recognised by the

Companies Acts as an activity which justifies the "piercing of the corporate veil" and the pursuit of those directors responsible.

The director who now, by his action or inaction, allows his company to trade wrongfully will risk potentially unlimited personal financial liability, even though he may have acted at all times honestly and (in his own view) to the best of his knowledge, skill and experience. The subjective and objective tests imposed, with the benefit of a large measure of hindsight, may well find his conduct below the required standard. In addition to the sanction of personal contribution, the director liable for wrongful trading may be disqualified from being, *inter alia*, a director or manager of a company for up to 15 years under S.10, Company Directors Disqualification Act 1986.

Until recently, the personal liabilities arising out of wrongful trading have been considered by many to be preventive rather than curative. It is true that several directors have been disqualified as a result of their involvement with an insolvent company (e.g. on the application of the Secretary of State under S.6, CDDA 1986) but no effective actions have been brought under S.214 leading to contribution with or without disqualification. There are probably three interlinked reasons for this:
(a) liquidators have limited funds at their disposal and cannot afford to pursue directors willy nilly, especially if (b) the directors have little or no personal assets worth pursuing, or (c) a compromise settlement can be made without resorting to the legislative sanctions. The liquidator is primarily interested in recovery for the benefit of the creditors, not in seeing the directors punished, either financially or by the restrictions of disqualification.

However, a recent case has shown the Insolvency Act's teeth to be capable of biting and should demonstrate that a director cannot rely on the complacency or impotency of the liquidator. In *Re Product Marketing Consortium Ltd. (in liquidation)* [The Times, 7.4.89], two directors of that company were declared liable to contribute a total of £75,000 (plus interest and costs) towards the Company's deficiency of assets on the grounds that they had indulged in wrongful trading, contrary to S.214, and that the contribution declared was the amount by which the company's assets could be discerned to have been depleted by their conduct. The liquidator in fact sought a contribution of £107,946 from *each* director but Knox J., having regard to all the circumstances and, in particular, the absence of fraudulent intent, considered that the total contribution should be restricted to the £75,000.

The case is also noteworthy in that a preliminary issue arising from the directors' defence had to be considered before the S.214 action could proceed from the

liquidator's originating summons. The directors had claimed that they should not be pursued under S.214 because ".... having acted honestly and reasonably, and having regard to all the circumstances of the case, they ought fairly to be excused from such breach of duty and be relieved from such liability pursuant to Section 727 of the Companies Act 1985." The latter section is one means, rarely usable in practice, whereby a director can be relieved from (or indemnified against) personal liability for his wrongful acts as a director because it would be unduly harsh for him to bear the full burden personally when his culpability can be shown to be diminished by the surrounding circumstances, e.g. where he is perhaps singled out as a culprit or a scapegoat. Knox J. was not persuaded by this defence (which was ordered to be struck out) on the basis that S. 727 was a subjective test with no application to those provisions of S. 214 which called for objective tests to be applied - tests which the subsequent action showed the directors not to have met.

The *Produce Marketing Consortium* case is a landmark in demonstrating the liability of the present-day director. It will no doubt be followed by many other S. 214 (and S.213) actions which have been quietly gestating since the 1985 legislation became effective. A director can no longer shrug his shoulders and leave the creditors entirely to their paltry shareout of the company's depleted assets if he has been involved in wrongful trading. Naturally, the company's insolvency will *ipso facto* deny him any company indemnity against the contribution he may be required to make - not that he would normally be able to enforce such an indemnity as any *prearranged* agreement to provide it would be void under S. 310, Companies Act 1985. The only ray of hope for the director in these circumstances will be if he is covered by directors' and officers' liability insurance, on either an individual basis or on the common 'board basis' for himself and his colleagues.

Wrongful trading contributions are damages within the indemnity contemplated by the conventional D&O policy and the costs of defending the action (and any brought in respect of disqualification) should also be met. The usual fraud exclusion will of course operate to deny indemnity if any element of fraud is proven - it is quite possible for action under S.214 to develop into one under S.213 as the true facts emerge, thus leaving the director on his own. In any event, care must be taken that the policy's limit of indemnity is adequate - large deficiencies may be involved, regardless of the number of potential 'target' directors expected to share in the contribution.

The view has been expressed that, where the insolvency originated from a wrongful act excluded from indemnity under the D&O policy (e.g. a breach of professional duty or property damage), any resultant wrongful trading action would itself be excluded. The writer does not agree with this view, for a good and fundamental reason

hinging on the doctrine of proximate cause. The proximate cause of the *insolvency* may well be an act of a director which is specifically excluded from indemnity, but mere insolvency is not *per se* a "loss" nor does it lead inevitably to wrongful trading, let alone the requirement to contribute to the deficiency which becomes the director's indemnifiable loss. The point is that there is a second and distinct wrongful act at the time when wrongful trading occurs, quite separate from the original circumstances (howsoever arising) that set the scene for it by directly or indirectly causing or worsening the insolvency.

Those directors who have shunned D&O cover until now will, perhaps, agree with the general view of those who provide it that the peril of wrongful trading is in itself sufficient reason to effect cover. However, it seems likely that a few more personal losses will be needed before the message really sinks in.

Lunchtime Address – 21st March 1989 "Procedure Abused is Justice Denied: The Challenge to Liability Insurance" by Iain Goldrein, Barrister, London and Liverpool

About a year ago, I was invited by your esteemed Chairman, Gordon Cornish, to deliver this lecture. Even allowing for the telescoping of the time which is a concomitant of professional practice, it seemed a long way ahead. How quickly the time has flown. In that time the government through its agencies has had published the reports of the Marre Commission, the Civil Justice Review and the "Green Paper". Surely not since the nineteenth century has there been such vigour brought to bear for the purposes of speedy law reforms.

The difference between the approach of the present administration, and that of previous administrations, is by reference both to orientation and expedition. By way of contrast for example, the Evershed Committee sat for 6 years. It could be argued that it said in 100 words what could have been reduced to 3. Its culminating achievement was the Summons for Directions. It proposed that by this means, there could be the eliciting of admissions and the clear distillation and identification of issues. By 1968, however, the Winn Committee reported that the Summons for Directions had effectively become a dead-letter and suggested "Automatic Directions". That took another 15 years to fall within the ambit of the Rules of the Supreme