

# Directors' Duties... Something old, something new

Frances Coulson writes about Directors' Duties, Wrongful and "Misfeasant Trading" in *Re BHS Group Limited (in liquidation)*; *Wright v Chappell*



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**A director of a company in England & Wales facing insolvency or the likelihood of insolvency confronts the prospect of becoming the target of a number of causes of action if the company goes into a formal insolvency procedure.**

These include, but are not limited to, claims arising out of a breach of their duties as a director and actions for fraudulent or wrongful trading; and now, it seems, one for "misfeasant trading", a concept hitherto unknown to the law, but the possibility of which, until recently, lay buried in existing legislation.

## Duties

A director is bound by a number of duties which are codified in sections 171-177 of the Companies Act 2006 (supplemented by sections 178-172). Section 172 provides that a director has a duty to promote the success of the company for the benefit of its members as a whole (section 172(1)). Sub-section (3) provides that that duty 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.

What has become known as "the creditor duty" has a long history. It was the subject of recent consideration by the Supreme Court in *BTI 2014 LLC v Sequana SA* [2022] UKSC 25, and although the judgments delivered in that case indicated differences of view as to the precise nature of the duty,

leaving some aspects open to be considered in future cases, it left no doubt about the existence of the duty itself.

## Fraudulent trading

Section 213 of the Insolvency Act 1986 provides for liability if, in the course of a company's winding-up, it appears that the business of the company has been carried on with intent to defraud its creditors (fraudulent trading). The need to demonstrate knowledge and intent make for a high evidential burden, as a result of which use of the remedy is relatively uncommon. A single incidence of fraud is insufficient, the business must have been "carried on" with intent to defraud.

## Wrongful trading

Section 214 of the Insolvency Act 1986 provides a remedy for wrongful trading. This occurs where the directors of a company have continued to trade when they knew, or ought to have concluded, that there was no reasonable prospect that the company would avoid insolvent liquidation or insolvent administration. The burden of proving the elements of wrongful trading are not as high as those applicable to fraudulent trading, but they too can give rise to problems.

In some cases it is easy to establish the date by which the directors concerned should have known that there was no prospect of avoiding insolvency; but in other cases the factual background can give rise to considerable difficulties. The

result is often that the insolvency practitioner bringing the application will rely on a number of "knowledge dates" in the hope that one at least will stick, usually the earliest which is likely to result in the highest recovery for the benefit of creditors. The recent case of *Re BHS Group Ltd; Wright & Ors v Chappell & Ors* [2024] EWHC 1417 (Ch) and [2024] EWHC 2166 (Ch) highlights some of those difficulties and offers a way of working around them via a cause of action called "trading misfeasance" or "misfeasant trading".

The facts of the case were complex with Leech J's first (substantive) judgment running to 1,160 paragraphs, his supplementary judgment to a modest 87. A short summary will have to suffice.

In 2015, Retail Acquisitions Limited acquired - for £1- the entire issued share capital of British Home Stores Group Ltd (BHS), which ran a chain of ailing department stores. On the same date, Dominic Chappell and Lennart Henningson were appointed as directors of four companies in the group, followed later by Dominic Chandler. In April 2016, the board resolved to put the group into administration. Creditors' voluntary liquidation followed shortly thereafter.

The liquidators' primary allegation was one of wrongful trading under section 214 of the Insolvency Act 1986 in that, from the date of RAL's acquisition of BHS, the directors either knew or ought to have known that there was no reasonable prospect of avoiding insolvent liquidation or



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administration. They relied, among other things, on the group's history of making losses, lack of financial support of the kind that had been relied on before the acquisition and a general lack of working capital. They posited six possible "knowledge dates". Leech J accepted the last of the dates relied on, 8 September 2015, and held Mr Chandler and Mr Henningson liable to make a contribution of £6.5 million to the liquidators on a several basis. (The trial against Mr Chappell had been adjourned).

As a hedge against the difficulties attendant on a wrongful trading claim (Leech J referred in his judgment to the bar being a very high one after *Sequana*), the office-holders in *Chandler v Wright* relied, in addition to wrongful trading, on director misfeasance (breach of duty) in the form of what is referred to in the judgment as "trading misfeasance", on one view, a novel cause of action, on another, not, all the elements to making out the claim being rooted in existing law to be found primarily in the Companies Act 2006 and the Insolvency Act 1986.

The liquidators relied on section 212 of the Insolvency Act 1986 as the procedural gateway to their "misfeasant trading" claim, which rested on allegations

of breach of the directors' Companies Act duties (see above), a common approach taken by office-holders (it was also the route to the wrongful trading claim in this case). The provision does not itself give rise to any particular cause of action: it provides the basis on which an office-holder can rely on what are often non-Insolvency Act causes of action, in this case causes of action arising out of breach of the duties set out in the Companies Act.

Whilst Leech J considered all the duties set out in the Companies Act, the focus was very much on section 172, the duty to promote the success of the company (and the creditor duty arising from that). The liquidators relied on the same knowledge dates as for their wrongful trading claim, claiming that the creditor duty arose at those times too. This enabled the judge to fix on an earlier date than he felt able to for wrongful trading purposes. He held that the duty to consider the interests of creditors arose on 17 June 2015 and had been breached. Had the directors complied with those duties by 26 June 2015 (and/or 8 September 2015), the companies should have ceased trading and put into insolvent administration.

This, in turn, opened up the possibility of a substantially

greater recovery than that available for wrongful trading. Leech J held, in essence, that the breaches of duty made out by the liquidators (they did not succeed on every count) were the effective cause of the net deficiency in the company and entitled them to equitable compensation as against Mr Henningson and Mr Chappell of £110 million odd on a joint and several basis.

### Summary

The concept of trading misfeasance is novel and, to the extent that it was successful, does mean that the decision in *Wright v Chappell* may be described as "something new". But even if it is "something old," in as much as it rests on existing law, it still represents a novel use of that law, for which those advising the liquidators are to be congratulated.

Quite apart from that, the case is widely reported as being the largest award of its kind. "Misfeasant trading" will undoubtedly figure in future cases, if only, as in this case, as an alternative to a wrongful trading claim. It will also serve as a warning against directors engaging in what Leech J (borrowing from Lady Arden in *Sequana*) described as "insolvency-deepening activity". ■



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