INSOLVENCY BULLETIN

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EXTENDING THE REACH OF FRAUDULENT TRADING

The Court of Appeal's findings in *Tradition Financial Services Ltd v Bilta (UK) Ltd and Ors [2023] EWCA 112* will be of great interest to practitioners when deciding against whom they may issue proceedings for fraudulent trading under section 213 of the Insolvency Act 1986.

S213 provides that:

1) If in the course of the winding up of a company it appears that 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, the following has effect.

2) The court, on the application of the liquidator 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.

Liquidators brought claims for dishonest assistance and fraudulent trading against third parties believed to be involved in missing trader intra-community ("MTIC") fraud (more commonly known as Carousel Fraud).

MTIC fraud is often complex. Numerous companies may be involved in deal chains. In its simplest form it involves purchasing goods within the EU at a zero rate of VAT then selling on whilst charging VAT on the sale price and avoiding paying VAT by going "missing".

In this instance the fraud involved the trading of carbon credits with TFS acting as broker to other entities whom they knew were unlikely to be legitimate and in the knowledge that their purpose was to avoid payment of VAT.

The s213 claims brought against four other respondents were dismissed or compromised. TFS was therefore the only appellant and argued that the scope of s213 was restricted to persons exercising management or control over a company.

The Court of Appeal rejected TFS' argument and referred to "*the modern approach to statutory construction",* which was to "*have regard to the purpose of a particular provision".* The purpose of s213 was to provide compensation to those who had suffered loss as a result of fraudulent trading of a company`s business. S213 was not limited to directors and "veil piercing" (i.e. persons who are directly involved in managing a company but who are not officially directors) but also extended to "outsiders" involved in the fraudulent trading as well.

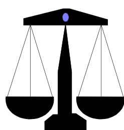
The Court of Appeal considered in great detail both case law and academic studies and could not find any authority that s213 was limited to only those directly involved in the running of a company. It held that s213 may therefore be interpreted more widely and so could extend to third party "outsiders" as well. The question as to whether such "outsiders" could be said to be involved in the carrying on of a fraudulent business would be dependent on the facts of each case.

A liquidator bringing a s213 fraudulent trading claim will still have to prove that the respondent had subjective knowledge of the fraudulent nature of the activity and that the conduct was dishonest *"according to the objective standards of ordinary decent people*" as decided in the *Re*: *JD Group Ltd [2022]* case.

Editor's Note

It has now been decided that liquidators have the power to bring s213 fraudulent trading claims against third party "outsiders", even where they were not directly involved in the management or control over the company in liquidation. Following on from last month's bulletin on s423 claims for transactions defrauding creditors, this judgment is yet a further example of the Courts' purposive approach to interpreting and widening the scope of the Insolvency Act 1986.

This is good news for office holders as the "reach" of their statutory claims has been significantly increased.



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