Julian Dobson SOLICITORS

Insolvency Lawyers

NEWSLETTER

It's all in the name

Re-use of company names – what directors should know.

Overview

Section 216 of the Insolvency Act 1986 restricts the re-use of company names following liquidation. It does this by preventing anyone who was a director of the company that went into liquidation from being a director of another company known by a prohibited name. A prohibited name is one by which the liquidated company was known at any time in the 12 months prior to liquidation, or a name which is so similar to a name by which the liquidated company was known as to suggest an association with that company.

The restriction applies to not only a director but also a shadow director of the liquidated company. In relation to the successor company that is known by a prohibited name, it prevents the director from being directly or indirectly concerned or taking part in the promotion, formation or management of such a company. It also prevents such a person from being directly or indirectly concerned or taking part in the carrying on of a business (otherwise than by a company) under a prohibited name. The restriction applies for a period of five years from the date on which the liquidated company went into liquidation.

The Exceptions

There are exceptions which can be used to allow a director to act in relation to a successor company known by a prohibited name. They are;

a) the business of the liquidated company is purchased from its liquidator and that either before or after liquidation has taken place notice is given to creditors and placed in the London Gazette.

b) an application is made to court for permission within seven days of liquidation.

c) the successor company has been known by the prohibited name for a period of at least 12 months prior to the company going to liquidation.

The Penalties

If a former director of the liquidated company acts in breach of section 216 it renders the director criminally liable to imprisonment and or a fine. Section 217 further states that the director shall be personally liable for all the relevant debts of the successor company if;

a) in contravention of section 216 he is involved in the management of the company, or

b) as a person involved in the management of the company, he acts on instructions given by a person whom he knows at that time to be in contravention in relation to the company of section 216.

Key Points

The provisions and the exceptions are technical in nature and must be strictly complied with. Set out below are some of the more important points that a director affected by these provisions should be aware of.

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1) **What is a prohibited name?**

The ban applies to use of the company name or a similar name and can include parts of the company name. It can also include a trading name or acronym by which the liquidated company was known. The fact that the names of the companies contain a common surname is irrelevant. The use of additional identifying words to the previous name will not prevent it being a prohibited name i.e., the addition of phrases such as southern, group or a year reference. Examples of prohibited names include;

Mike Spence Classic Cars Ltd was held to be similar to **Mike Spence (Reading) Ltd** and **Mike Spence (Motor Sport) Ltd**.

Classics Roofs Ltd was held to be similar to **Classic Conservatories & Windows Ltd**.

2) **What about other companies in the group with similar names?**

Following liquidation of the company the re-use of its name in whole or in part by other companies within the same group can result in directors being caught out by the provisions. Depending on how long the other group companies have been known by the prohibited name the exemption referred to above may apply. Care should be taken to ensure that if a breach does occur steps are taken to change the name of other group companies if required.

3) **When does a director become liable for a breach?**

The way in which the provisions of sections 216 and 217 are framed, a director automatically becomes liable both criminally and civilly on the conditions being satisfied. Once a director becomes liable, he cannot be excused of that liability by the court or its effects mitigated. Even if a director applies to court and obtains leave to act in relation to a company known by a prohibited name, that leave will not be retrospective or alleviate any criminal or civil liability that has accrued prior to the application being made unless the application is made within 7 business days of liquidation under the Second excepted case.

4) **A director is only liable if someone has been confused or misled?**

Wrong. Although the legislation was brought in to curtail the activities of directors involved in Phoenixing and in particular to protect the public from them, there is no requirement to establish that anyone has been misled by the similarity of the names of the two companies. (Ad Valorem Factors Limited v Ricketts [2003] EWCA Civ 1706)

5) **Personal liability for which debts?**

Section 217 provides that a director who is in breach of section 216 is personally liable for the "relevant debts" of a company. That is to say the successor company that is using the prohibited name and not the company in liquidation. In such circumstances the director is liable primarily and jointly and severally with the company. Again, liability is automatic, and the court has no power to grant relief from liability to a director (First Independent Factors and Finance Limited V Mountford [2008] EWHC 835 Ch). Whilst liability is not dependent upon the successor company going into liquidation, in the event of the successor company being liquidated then the director becomes an attractive target to its creditors.

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6) **It’s all about timing.**

   Once a director has acted in breach of s216 it cannot be undone even if it is intended to use one of the exceptions. It is therefore important that the successor company does not use the prohibited name until leave of the court is granted, save in the limited circumstances permitted under the Second Excepted case or the exception by giving notice to creditors has been fully implemented. To avoid this notice can be given before liquidation.

7) **What are the chances of anybody doing anything about it?**

   Directors may be tempted to take a chance perhaps believing that it is unlikely that anyone will know about their involvement in the liquidated company, the prohibited name and the successor company. Such a stance may also be bolstered by their belief that the successor company will not fail and therefore they would not be called upon to pay it’s “relevant debts”. The early decisions in this area of the law involved factoring companies who actively pursued directors in breach of sections 216 and 217 with significant success. More recently specialist companies have targeted directors in breach of these provisions. They will where the successor company goes into in liquidation purchase debts from its creditors. They then pursue those creditors’ claims against the directors personally using sections 216 and 217.

Conclusion

The pitfalls of sections 216 and 217 can be avoided with some advance planning.

Re-use of a company name or similar title should be considered at an early stage and preferably before liquidation takes place. Careful planning and use of the exceptions, if appropriate, can avoid directors falling into an irreversible trap.

Julian Dobson SOLICITORS

Insolvency Lawyers

Author: Julian Dobson

1 Frederick Terrace, Frederick Place, Brighton BN1 1AX
Tel 01273 766 355 Fax 01273 766 350 **Email: info@juliandobson.com Web: www.juliandobson.com**