



## **Directors' Liability in The Netherlands remains a difficult issue**

Unless otherwise prescribed, in matters relating to property rights, Dutch law treats legal entities and natural persons in the same manner. Legal entities have rights and obligations as well as their own, separate capital. Legal entities may enforce their rights in the same way as natural persons, and they must fulfil their duties. However, a legal entity cannot perform actual actions. Those actions ultimately require intervention from natural persons. The rules and regulations outline who is primarily tasked with acting on behalf of a legal entity, and who is authorised to represent a company.

Those authorised are called the board of the legal entity, and in principle each individual director. In addition, competent bodies within the legal entity, (such as shareholders or members) may appoint others to act and hold the power to bind on behalf of the legal entity. Such actions by a director can in turn give rise to personal liability, as it will be explained below.

### **The internal and external liability of Directors**

Internal liability arises from the relationship between the Director and the legal entity, and from the consequent duties of the Director. If the Director, through his actions damages the company, he may under certain circumstances, be liable for those damages.

External liability refers to the Director being liable, alongside with the legal entity, for any third party damages that arise from the actions of the Director.

### **Internal liability of Directors**

Dutch law stipulates that Directors must fulfil their duties towards the legal entity with due care and attention. The Supreme Court has ruled that liability is only incurred in case of serious blame and manifestly improper performance of duties. In establishing this, the type of activity of the legal entity and all other relevant circumstances must be taken into account.

Any action that is wrongful according to the statutes, laws and rules designed to protect the legal entity, is usually considered improper performance of duties.

The following is a non-exhaustive list of examples of such conduct.

- Diverting the legal entity's funds for instance for personal use.
- Mixing private business with the affairs of the legal entity, acting as a competitor of the legal entity, and in particular, subordinating the interest of the legal entity to their own private interest, or to the interest of a third party.
- Binding without authorisation, the legal entity in its relation to a third party.

- Taking unnecessarily large financial risks, or making decisions with far-reaching financial consequences without proper preparation, or entering into transactions that are significantly beyond the financial capability of the legal entity, for instance through irresponsible several liability undertakings.
- Failure to prevent or counteract undercapitalisation or neglecting credit control
- Failure to arrange for customary insurance coverage.

In case of improper performance of duties by a director, in principle all directors are jointly and severally liable.

### **External liability of Directors**

External liability entails that alongside the legal entity, the Director is also usually liable for any damages to third parties that arise due to the actions of that Director. There are two ways of holding Directors of legal entities personally liable for their actions with regards to third parties, who have come into or have established contact with the legal entity.

- Piercing the veil
- The Beklamel rule

Piercing the veil applies if the Director is misusing the legal entity, merely to avoid personal liability, thereby prejudicing the creditors, since the legal entity doesn't offer recourse, and since the services they deliver benefit the Director. In this case, Dutch law allows for piercing the corporate veil and equating the legal entity and the person acting on its behalf.

The Beklamel rule applies when the person acting on behalf of the legal entity, that is to say the Director, is deemed responsible for not fulfilling the obligations of the legal entity. This is considered a wrongful act committed by the person who is acting on behalf of the legal entity, the Director, which disqualifies him or her as a contracting party.

In certain cases, Dutch law provides for a presumption of liability. If the management has manifestly preformed its duties improperly, and this is likely to have been a major contributor to bankruptcy of the legal entity, each Director shall be liable to the estate for all debts incurred. Dutch law presumes that manifestly improper management is the case, if the accounting has not been kept up-to-date or if the annual accounts are not published in a timely manner.

### **Equation**

Especially where liability is concerned, equation is often called for. This entails an expansion of the identity of the debtor and/or the unit of the collateral, both being conditions for the collection of claims. Often, the Court is only prepared to allow direct redress between third parties in exceptional circumstances.

Parts of the assets of a third party could be realised as long as these are the actual property of the debtor himself.

Furthermore, it may be presumed that the (natural) person acting on behalf of the legal entity is the contracting party. Only in cases where the use of a legal entity leads to the abuse of the legal structure and to socially unacceptable consequences, is it reasonable and justifiable to ignore the legal entity in question. Directors, who purposely prejudice the redress of creditors of the legal entity, may be making themselves subject to personal liability.

In any event, refusal by a Director to fulfil an obligation of the legal entity, due to a reluctance to pay, is considered a wrongful action. According to the Supreme Court, if there is evidence of an unwillingness to pay, it is reasonable to request that whomever holds full control of the failing company clarify whether the company is unable to pay. Furthermore, the Director in question is obliged to clarify whether the legal entity is unwilling or unable to pay. He cannot claim to be unable to pay, if he does not make use of credit facilities available to the company. To do so, would be a wrongful act towards the creditor.

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